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WHO WILL STOP THE RAIN? REPAIRING THE HOLE IN THE D'OENCH, DUHME UMBRELLA BY PROTECTING THE FDIC AGAINST FRAUDULENT TRANSFEREE LIABILITY UNDER THE BANKRUPTCY CODE

I. INTRODUCTION

The banking industry is in trouble. For a multitude of reasons, record numbers of banks insured by the Federal Deposit Insurance Corporation (FDIC) continue to fail.¹ The failure of 200 FDIC-insured banks

1. In a study conducted by the Corporate Financial Audits, Accounting and Financial Management Division of the United States General Accounting Office, regulators found serious internal control weaknesses in the 184 banks that failed during 1987. Regulators discovered that banks often "lacked appropriate policies for loan underwriting and approval, had poor loan documentation and inadequate credit analysis, or established inadequate allowances for losses on loan portfolios." *Deposit Insurance: Hearings of the Financial Institutions Subcommittee of the House Banking Committee*, 101st Cong., 1st Sess. (Sept. 19, 1989) (LEXIS, NEXIS Library, Omni File) [hereinafter *Hearings*] (statement of Robert Gramling, Director of the Corporate Financial Audits, Accounting and Financial Management Division, United States General Accounting Office).

The recent failure of Lincoln Savings & Loan of Irvine, seized by federal regulators on April 14, 1989, presents a good example of internal control weaknesses. Eaton, *Lincoln Exemplifies How S&Ls Collapse*, *Official Says*, L.A. Times, Oct. 28, 1989, at D1, col. 4. William K. Black, regional counsel for the Office of Thrift Supervision in San Francisco, testified in hearings before Congress that a typical Lincoln ADC [acquisition, development, and construction] loan needed no down payment by the borrower, and included architect and developer fees, in addition to the cost of purchasing the property and construction. *Id.* at D9, col. 2. Additionally, Black testified that borrowers were not required to pay off any principal for up to five years from the date of the loan. *Id.* "The typical ADC project that sank thrifts," he said, "was scores of millions of dollars in size Yet hundreds of such loans were made with no loan application, no credit checks, with no appraisal or feasibility study, with no down payment and no personal guarantee" *Id.*

Irresponsible lending policies in both the domestic and international markets have led to the majority of the banking industry's current ills. *Hearings, supra* (statement of Rep. Annunzio). "While thrifts [S&Ls] were making bad loans in the United States, banks were making bad loans all over the world." *Id.* (statement of Rep. Annunzio). These "bad" loans generally fall into one of two categories. The first category entails those loans used to finance leveraged buyouts (LBOs). *Id.* These are high-risk loans because the heavy indebtedness of the target company (whose assets are used to secure the loan), resulting from the LBO, often drives the company into bankruptcy. *See, e.g.,* Kupetz v. Wolf, 845 F.2d 842 (9th Cir. 1988) (bankruptcy filed two and one-half years after LBO); Wieboldt Stores, Inc. v. Schottenstein, 94 Bankr. 488 (N.D. Ill. 1988) (bankruptcy filed one year after LBO), *appeal granted*, No. 89-5216 (N.D. Ill. 1989) (LEXIS, Bkrtcy Library, Cases file). At the end of 1988, United States banks had LBO exposure over \$175 billion. *Hearings, supra* (statement of Rep. Annunzio).

The second category of "bad" loans consists of loans made to "less developed countries" (LDCs). FDIC, 1988 ANNUAL REPORT 55 (1989) [hereinafter FDIC]. Many LDCs have problems repaying their debt. *Id.* at 56. Further problems could result in major losses and write-downs of the debt (a recognition that a portion of the debt is irrecoverable), thus

in 1988, with deposits of over \$24 billion and assets of over \$35 billion, set a post-Depression record exceeding the previous high of 184 failures in 1987.² This was eclipsed in 1989 as 206 FDIC-insured banks either failed or received assistance.³ The chairman of the Resolution Trust Corporation, the federal agency created by the recent savings and loan bailout bill⁴ and charged with liquidating failed savings institutions, has identified 223 troubled savings and loans as likely candidates for federal takeover.⁵

The high number of insolvent banks and savings institutions reflects

"plac[ing] a strain on banks holding a significant amount of LDC debt." *Hearings, supra* (statement of Robert Gramling, Director of the Corporate Financial Audits, Accounting and Financial Management Division, United States General Accounting Office). At the end of 1988, United States banks held over \$81 billion in LDC debt. *Id.* (statement of Rep. Annunzio).

2. FDIC, *supra* note 1, at 8. At the end of 1988, federal regulators had identified 1,406 "problem" banks of the 13,606 banks insured by the FDIC. *Id.* at 5. "Problem" banks are those institutions "whose financial, operational or managerial weaknesses are so severe so as to pose a serious threat to continued financial viability" *Id.*

3. FDIC, QUARTERLY BANKING PROFILE 4 (Dec. 31, 1989). In contrast, a total of only 566 banks failed from 1934 to 1979. FDIC, *supra* note 1, at 61. The following table presents the number of FDIC-insured banks that have failed since 1970, their deposits and assets:

YEAR	NUMBER	DEPOSITS (in thousands)	ASSETS (in thousands)
1970	7	\$ 55,229	\$ 62,147
1971	6	132,058	196,520
1972	1	99,784	22,054
1973	6	971,296	1,309,675
1974	4	1,575,832	3,822,596
1975	13	340,575	419,950
1976	16	865,659	1,039,293
1977	6	205,208	232,612
1978	7	854,154	994,035
1979	10	110,696	132,988
1980	10	216,300	236,164
1981	10	3,826,022	4,859,060
1982	42	9,908,379	11,632,415
1983	48	5,441,608	7,026,923
1984	79	2,883,162	3,276,411
1985	120	8,059,441	8,741,268
1986	138	6,471,100	6,991,600
1987	184	6,281,500	6,850,700
1988	200	24,931,302	35,697,789

FDIC, *supra* note 1, at 61.

4. Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, § 501, 103 Stat. 183, 369 (1989).

5. Rosenblatt, *Up to \$100 Billion Extra Sought for S&L Rescues*, L.A. Times, Nov. 1, 1989, at A1, col. 2. The Resolution Trust Corporation created by FIRREA has already seized 283 savings and loan institutions with assets totalling \$112 billion. *Id.* For a year-by-year breakdown of the rate of federally insured bank and savings and loan failures of the early 1980s, see Note, *Borrower Beware: D'Oench, Duhme and Section 1823 Overprotect the Insurer When Banks Fail*, 62 S. CAL. L. REV. 255, 259 n.14 (1988).

a state of crisis.⁶ More and more money is required to bail them out.⁷ Concern has grown over the FDIC's ability to manage this crisis effectively in light of a dwindling FDIC insurance fund.⁸ The insurance fund's size depends in part upon the FDIC's ability to collect debts from the obligors of failed banks.⁹ Due to the FDIC's important role as insurer of banks, courts have traditionally aided the FDIC in its attempts to collect upon these obligations.¹⁰ Specifically, courts bar the use of certain defenses by borrowers under a body of judge-made law originating in

6. Many banks participate in, among other things, loan syndications and mortgage participation agreements, so as to "link their destinies with other institutions." Norcross, *The Bank Insolvency Game: FDIC Superpowers, the D'Oench Doctrine, and Federal Common Law*, 103 BANKING L.J. 316, 318 (1986). Because of this interrelatedness of financial institutions, while "[t]he spark that ignites the flames of failure may still be grounded in mismanagement or fraud, . . . by the time the regulators douse today's fires, they will have ravaged the credit relationships of banks, businesses, and individuals from coast to coast and, possibly, around the world." *Id.* In congressional subcommittee hearings, Representative Annunzio noted that "[t]he health of deposit insurance goes to the very heart of our financial system." *Hearings, supra* note 1 (statement of Rep. Annunzio).

Eighteen days after his inauguration, President Bush recognized the seriousness of the problem at a press conference: "I have decided to attack this problem head-on, with every available resource of our government because it is a national problem. I have directed that the combined resources of the federal agencies be brought together in a team effort to resolve the problem." H.R. REP. NO. 54(I), 101st Cong., 1st Sess. 304, *reprinted in* 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 100.

7. The recent failure of Lincoln Savings and Loan of Irvine, California, is expected to cost the FDIC up to \$2 billion alone. Eaton, *supra* note 1, at D1, col. 4. The owner of Lincoln Savings has predicted that the federal bailout of the savings and loan industry will cost more than \$500 billion. Pine, *Keating Predicts S&L Bailout Will Cost \$500 Billion*, L.A. Times, Jan. 15, 1990, at D2, col. 2. Industry experts generally use a lower estimate of \$300 billion, a figure which covers only the cost of dismantling failed S&Ls and paying off depositors; that figure does not include depreciation of the real estate holdings of those S&Ls. *Id.* The United States Treasury estimates initial costs at \$157 billion. *Id.* Congress has recognized that the \$50 billion originally authorized by FIRREA will be insufficient and now seeks an extra \$100 billion. Rosenblatt, *supra* note 5, at A1, col. 2.

8. In 1988, the Bank Insurance Fund took a net loss of \$4.2 billion, the first such loss since its creation fifty years ago. FDIC, *supra* note 1, at 42-43. At the end of 1988, the ratio of the deposit insurance fund balance to insured deposits was 0.80%, down from 1.10% the year before. *Id.* at 74. This was its lowest level ever and represents a 23% decline. *Id.* at xiii (Chairman's Statement). Though the banking industry as a whole posted all-time six-month record profits in the first half of 1989, these record profits do not help the FDIC because the insurance fund pays for bank failures but does not share in bank profits. *Hearings, supra* note 1 (statement of Rep. Annunzio). Additionally, the record first-half profits were followed by two of the worst quarters of the eighties. FDIC, *Commercial Banking Performance*, Q. BANKING PROFILE, 4th Quarter, 1989, at 1.

9. See *Gunter v. Hutcheson*, 674 F.2d 862, 865 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982). For a discussion of the various factors which affect the size of the insurance fund, see *infra* notes 468-70 and accompanying text.

10. See, e.g., *Langley v. FDIC*, 484 U.S. 86, 96 (1987); *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 456-59 (1942); *Gunter*, 674 F.2d at 868-72; see also *infra* note 305 and accompanying text.

D'Oench, Duhme & Co. v. FDIC.¹¹ The *D'Oench, Duhme* doctrine states that secret agreements between a bank's obligors and the bank are unenforceable if such an agreement would diminish the FDIC's rights.¹² Congress granted the FDIC even more protection than that conferred by the Supreme Court in *D'Oench, Duhme* by codifying a variation of this doctrine within the Federal Deposit Insurance Act at 12 U.S.C. § 1823(e).¹³ Courts also shield the FDIC from various state-law defenses under another federal common-law doctrine originating in *United States v. Kimbell Foods, Inc.*¹⁴ which affords the FDIC the status of a holder-in-due-course.¹⁵ These various litigation "superpowers" are generally raised by the FDIC as "counter-defenses" to an obligor's "defenses" when the FDIC brings suit upon an asset of a failed bank.¹⁶

Despite these various FDIC shields, recent cases suggest that the FDIC may still be unable to recover on an asset where it is a fraudulent

11. 315 U.S. 447 (1942).

12. *Id.* at 460-61.

13. 12 U.S.C. § 1823(e) (1988).

14. 440 U.S. 715 (1979).

15. See, e.g., *Gunter*, 674 F.2d at 873. Holder-in-due-course is defined by U.C.C. § 3-302 (1987). Section 3-302 provides:

- (1) A holder in due course is a holder who takes the instrument
 - (a) for value; and
 - (b) in good faith; and
 - (c) without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person.
- (2) A payee may be a holder in due course.
- (3) A holder does not become a holder in due course of an instrument:
 - (a) by purchase of it at judicial sale or by taking it under legal process; or
 - (b) by acquiring it in taking over an estate; or
 - (c) by purchasing it as part of a bulk transaction not in regular course of business of the transferor.
- (4) A purchaser of a limited interest can be a holder in due course only to the extent of the interest purchased.

Id. Holder-in-due-course status carries with it special rights set out in U.C.C. § 3-305. Generally, the holder-in-due-course takes free of what are called "personal" defenses, including failure or lack of consideration, breach of warranty, unconscionability, and fraud in the inducement. Norcross, *supra* note 6, at 331. Defenses that may be asserted against a holder-in-due-course are known as "real" defenses and include infancy (to the extent that it is a defense to a simple contract), incapacity, duress, illegality of the transaction, fraud in the factum, discharge in bankruptcy, and any other discharge of which the holder has notice when he takes the instrument. U.C.C. § 3-305(2) (1987). For a discussion of the *Kimbell Foods* analysis, see *infra* notes 308-52 and accompanying text.

16. Norcross, *supra* note 6, at 335.

transferee¹⁷ under the United States Bankruptcy Code.¹⁸ In other words, a bankruptcy trustee may be able to avoid the FDIC's interest in an asset acquired from a failed bank where the asset was originally fraudulently transferred to the bank by a now-bankrupt debtor. A strong argument remains, however, that the Bankruptcy Code shields the FDIC from liability as a bona fide purchaser for value.¹⁹ Given the current crisis, it is crucial that the FDIC be invulnerable to fraudulent transferee liability when suing upon an asset of a failed bank in order to prevent a far-reaching detrimental economic impact.²⁰

This Comment traces the birth and development of the FDIC and the protection traditionally afforded it by courts and Congress. It also follows the development of bankruptcy law and analyzes the bankruptcy trustee's powers. This Comment then focuses on the conflict between the federal Bankruptcy Code and the federal statutory and common-law FDIC "superpowers," and analyzes how a court might resolve the conflict under each of the traditional FDIC "superpowers." To answer the question whether the traditional protection granted the FDIC can be consistently extended to fraudulent transferee liability, this Comment analyzes the policies embodied within the conflicting laws. Thus, the policy behind bankruptcy law, equitable distribution of the assets of bankrupt debtors, is weighed against the policy behind the FDIC "super-

17. A bankruptcy trustee has broad powers to recover property of the estate transferred by the debtor prior to the declaration of bankruptcy. 11 U.S.C. § 548(a)(1) (1988); Levin, *An Introduction to the Trustee's Avoiding Powers*, 53 AM. BANKR. L.J. 173, 174-77 (1979). One such power allows the trustee to avoid (and ultimately perhaps recover) any transfer by the debtor which is deemed fraudulent and which was made on or within one year of the filing of the bankruptcy petition. *Id.* at 179-83. A recipient of such property would be a "fraudulent transferee."

18. See *Gallant v. Kanterman (In re Kanterman)*, 97 Bankr. 768 (Bankr. S.D.N.Y.) (FDIC not protected from avoidance of fraudulent transfer of mortgage and note), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989). For the facts and holding of *Kanterman*, see *infra* notes 182-203 and 232-52 and accompanying text. See also *La Mancha Aire, Inc. v. FDIC (In re La Mancha Aire, Inc.)*, 41 Bankr. 647, 649 (Bankr. S.D. Fla. 1984) (FDIC not protected from avoidance of preferential transfer of security interest); 11 U.S.C. §§ 101-1330 (1988).

19. 11 U.S.C. § 550(b) protects from fraudulent transferee liability any "transferee that takes for value, including satisfaction or securing of a present or antecedent debt in good faith, and without knowledge of the voidability of the transfer avoided; or . . . any immediate or mediate good faith transferee of such transferee." 11 U.S.C. § 550(b) (1988).

20. The FDIC records the funds expended to assist or close a bank as a receivable and then attempts to recover on the assets of the bank. FDIC, *supra* note 1, at 45. At the end of 1988, the FDIC held gross receivables from bank assistance and failures of over \$17.5 billion. *Id.* at 47. It set aside reserves for expected losses due to inability to collect upon assets of the failed banks of over \$12 billion. *Id.* As the court in *FDIC v. McClanahan* noted, "when the FDIC sues as receiver, victory for the defendant will ordinarily mean a loss that is borne or shared by the uninsured creditors or depositors of the failed bank." 795 F.2d 512, 516 (5th Cir. 1986).

powers," the protection of the banking industry. Noting Congress' repeated efforts to protect the banking industry and the FDIC,²¹ this Comment concludes that future congressional legislation to afford the FDIC the status of a holder-in-due-course would advance Congress' goals and best protect the FDIC.

II. BACKGROUND

Analysis of this conflict requires familiarity with the FDIC, its purposes, and the powers that Congress vested in the FDIC. It also requires some knowledge of the bankruptcy trustee's avoidance powers.²² The following background should provide the reader with a better understanding of the protection afforded the FDIC by Congress and the courts, as well as the conflict that arises between the FDIC and the bankruptcy trustee.

A. *The Federal Deposit Insurance Corporation*

1. The creation and function of the FDIC

In 1933, caught in the midst of the Great Depression, the United States struggled in dire economic straits.²³ "Runs" on banks became common as "[m]en and women with life savings and business earnings

21. This is evidenced most recently by the federal legislation bailing out the savings and loan industry. See FIRREA, Pub. L. No. 101-73, 103 Stat. 183 (1989).

22. Various powers are granted the trustee by the Bankruptcy Code to gather certain assets into the "estate" of the bankrupt debtor in order to pay off unsecured creditors. Levin, *supra* note 17, at 173. These are known collectively as the trustee's "avoiding powers." *Id.* The first is the ability of the trustee to avoid and recover "preferences" given by the debtor to creditors. 11 U.S.C. § 547 (1988). A transfer is a "preference" and thus avoidable if made to or for the benefit of a creditor, for or on account of an antecedent debt, made while the debtor was insolvent and on or within 90 days of the filing for bankruptcy or up to one year if the creditor who received the transfer was an insider of the debtor, which enabled the creditor to receive more than the creditor would receive in a liquidation. *Id.* § 547(b). Another avoidance power is the ability of the trustee to avoid fraudulent transfers. *Id.* §§ 544(b), 548; see also *infra* notes 149-72 and accompanying text. A third avoidance power is the "strong-arm" clause. Levin, *supra* note 17, at 173. This grants the trustee the rights of a judicial lien creditor with respect to personal property, and the rights of a bona fide purchaser with respect to real property. 11 U.S.C. § 544(a) (1988). This enables the trustee to "beat out" security interests that are unperfected, and property transfers that are unrecorded, at the time of the filing of the petition. H.R. REP. NO. 595, 95th Cong., 2d Sess. 314, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6326.

23. The gross national product in 1933 was nearly a third less than in 1929. J.K. GALBRAITH, *THE GREAT CRASH* 173 (1961). The unemployment rate was 25%, with over 13 million people out of work. *Id.* According to another economic historian, "[T]he country was gripped with financial chaos; banks were closing, checks were unpaid. Travelers were left stranded without ready funds and credit was at a standstill." J.F.T. O'CONNOR, *THE BANK CRISIS AND RECOVERY UNDER THE ROOSEVELT ADMINISTRATION* 7 (1938).

deposited in banks stormed doors to retrieve their fortunes before it was too late."²⁴ Congress passed a variety of banking bills²⁵ both as an immediate stop-gap measure to prevent further economic disaster, and as a method of ensuring a continuing stable economy. Congress created and financed the FDIC²⁶ as one such measure "to bolster the entire banking and credit structure" of the United States.²⁷ The FDIC, a federal agency, acts primarily as an insurer of bank deposits.²⁸ By acting as insurer, the FDIC ensures the soundness of the United States banking system by generating public confidence in banks and the economy in

24. J.F.T. O'CONNOR, *supra* note 23, at 7-8. A "run" on a bank occurs when large numbers of depositors panic, thinking the bank will be unable to meet its obligations. Their fears become a reality as depositor after depositor attempts to withdraw all of their funds. As banks do not retain that much cash on hand, the bank soon becomes unable to meet depositor demands, thus fueling the panic. See generally National Radio Address of President Roosevelt (Mar. 12, 1933) (delivered from the President's study in the White House), *reprinted in* J.F.T. O'CONNOR, *supra* note 23, at 100-04 app. (explaining reasons behind Roosevelt's declaration of bank holiday on Mar. 6, 1933).

25. Norcross, *supra* note 6, at 316 n.1. Banking bills passed included the Banking Act of 1935, Pub. L. No. 74-305, ch. 614, 49 Stat. 684 (codified in scattered sections of 12 U.S.C.); and the Banking Act of 1933, Pub. L. No. 73-66, ch. 89, 48 Stat. 162 (codified in scattered sections of 12 U.S.C.). For a thorough treatment of the measures taken by President Roosevelt during the Depression to stabilize the banking industry, see J.F.T. O'CONNOR, *supra* note 23.

26. The FDIC was first created by the Banking Act of 1933, amending the Federal Reserve Act of 1913. Banking Act of 1933, ch. 89, 48 Stat. 162; see also Norcross, *supra* note 6, at 316 n.1. In 1950, Congress amended the Federal Reserve Act to set forth the Federal Deposit Insurance Act separately. Act of Sept. 21, 1950, Pub. L. No. 81-797, ch. 967, 64 Stat. 873 (1950) (codified as amended at 12 U.S.C. §§ 1811-32 (1988)). Unless otherwise noted, all references to the FDIC will also refer to the Federal Savings and Loan Insurance Corporation (FSLIC). The FSLIC was created in 1934 as an insurer of savings and loan institutions. Act of June 27, 1934, ch. 847, 48 Stat. 1256, *repealed by* FIRREA, Pub. L. No. 101-73, § 401, 103 Stat. 183, 354 (1989). The similarity of FSLIC's role to that of the FDIC led the court in *FSLIC v. Murray* to note a "parallel in statutory missions." 853 F.2d 1251, 1254 (5th Cir. 1988). The *Murray* court held that the *D'Oench, Duhme* doctrine's protection applies to the FDIC and the FSLIC alike. *Id.* See also *Taylor Trust v. Security Trust Fed. Sav. & Loan Ass'n, Inc.*, 844 F.2d 337, 342 (6th Cir. 1988) (*D'Oench, Duhme* doctrine protects both FDIC and FSLIC). FSLIC has since been abolished by FIRREA, Pub. L. No. 101-73, § 401, 103 Stat. 183, 354 (1989). FIRREA transfers the functions and activities of FSLIC to the FDIC or one of three entities: The Office of Thrift Supervision, the Federal Housing Finance Board, or the Resolution Trust Corporation. *Id.* See also H.R. REP. NO. 54(I), 101st Cong., 1st Sess., 291, *reprinted in* 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 87. For further discussion of the effects of FIRREA, see *infra* notes 468 and 474 and accompanying text.

27. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 472 (1942) (Jackson, J., concurring) (citation omitted). In *Doherty v. United States*, the court wrote:

The [Federal Deposit Insurance Act] is an elaborate one by which Congress created a scheme for insuring to a limited extent the deposits of the banks participating in the plan for insurance for the manifest purpose of stabilizing or promoting the stability of banks, and to aid the government in its evergrowing financial transactions.

94 F.2d 495, 497 (8th Cir.), *cert. denied*, 303 U.S. 658 (1938).

28. *Gunter v. Hutcheson*, 674 F.2d 862, 865 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982). The FDIC insured 13,606 banks at the end of 1988. FDIC, *supra* note 1, at 5.

general.²⁹

Although the FDIC's powers have grown over the years, its role remains the same.³⁰ The FDIC performs its role by acting in two different capacities.³¹ First, the FDIC acts in a corporate capacity. In this role, the FDIC regulates and supervises insured banks,³² has the power to financially assist troubled banks before and after they fail,³³ and insures deposits up to \$100,000 per depositor.³⁴

29. *Hearings, supra* note 1 (statement of Rep. Annunzio). See also J.F.T. O'CONNOR, *supra* note 23, at 25-26. J.F.T. O'Connor served as Comptroller of the Currency from 1933 to 1938, as a member of the Federal Reserve Board from 1933 to 1935, and as vice-chairman of the FDIC from 1934 to 1938. *Id.* at i. Of the FDIC's beneficial impact, he wrote:

Experience has shown in connection with the failures of insured banks since the formation of the [FDIC] that no longer does a community undergo convulsive excitement nor do depositors in the affected bank go about with blanched faces seeking to determine how they will be able to carry on their own affairs because of the bank's failure. They know that the [FDIC] will move in promptly and make available to them the total of their funds up to the [statutory] limit and that their business may move on and that their own financial affairs will not be materially hampered.

Id. at 25-26.

30. The FDIC is authorized to issue "cease and desist" orders to prevent "unsafe or unsound" banking practices. 12 U.S.C. § 1818(b) (1988). From 1986 to 1988, the FDIC issued a total of 356 cease and desist orders. FDIC, *supra* note 1, at 21. The FDIC can also order the suspension or removal of any officer or director of an insured depository institution. 12 U.S.C. § 1818(e) (1988). In the years 1987 and 1988, the FDIC brought a total of 98 removal and prohibition actions involving 108 individuals. FDIC, *supra* note 1, at 21. Perhaps most importantly, the FDIC can terminate the insured status of any member bank. 12 U.S.C. § 1818(a) (1988). From 1986 to 1988, the FDIC terminated the insurance of seven banks. FDIC, *supra* note 1, at 21. Lastly, the FDIC may "exercise . . . all powers specifically granted . . . and such incidental powers as shall be necessary to carry out the powers so granted." 12 U.S.C. § 1819 (1988).

31. *Gunter*, 674 F.2d at 865; Note, *supra* note 5, at 260. These capacities are authorized by statute. 12 U.S.C. § 1819 (1988) (authorizing corporate capacity); *id.* § 1821(e) (authorizing capacity as receiver).

32. 12 U.S.C. §§ 1820(b), 1828 (1988).

33. *Id.* § 1823(c)(1), as amended by FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 255 (1989). The statute provides:

The Corporation is authorized, in its sole discretion and upon such terms and conditions as the Board of Directors may prescribe, to make loans to, to make deposits in, to purchase the assets or securities of, to assume the liabilities of, or to make contributions to, any insured depository institution—(A) if such action is taken to prevent the closing of such insured depository institution; (B) if, with respect to a closed insured depository institution, such action is taken to restore such closed insured depository institution to normal operation; or (C) if, when severe financial conditions exist which threaten the stability of a significant number of insured depository institutions or of insured depository institutions possessing significant financial resources, such action is taken in order to lessen the risk to the Corporation posed by such insured depository institution under such threat of instability.

Id. In 1988, the FDIC assisted 81 banks at an estimated savings to the FDIC of over \$900 million. FDIC, *supra* note 1, at 7. The savings estimate is calculated through comparison with the estimated costs if the banks had failed. *Id.*

34. 12 U.S.C. § 1821(a) (1988). Interest accumulation over \$100,000 is not covered by deposit insurance. Lazzareschi, *Deposit Insurance Cap Includes Interest*, L.A. Times, Mar. 3,

The FDIC also acts as a receiver of failed banks.³⁵ As receiver, the FDIC is empowered to give notice of the bank's closing to those holding claims against the bank, collect upon obligations held by the bank as assets, enforce the individual liability of stockholders and directors, and otherwise liquidate and wind up the bank's affairs.³⁶

2. FDIC options as regulator and insurer of failed banks

The FDIC has two primary options when a bank fails, both arising out of its role as regulator and insurer: (1) liquidation or (2) purchase and assumption.³⁷ The option chosen will ultimately determine the capacity, corporate or receiver, in which the FDIC sues upon the failed bank's assets.³⁸

In exercising the liquidation option, the FDIC becomes the receiver of the failed bank and sells off the bank's assets.³⁹ The funds generated are used to pay off the bank's depositors, and the insurance fund covers any deficiency.⁴⁰ When the FDIC chooses this method, it brings suit in its capacity as receiver to collect the loans of the failed bank.⁴¹

The liquidation method, however, has several disadvantages. First, closing a bank significantly affects the public's perception of the banking industry's stability and thus undermines the very confidence the FDIC is supposed to generate.⁴² Second, the bank's depositors suffer great inconvenience; regular banking services are no longer available to them, depositors' accounts are frozen, and checks are returned unpaid.⁴³ Lastly, payment to depositors of the insured portion of their funds may take a

1990, at D3, col. 1. Thus, if a depositor holds as an individual a \$5,000 checking account, a \$25,000 savings account, and a \$75,000 certificate of deposit, the total amount exceeds the insurance cap by \$5,000 plus any accumulated interest. *Id.* Depositors are actually covered up to \$100,000 in each of two categories of accounts, joint and individual. *Id.* Therefore, accounts held jointly with another are also covered up to \$100,000 in addition to the coverage on accounts held as an individual. *Id.*

35. 12 U.S.C. § 1821(c) (1988) (FDIC as receiver of national banks); *id.* § 1821(e) (FDIC as receiver of state banks). Federal statute requires the FDIC to accept appointment as receiver of a failed bank. *Id.* § 1821(c).

36. *Id.* § 1821(d).

37. *Gunter*, 674 F.2d at 865. A third option used by the FDIC in connection with 30 of the banks that failed in 1988 is the insured deposit transfer. FDIC, *supra* note 1, at 9. In an insured deposit transfer, the insured deposits are not paid off directly to their owners but rather the accounts are transferred to an existing healthy institution. *Id.*

38. Note, *supra* note 5, at 260.

39. 12 U.S.C. § 1821(d) (1988).

40. *Gunter*, 674 F.2d at 865.

41. Note, *supra* note 5, at 259.

42. *Gunter*, 674 F.2d at 865.

43. *Id.*

long time, and the uninsured portion may be irretrievably lost.⁴⁴

The other alternative, preferred by the FDIC whenever feasible,⁴⁵ is to execute a "purchase and assumption" transaction.⁴⁶ Here, the FDIC operates in both its corporate capacity as insurer and in its capacity as receiver.⁴⁷ The appropriate banking authority appoints the FDIC as receiver of the failed bank,⁴⁸ and the FDIC solicits bids⁴⁹ from other healthy banks for the purchase of the failed bank's assets and assumption of its liabilities.⁵⁰ Upon acceptance of a bid, the healthy bank purchases the assets and assumes the liabilities from the FDIC as receiver.⁵¹

These transactions must occur immediately upon the closing of a failed bank, in order to preserve the bank's value as a "going concern" and avoid an interruption in banking services.⁵² Accordingly, as the healthy bank may not have enough time to evaluate the quality of the assets it purchases, purchase and assumption agreements provide that the

44. *Id.* At the end of 1988, over \$580 million of the deposits in FDIC-insured banks were uninsured. FDIC, *supra* note 1, at 74. Despite these disadvantages, under 12 U.S.C. § 1823(c)(4)(A), the FDIC must implement a liquidation when the cost of other options would be higher. 12 U.S.C. § 1823(c)(4)(A) (1988).

45. *Gunter*, 674 F.2d at 865. In the years 1986 to 1988, the FDIC arranged 395 purchase and assumption transactions. FDIC, *supra* note 1, at 10. Only 38 straight liquidations were conducted in that same period. *Id.*

46. *Gunter*, 674 F.2d at 865. See 12 U.S.C. § 1823(c)(2)(A) (1988).

47. *Gunter*, 674 F.2d at 865; FDIC v. Ashley, 585 F.2d 157, 160 (6th Cir. 1978) (FDIC often acts in two capacities simultaneously).

48. *Gunter*, 674 F.2d at 865. For a national bank, the appropriate banking authority is the chartering authority, the Office of the Comptroller of the Currency (OCC). Portis, *FDIC's Powers After a Bank Failure*, 65 U. DET. L. REV. 259, 260 (1988). Federal statute requires that the OCC appoint the FDIC receiver. 12 U.S.C. § 1821(c) (1988). The FDIC is required by statute to accept this appointment. *Id.* § 1821(d). For a state bank, the appropriate banking authority varies from state to state. Portis, *supra*, at 260. Although some states make it optional, many states require the banking authority to appoint the FDIC as receiver. Compare CAL. FIN. CODE § 3221 (West 1989) (superintendent may tender appointment as receiver to FDIC if advisable) with MICH. STAT. ANN. § 23.710(251) (1983) (commissioner shall request that court appoint FDIC receiver). The FDIC must also accept this appointment. 12 U.S.C. § 1821(e) (1988).

49. After an insured bank's primary regulator notifies the FDIC of the bank's imminent insolvency, the FDIC's Department of Liquidation prepares a bid information package for that bank. FDIC, *supra* note 1, at 19. This package contains financial and non-financial information about the bank that helps the Division of Bank Supervision prepare a recommendation for the FDIC's Board of Directors as to whether to attempt a purchase and assumption or a liquidation. *Id.* This package is also given to potential bidders so they can make an informed decision. *Id.*

50. *Gunter*, 674 F.2d at 865. See also Portis, *supra* note 48, at 261-62. Generally, a failed bank's liabilities will exceed its assets since it was insolvent when closed. *Id.* at 261 & n.22. The FDIC, in its corporate capacity, will pay the purchasing bank the difference in cash to make the transaction attractive. *Id.* at 261.

51. *Gunter*, 674 F.2d at 865.

52. *Id.*

purchasing bank may return all assets not of the highest banking quality to the FDIC in the FDIC's capacity as receiver.⁵³ The FDIC, in its corporate capacity as insurer, then buys these assets from the FDIC as receiver using money from the insurance fund.⁵⁴ The FDIC as receiver then transfers these payments to the purchasing bank.⁵⁵ The FDIC, as insurer, then attempts to collect on these "bad" assets in order to minimize loss to the insurance fund.⁵⁶ With this method, the FDIC holds the uncollected loans in its corporate capacity as insurer and brings suit in that capacity to collect upon the assets.⁵⁷

The purchase and assumption route has many advantages over a

53. *Id.* at 865. Acceptable assets include the failed bank's cash, its securities portfolio, the bank building, and portions of the loan portfolio that are not past-due. Burgee, *Purchase and Assumption Transactions Under the Federal Deposit Insurance Act*, 14 FORUM 1146, 1154 (1979). Assets which are not of the "highest banking quality" are generally the bank's non-performing assets. Portis, *supra* note 48, at 262 n.24. These include assets which are in default and assets which bank examiners have criticized as having inflated values. *Id.* At the end of the third quarter of 1989, the composition of non-performing assets held by United States banks was as follows:

Non-current Commercial and Industrial Loans	29.5%
Non-current Real Estate Loans	27.1%
Non-current Consumer Loans	5.9%
All Other Non-current Loans	20.8%
Real Estate Owned	16.7%

FDIC, *Commercial Banking Performance*, Q. BANKING PROFILE, 3d Quarter, 1989, at 2.

To reduce the size of its asset portfolio, the FDIC has recently begun using "whole-bank" purchase and assumption transactions. FDIC, *supra* note 1, at xiii (Chairman's Statement). In a "whole-bank" purchase and assumption transaction, the acquiring bank purchases essentially all of the assets of the failed bank, including its bad loans, at a discounted price. *Id.* at 9. Of the 164 purchase and assumption transactions conducted in 1988, 69 were "whole-bank" transactions. *Id.* at xiii (Chairman's Statement).

54. *Gunter*, 674 F.2d at 865.

55. *Id.*

56. *Id.*

57. Note, *supra* note 5, at 259-60. The FDIC has also begun using a modified purchase and assumption technique which results in it holding the assets and bringing suit upon them in its capacity as receiver. Norcross, *supra* note 6, at 350 n.146. In a modified purchase and assumption transaction, the FDIC in its corporate capacity loans money to the FDIC as receiver for the failed bank, taking back a security interest in the substandard assets not transferred to the acquiring bank. *Id.* Title and possession of these assets are still held by the FDIC as receiver and suit is brought in that capacity. *Id.* at 350. The first time the FDIC used this method, there was no specific enabling legislation. *Id.* at 348. However, after passage of FIRREA, the modified purchase and assumption is expressly authorized. The statute provides:

Any conservator, receiver, or liquidator appointed for any insured depository institution in default, including the Corporation acting in such capacity, shall be entitled to offer the assets of such depository institutions for sale to the Corporation or as security for loans from the Corporation. . . . The Corporation, in its discretion, may make loans on the security of or may purchase and liquidate or sell any part of the assets of an insured depository institution which is now or may hereafter be in default.

FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989).

liquidation. First and foremost under this method, the bank never closes.⁵⁸ This prevents inconvenience to depositors and limits erosion of public confidence.⁵⁹ Moreover, short-term loss to the insurance fund is minimized and the FDIC avoids having to pay out large sums of cash to insured depositors.⁶⁰ Finally, the purchasing bank receives a new investment with little risk and with full recourse to recover on "bad" assets against the FDIC as receiver.⁶¹

3. The protection afforded the FDIC

a. *D'Oench, Duhme & Co. v. FDIC and its progeny*

The importance of the FDIC's role as insurer required that courts enhance its ability to collect upon an asset acquired from a failed bank where an obligor of the insured bank misled the FDIC as to the true value of the asset.⁶² In other words, if the borrower had made some sort of misrepresentations either to the bank or in concert with the bank to the FDIC, the FDIC needed to be shielded from defenses relating to the misrepresentation that the borrower could raise against the FDIC's attempts to collect. The United States Supreme Court created such protection in *D'Oench, Duhme & Co. v. FDIC*.⁶³

In *D'Oench, Duhme*, defendant D'Oench, Duhme & Co., a securities dealer, had sold certain bonds which later defaulted to the Belleville Bank & Trust Co.⁶⁴ The bank did not wish to carry past-due bonds on its books, so it entered into an agreement under which the defendant executed notes payable to the bank in the amount of and secured by the bonds.⁶⁵ The bank could then carry the notes on its books as a "good"

58. Note, *supra* note 5, at 260.

59. *Id.*

60. *Id.* at 261.

61. *Gunter*, 674 F.2d at 865-66. A purchasing bank pays a premium when taking over a failed bank due to the bank's "going-concern" value. Barnett, Horvitz & Silverberg, *Deposit Insurance: The Present System and Some Alternatives*, 94 BANKING L.J. 304, 312 (1977). This premium is subtracted from the cash that the FDIC provides the acquiring bank to make up difference between the assets purchased and the liabilities assumed. *Id.* The "going-concern" value exists because the failed bank already has a deposit and liability structure in place. Norcross, *supra* note 6, at 319 n.14. The failed bank's existing customers, fully insured, will probably continue to bank there following the purchase and assumption. *Id.* Thus, a purchasing bank "'buy[s]' customers as opposed to paying marketing expenses to attract them." *Id.*

62. See *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 472-73 (1942) (Jackson, J., concurring). One commentator noted that "[e]very dollar recovered from an asset being liquidated by the FDIC reduces the exposure of the [insurance] fund" Norcross, *supra* note 6, at 329.

63. 315 U.S. 447 (1942).

64. *Id.* at 454.

65. *Id.*

asset, instead of carrying the defaulted bonds.⁶⁶ The receipts given to the defendant for the notes stated: "This note is given with the understanding it will not be called for payment. All interest payments to be repaid."⁶⁷ The purpose of the interest payments, known to the defendant, was to keep the notes as "live paper."⁶⁸ The true nature of this arrangement was not apparent to third parties such as the FDIC.⁶⁹

The FDIC, the bank's insurer since 1934, acquired the note in 1938 after the bank failed.⁷⁰ When the FDIC sued upon the note, the defendant argued that, since it gave the note without any consideration and with the understanding that suit would never be brought upon it, the defendant was immune from liability.⁷¹ The FDIC responded that the defendant could not assert these defenses, since the note had been executed for the purpose of allowing the bank to misrepresent its assets to creditors, state banking authorities, and the FDIC.⁷²

The Supreme Court, holding that federal law controlled the FDIC's rights and obligations,⁷³ ruled for the FDIC.⁷⁴ According to the Court, certain provisions of the Federal Reserve Act evidenced a congressional intent to protect the FDIC.⁷⁵ This was manifested particularly by the Act's provisions allowing criminal punishment of anyone who " 'for the purpose of obtaining any loan from the Corporation [FDIC] . . . or for the purpose of influencing in any way the action of the Corporation under this section, makes any statement, knowing it to be false, or wilfully overvalues any security. . . . ' " ⁷⁶

In order to effectuate this federal policy, the Court estopped the defendant from asserting either a failure of consideration or the existence of a secret agreement that the note would not be enforced.⁷⁷ The Court held that estoppel could arise without a finding of a "penal offense."⁷⁸

66. *Id.*

67. *Id.*

68. *Id.* "Live paper" refers to a banking transaction where the borrower has not defaulted, and where the bank has not noted the loan as substandard in its financial statements. Norcross, *supra* note 6, at 325 n.39.

69. *D'Oench, Duhme*, 315 U.S. at 473 (Jackson, J., concurring).

70. *Id.* at 454.

71. *Id.* at 456.

72. *Id.*

73. *Id.*

74. *Id.* at 459.

75. *Id.* at 456-57 (citing 12 U.S.C. § 264(s) (1988) (current version at FIRREA, Pub. L. No. 101-73, § 961, 103 Stat. 183, 500 (1989) (to be codified at 18 U.S.C. § 1007))).

76. *Id.* (quoting 12 U.S.C. § 264(s) (1988) (current version at FIRREA, Pub. L. No. 101-73, § 961, 103 Stat. 183, 500 (1989) (to be codified at 18 U.S.C. § 1007))).

77. *Id.* at 459-62.

78. *Id.* at 460.

The Court established that "[i]t would be sufficient in this type of case that the maker lent himself to a scheme or arrangement whereby the [FDIC] was or was likely to be misled."⁷⁹

Later cases have expanded the so-called *D'Oench, Duhme* doctrine to protect the FDIC from other sorts of agreements, including oral agreements of accord and satisfaction⁸⁰ and separate agreements regarding payment of loan proceeds.⁸¹ The *D'Oench, Duhme* doctrine has also defeated defenses of usury,⁸² estoppel,⁸³ fraud in the inducement,⁸⁴ laches,⁸⁵ waiver,⁸⁶ and lack of good faith.⁸⁷

*b. Section 1823(e): Congress' codification of the
D'Oench, Duhme doctrine*

Congress has since codified the *D'Oench, Duhme* doctrine.⁸⁸ The statute provides that for an obligor to enforce any agreement that diminishes the FDIC's rights in any asset acquired from a failed bank, the agreement must: (1) be in writing; (2) have been executed at the time the bank acquired the asset; (3) have been approved by the bank's directors; and, (4) have been held continuously in the bank's records.⁸⁹ As first

79. *Id.*

80. *FDIC v. Hoover-Morris Enters.*, 642 F.2d 785, 787 (5th Cir. Unit B Apr. 1981) (FDIC protected under *D'Oench, Duhme* from agreement by payee on note not to seek deficiency judgment against defendant).

81. *FDIC v. Sarvis*, 697 F. Supp. 1161, 1163-64 (D. Colo. 1988) (court rejected defense of failure of consideration under *D'Oench, Duhme* doctrine because "[D]efendant [had] signed a facially unqualified promissory note subject to an unwritten 'agreement' that the Bank would pay the loan amount to a holding company instead of to the defendant.").

82. *FDIC v. Julius Richman, Inc.*, 666 F.2d 780, 781 (2d Cir. 1981); *Charter Executive Center Ltd. v. FDIC (In re Charter Executive Center Ltd.)*, 34 Bankr. 131, 135-36 (Bankr. M.D. Fla. 1983); *FDIC v. Leach*, 525 F. Supp. 1379, 1389 (E.D. Mich. 1981).

83. *FDIC v. First Mortgage Investors*, 485 F. Supp. 445, 452-53 (E.D. Wis. 1980); *FDIC v. Willis*, 497 F. Supp. 272, 277-78 (S.D. Ga. 1980).

84. *FDIC v. McClanahan*, 795 F.2d 512, 513 (5th Cir. 1986); *FDIC v. Timbalier Towing Co.*, 497 F. Supp. 912, 920-21 (N.D. Ohio 1980); *British Columbia Inv. Co. v. FDIC*, 420 F. Supp. 1217, 1224 (S.D. Cal. 1976).

85. *Leach*, 525 F. Supp. at 1384-86.

86. *First Mortgage*, 485 F. Supp. at 453-54.

87. *Id.* at 453.

88. See 12 U.S.C. § 1823(e) (1988).

89. *Id.* The statute (as amended by FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989)) provides in pertinent part:

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 11, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement (1) is in writing, (2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution, (3) was approved by the board of directors of the depository

enacted, however, the statute only applied where the FDIC sued or was sued in its corporate capacity as insurer.⁹⁰ Thus, the original statute did not preempt application of the common-law doctrine in situations where the FDIC sued in its capacity as receiver.⁹¹ Accordingly, courts applied both the statute and the common-law doctrine in cases involving the FDIC.⁹² In 1989, Congress extended section 1823(e)'s protection to the FDIC as receiver by passage of FIRREA.⁹³ This amendment, however, still does not preempt application of the common-law doctrine⁹⁴ since the scope and application of section 1823(e)'s protection differ from that of the common-law doctrine.⁹⁵

institution or its loan committee, which approval shall be reflected in the minutes of said board or committee; and (4) has been, continuously, from the time of its execution, an official record of the depository institution.

Id.

90. 12 U.S.C. § 1823 (1988). Subsection (e) of 1823 previously referred only to the FDIC in its corporate capacity and courts accordingly restricted its application. *See, e.g.,* Gallant v. Kanterman (*In re Kanterman*), 97 Bankr. 768, 776 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989) (section 1823(e) inapplicable to actions brought by FDIC as receiver); *In re Selden*, 58 Bankr. 667, 677 (Bankr. D. Neb. 1986) ("[S]ection [1823] deals with the FDIC in its corporate capacity, not in its capacity as receiver of a state bank."). *But see* La Mancha Aire, Inc. v. FDIC (*In re La Mancha Aire*), 41 Bankr. 647, 649 (Bankr. S.D. Fla. 1984) (section 1823(e) "designed to protect the FDIC both as insurer and as receiver from the effect of secret agreements between an insured bank and its obligors"). Congress has since essentially codified the *La Mancha* holding by explicitly extending section 1823(e)'s protection to the FDIC as receiver. FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. 1823(e)).

91. It is well settled that the common-law doctrine is also applicable to the FDIC acting in its capacity as receiver. *See, e.g.,* FDIC v. McClanahan, 795 F.2d 512, 516 (5th Cir. 1986) (common-law rule of *D'Oench, Duhme* applies where FDIC sues in capacity as receiver); FDIC v. Hoover-Morris Enters., 642 F.2d 785, 787 (5th Cir. Unit B Apr. 1981) ("Apart from the protection against side agreements provided by § 1823(e), FDIC is protected under federal common law as announced in *D'Oench, Duhme & Co. v. FDIC*"); Howell v. Continental Credit Corp., 655 F.2d 743, 746 (7th Cir. 1981) ("Both *D'Oench* and § 1823 have been applied numerous times to effectuate the public policy interest in not enforcing 'secret agreements' against the FDIC when it is carrying out its statutorily-mandated duties to protect depositors."); *Sarvis*, 697 F. Supp. at 1164 (court barred defense of no consideration through application of both § 1823(e) and common-law doctrine where FDIC sued as receiver). For a discussion of the difference between the FDIC as receiver of a failed bank and its corporate role, see *supra* notes 31-36 and accompanying text.

92. *See supra* note 91 and accompanying text.

93. FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823(e)).

94. FIRREA's legislative history evidences congressional intent to provide more rather than less protection to the FDIC. It notes that FIRREA "makes it clear that [section 1823(e)] appl[ies] to assets that the FDIC acquires as receiver as well as to assets that it acquires in its corporate capacity. H.R. REP. NO. 101-54(I), 101st Cong., 1st Sess. 335, *reprinted in* 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 131.

95. Note, *supra* note 5, at 271. The protection of section 1823(e) is both more and less inclusive than that of *D'Oench, Duhme*. *Id.* at 271-72. Section 1823(e) is more inclusive, as it applies to *any* agreement, whether secret or not, and without reference to the obligor's culpa-

In interpreting cases in which the FDIC raises section 1823(e), the Supreme Court has expanded the statute's scope beyond the traditional protection the *D'Oench, Duhme* doctrine affords.⁹⁶ In *Langley v. FDIC*,⁹⁷ the Court held that the word "agreement" in the statute included "a misrepresentation concerning an existing fact."⁹⁸ The Court reasoned:

[O]ne who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to a scheme or arrangement that is likely to mislead the banking authorities, whether the condition consists of performance of a counterpromise (as in *D'Oench, Duhme*) or of the truthfulness of a warranted fact.⁹⁹

The Court relied upon the language of its opinion in *D'Oench, Duhme*, and found that where the "maker of the note lent himself to a *scheme or arrangement* whereby the banking authority . . . was likely to be misled," that scheme or arrangement could not be used as a defense against the FDIC.¹⁰⁰

The statute's underlying purpose supported the Court's broad reading. The Court noted that section 1823(e)'s purpose is to allow federal and state bank examiners to rely on a bank's records when valuing its assets.¹⁰¹ The Court observed that quick, accurate valuation is critical when the FDIC examines a bank for fiscal soundness and decides whether to liquidate it or to arrange a purchase and assumption of its assets.¹⁰² A misinformed regulatory decision will undoubtedly be a poor decision.¹⁰³ This would be detrimental to the role Congress envisioned for the FDIC as insurer of the United States banking industry's fiscal

bility. *Id.* Section 1823(e) is also less inclusive, because it only applies where the obligor asserts an agreement as a defense. *Id.* at 272.

96. See Portis, *supra* note 48, at 264 & n.42.

97. 484 U.S. 86 (1987).

98. *Id.* at 93.

99. *Id.*

100. *Id.* (emphasis in original).

101. *Id.* at 91. When a bank fails, the FDIC's Department of Liquidation conducts a detailed asset review. FDIC, *supra* note 1, at 19. This is used to provide the FDIC's Board of Directors with an estimate of the loss that would be involved in a liquidation of the bank. *Id.*

102. *Langley*, 484 U.S. at 91. For a discussion of the FDIC's options of either liquidating a failed bank or arranging a purchase and assumption, see *supra* notes 37-61 and accompanying text.

103. In *Gunter*, the court noted that in making such a decision, the FDIC must rely on the failed bank's records to estimate the amount of assets that will ultimately prove uncollectible. 674 F.2d at 879. The *Gunter* court explained that "[t]he [FDIC] can then compare its estimated loss from a purchase and assumption against its estimated loss from a liquidation and make the statutory judgment required under [section] 1823(e)." *Id.*

soundness.¹⁰⁴

*c. holder-in-due-course status for the FDIC under
United States v. Kimbell Foods, Inc.
and its progeny*

Further protection for the FDIC is found in a body of federal common law separate from *D'Oench, Duhme*. Courts in the Fifth, Sixth, and Eleventh Circuits have concluded that where the FDIC takes a note in good faith and without actual knowledge of any defense against the note, it takes the note free of all defenses which would not prevail against a holder-in-due-course.¹⁰⁵ Some courts have held that Congress, in passing section 1823(e), intended to give the FDIC holder-in-due-course status and have implied it into the statute itself.¹⁰⁶ Other courts, though, have found that although Congress clearly intended to protect the FDIC, section 1823(e) does not authorize holder-in-due-course status.¹⁰⁷ Instead, they have gone on to examine the federal common law.¹⁰⁸ Although these courts often rely on the policy articulated in *D'Oench, Duhme*, the decisions stem from a different federal policy of enabling purchase and assumption transactions to be speedily negotiated.¹⁰⁹

In granting the FDIC holder-in-due-course status, these courts have

104. See *supra* notes 23-36 and accompanying text.

105. See *Holt v. FDIC (In re CTS Truss, Inc.)*, 859 F.2d 357, 362 (5th Cir. 1988), *modified in part*, 868 F.2d 146 (5th Cir. 1989); *FDIC v. The Cremona Co.*, 832 F.2d 959, 964 (6th Cir. 1987), *cert. dismissed sub nom.* *Gonda v. FDIC*, 485 U.S. 1017 (1988); *FDIC v. Gulf Life Ins. Co.*, 737 F.2d 1513, 1518 (11th Cir. 1984); *Gunter*, 674 F.2d at 873; *Gilman v. FDIC*, 660 F.2d 688 (6th Cir. 1981). For a discussion of the similarity of this doctrine with the Bankruptcy Code's protection of bona fide purchasers for value see *infra* notes 354-432 and accompanying text.

106. See *FDIC v. Rosenthal*, 477 F. Supp. 1223, 1226 (E.D. Wis. 1979), *aff'd*, 631 F.2d 733 (7th Cir. 1980); *FDIC v. Rockelman*, 460 F. Supp. 999, 1003 (E.D. Wis. 1978).

107. *FDIC v. Wood*, 758 F.2d 156, 159 (6th Cir.), *cert. denied*, 474 U.S. 944 (1985).

108. *Id.* See also *Gunter*, 674 F.2d at 867.

109. *Kanterman*, 97 Bankr. at 775. In *Cremona*, the court refused to apply Ohio law which precluded the FDIC from obtaining holder-in-due-course status, as the application of that law frustrated the objectives of the federal program. 832 F.2d at 964; see also *Gunter*, 674 F.2d at 873 (claims barred not by section 1823(e) but rather by common-law doctrine protecting FDIC when it acquires note in execution of purchase and assumption transaction, in good faith, for value, and without actual knowledge of claims at time of entering into purchase and assumption); *FSLIC v. Murray*, 853 F.2d 1251 (5th Cir. 1988) (applying same rule to FSLIC). The *Kanterman* court also considered *Holt v. FDIC (In re CTS Truss, Inc.)*, 859 F.2d 357, 362 (5th Cir. 1988), *modified in part*, 868 F.2d 146 (5th Cir. 1989). In *CTS Truss*, the court added in dictum that FDIC holder-in-due-course status with respect to notes acquired in a purchase and assumption transaction precludes a bankruptcy trustee from seeking to subordinate the FDIC's claim on the basis of misconduct by the failed bank. 859 F.2d at 360-62. The *Kanterman* court noted, however, that "[t]he equitable subordination precluded in *CTS Truss* . . . hardly arose out of a secret agreement." *Kanterman*, 97 Bankr. at 775. Accordingly, the

held that where application of the state law would frustrate a federal program's objectives, state law does not apply.¹¹⁰ The leading case on this subject is *United States v. Kimbell Foods, Inc.*¹¹¹ In *Kimbell Foods*, the Small Business Administration and the Farmers Home Administration argued that federal, not state, law should govern the priority of their liens.¹¹² The Supreme Court, noting that it had "consistently held that federal law governs questions involving the rights of the United States arising under nationwide federal programs," agreed that federal law applied.¹¹³

The court in *Gunter v. Hutcheson*,¹¹⁴ applied this reasoning in a suit to collect on a note brought by the FDIC and rejected the defendant's state-law fraud claims where the FDIC lacked knowledge of the claims at the time it was appointed receiver of the bank.¹¹⁵ The court reasoned that otherwise, the "result would run directly counter to the policies behind the creation of the FDIC."¹¹⁶ The court in *Gunter* recognized that if the FDIC had to consider the possible impact of "variable state law" it would significantly impair its ability to carry out its function.¹¹⁷ Other courts have agreed that the increase in the cost of each purchase and assumption transaction due to assets that are uncollectible under state law would result in a "potentially enormous cost to the banking system as a whole."¹¹⁸ Accordingly, the *Gunter* court gave the FDIC holder-in-due-course status and protection from the state-law fraud claims.¹¹⁹ This

Kanterman court refused to consider whether the holder-in-due-course rule did or should apply. *Id.* at 775 n.7.

110. See, e.g., *Cremona*, 832 F.2d at 964 (Ohio law precluding holder-in-due-course status inapplicable); *Wood*, 758 F.2d at 160 (inappropriate to apply state law if state law prevents holder-in-due-course status).

111. 440 U.S. 715 (1979).

112. *Id.* at 726.

113. *Id.*

114. 674 F.2d 862 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982).

115. *Id.* at 873.

116. *Id.* at 870.

117. *Id.* at 869.

118. *Wood*, 758 F.2d at 161.

119. *Gunter*, 674 F.2d at 873. Under the Uniform Commercial Code (U.C.C.), the FDIC holding a note in its corporate capacity could almost never be a holder-in-due-course for two reasons. First, when the FDIC in its corporate capacity purchases notes from the FDIC as receiver as part of a purchase and assumption transaction, the notes are generally overdue. The U.C.C. definition of holder-in-due-course requires that the holder have no knowledge of default or of any defenses to enforcement. U.C.C. § 3-302(1)(c) (1987). The FDIC would also be precluded from holder-in-due-course status even without knowledge as the assets are acquired by the FDIC in a "bulk transaction not in regular course of business of the transferor." *Id.* § 3-302(3)(c). For the U.C.C. definition of holder-in-due-course, see *supra* note 15 and accompanying text.

holder-in-due-course protection has since been extended to protect the FDIC from defenses of usury,¹²⁰ federal securities law violations,¹²¹ waiver,¹²² estoppel,¹²³ unjust enrichment,¹²⁴ and equitable subordination.¹²⁵

As shown above, the FDIC receives significant protection when it seeks to collect on the assets of failed banks.¹²⁶ A problem arises, however, where a debtor has transferred property to a bank where such property may be recoverable by a bankruptcy trustee under the applicable sections of the Bankruptcy Code. The questions that arise in this situation include whether courts should treat such fraudulent transfers similarly to "secret agreements" under *D'Oench, Duhme*, thus validating the transfers; whether section 1823(e) bars avoidance; or whether the FDIC is a holder-in-due-course under the rationale of *Gunter*. Conversely, should the FDIC, when it assumes a bank's liabilities, also be deemed to have assumed the bank's liability for fraudulent transfers? In order to answer these questions, some background material on bankruptcy law is necessary.

B. Bankruptcy Law

1. The development of fraudulent transfer liability under bankruptcy law

Bankruptcy law has ancient origins. Since society first used fungible items as units of monetary measure and began to extend credit, the problem of insolvent debtors has troubled many commentators.¹²⁷ Modern United States bankruptcy law can be traced to the laws of various Italian city-states.¹²⁸ Bankruptcy principles of ancient Rome later combined with the law of other European countries and found their way into Eng-

120. *Wood*, 758 F.2d at 161.

121. *Gilman v. FDIC*, 660 F.2d 688, 695 (6th Cir. 1981).

122. *FDIC v. Gulf Life Ins. Co.*, 737 F.2d 1513, 1518 (11th Cir. 1984).

123. *Id.*

124. *Id.*

125. *CTS Truss*, 859 F.2d at 362.

126. See *supra* notes 62-125 and accompanying text.

127. The Old Testament speaks to the question:

[1] At the end of seven years thou shalt make a release. [2] And this is the manner of the release: Every creditor that lendeth ought unto his neighbour shall release it; he shall not exact it of his neighbour, or of his brother; because it is called [the Lord's] release. [3] Of a foreigner thou mayest exact it again

Deut. 15:1-3, reprinted in C. CARMICHAEL, *LAW AND NARRATIVE IN THE BIBLE* 78-79 (1985).

128. Levinthal, *The Early History of Bankruptcy Law*, 66 U. PA. L. REV. 223, 241-44 (1918).

lish common law.¹²⁹ These principles eventually crossed the Atlantic to the United States through colonial adoption of English common law.¹³⁰

Bankruptcy laws traditionally were enacted to protect creditors.¹³¹ Without such a statutory scheme, creditors would have incentive to individually collect as much as possible from the debtor prior to bankruptcy.¹³² Such behavior assures the debtor's ultimate collapse and ruin.¹³³ The equitable distribution ensured by bankruptcy laws is, in theory, that which the various creditors would reach on their own given the availability of perfect information.¹³⁴ Thus, as Professor Levinthal noted: "A special process of collective execution is devised, a process directed against all of the property of the debtor, resorted to for the common benefit and at the common expense of all the creditors."¹³⁵

The most important early English bankruptcy law, the Statute of Bankrupts, specifically targeted fraudulent debtors.¹³⁶ The statute was mostly punitive in nature and provided that a debtor who committed an

129. Levinthal, *The Early History of English Bankruptcy*, 67 U. PA. L. REV. 1, 4 n.12 (1919).

130. R. COSGROVE, *OUR LADY THE COMMON LAW: AN ANGLO-AMERICAN LEGAL COMMUNITY 1870-1930*, at 70-72 (1987). In *Gardner v. Cole*, the court wrote:

But antedating as [the English] statutes do the settlement of this country, and being mainly if not wholly, declaratory of the common law, which set a face of flint against frauds in every shape, they constitute the basis of American jurisprudence on these subjects, and are, in this State, part of the *unwritten law*.

21 Iowa 205, 210 (1866) (emphasis in original). Congress, in the legislative history of the 1978 Bankruptcy Code, noted that the history of present laws governing fraudulent transfers "dates from the statute of 13 Elizabeth," passed in 1570. H.R. REP. NO. 595, 95th Cong., 1st Sess. 375, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6331. Elizabeth I, daughter of Henry VIII and Anne Boleyn, ruled as England's queen from 1558 to 1603. 18 ENCYCLOPEDIA BRITANNICA 343-46 (15th ed. 1985). As monarch, her efforts to keep the royal coffers filled and thus avoid bankruptcy herself included sanctioning the plundering of gold-filled Spanish galleons by English privateers. R. ANAND, *ORIGIN AND DEVELOPMENT OF THE LAW OF THE SEA* 73 (1983); see also A. RUBIN, *THE LAW OF PIRACY* 40-50 (1988).

131. McCoid, *Bankruptcy, the Avoiding Powers, and Unperfected Security Interests*, 59 AM. BANKR. L.J. 175, 176-78 (1985).

132. H.R. REP. NO. 595, 95th Cong., 1st Sess. 340, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6297 ("Without [the automatic stay provision of the Bankruptcy Code], certain creditors would be able to pursue their own remedies against the debtor's property. Those who acted first would obtain payment of the claims in preference to and to the detriment of other creditors.").

133. R. POSNER, *ECONOMIC ANALYSIS OF LAW* 375-76 (3d ed. 1986). Financial disaster for a debtor can be caused by creditors who seize assets in order to satisfy debts and "leave other creditors to worry about the rent." *Id.* at 375. Judge Posner writes that, "[e]ach creditor . . . will have an incentive to be first to get a judgment against the bankrupt, and the race is likely to drain the company of its assets too rapidly to maximize the value of those assets." *Id.* at 376.

134. See W. HIRSCH, *LAW AND ECONOMICS* 21-22 (2d ed. 1988).

135. Levinthal, *supra* note 128, at 225.

136. Statute of Bankrupts, 1570, 13 Eliz., ch. 7.

act of bankruptcy, including flight from creditors or the taking of sanctuary within the debtor's home, "[would] be reputed, deemed and taken for a bankrupt."¹³⁷ The court would seize the debtor's assets and the debtor would "suffer such Pains by Imprisonment of his or their Bodies, or pay such Fine to our Sovereign Lady the Queen's Majesty"¹³⁸ This statute did not provide for the bankrupt debtor's ultimate discharge to allow a fresh start, so the debtor remained fully liable until the debt was paid in full.¹³⁹

The statute particularly protected creditors from fraudulent conveyances. Fraudulent conveyances have been roughly defined as conveyances which "the object, tendency, or effect of which is to defraud another, or the intent of which is to avoid some duty or debt due by or incumbent on the party making it."¹⁴⁰

The English Parliament first addressed fraudulent transfers by "An Act against fraudulent Deeds, Alienations, & c."¹⁴¹ The Act's declared purpose was "[f]or the Avoiding and Abolishing of feigned, covinous and fraudulent Feoffments, Gifts, Grants, Alienations, Conveyances, Bonds, Suits, Judgments, and Executions, as well of Lands and Tenements as of Goods and Chattels"¹⁴² Following an increase in the number of bankruptcies, Parliament passed another statute providing for harsher penalties, in hopes of curtailing fraudulent transfers through deterrence.¹⁴³ If a court found that a debtor had "fraudulently or deceitfully" conveyed property of the estate, the debtor would "be set upon the Pillory in some publick Place for the Space of two Hours, and have one of his or her Ears nailed to the Pillory and cut off."¹⁴⁴

In a famous Star Chamber decision, *Twyne's Case*,¹⁴⁵ the court applied the English fraudulent transfer statute and found a conveyance fraudulent under a six-part test.¹⁴⁶ The court offered this advice:

137. *Id.* § IX.

138. *Id.*

139. *Id.* § X.

140. D. MOORE, A TREATISE ON FRAUDULENT CONVEYANCES AND CREDITORS' REMEDIES § 2, at 3 (1908).

141. Act against Fraudulent Deeds, Alienations, & c., 1570, 13 Eliz., ch. 5.

142. *Id.* § I.

143. An Act for the Further Description of a Bankrupt and Relief of Creditors against such as shall become Bankrupts, and for inflicting Corporal Punishment upon the Bankrupts in some Special Cases, 1623, 21 Jacob, ch. 19. For a discussion of the history of English bankruptcy law, see Levinthal, *supra* note 129, at 16-18.

144. An Act for the Further Description of a Bankrupt and Relief of Creditors against such as shall become Bankrupts, and for inflicting Corporal Punishment upon the Bankrupts in some Special Cases, 1623, 21 Jacob, ch. 19, § VII.

145. 76 Eng. Rep. 809 (1601).

146. *Id.* at 812-14. The six "badges of fraud" were:

[A]nd therefore, reader, when any gift shall be to you in satisfaction of a debt, by one who is indebted to others also; 1st, Let it be made in a public manner, and before the neighbours, and not in private, for secrecy is a mark of fraud. 2nd, Let the goods and chattels be appraised by good people to the very value, and take a gift in particular in satisfaction of your debt. 3rd, Immediately after the gift, take possession of them; for continuance of the possession in the donor, is a sign of trust. And know, reader, . . . equity requires, that such gift, which defeats others, should be made on as high and good consideration as the things which are thereby defeated¹⁴⁷

2. The Bankruptcy Reform Act of 1978¹⁴⁸

The Star Chamber's advice in *Twyne's Case* would still be sound today under section 548 of the United States Bankruptcy Code¹⁴⁹ which

1st. That this gift had the signs and marks of fraud, because the gift is general, without exception 2nd. The donor continued in possession . . . and used them as his own 3rd. It was made in secret 4th. It was made pending the writ 5th. Here was a trust between the parties . . . and fraud is always apparelled and clad with a trust, and a trust is the cover of fraud. 6th. The deed contains, that the gift was made honestly, truly and bona fide

Id. at 814. These badges of fraud were the precursors to today's statutory test for constructively fraudulent transfers. As set out in 11 U.S.C. § 548, a conveyance of property will be found constructively fraudulent if made for less than reasonably equivalent value and either: 1) was made at a time when the debtor was insolvent; or 2) left the debtor with unreasonably small capital; or 3) left the debtor unable to pay his debts as they matured. 11 U.S.C. § 548 (1988).

147. *Twyne's Case*, 76 Eng. Rep. at 814.

148. Act of Nov. 6, 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1988)). Uniform nationwide bankruptcy laws are promulgated by Congress pursuant to constitutional authorization. U.S. CONST. art. I, § 8, cl. 4. The new Title 11, the Bankruptcy Code, completely replaced the 1898 Bankruptcy Act, ch. 541, 30 Stat. 544, which had been in effect longer than the three preceding bankruptcy acts combined. The 1898 act was repealed by 11 U.S.C. § 401. 11 U.S.C. § 401 (1988). Most of the new Bankruptcy Code, excluding specific exceptions set forth in sections 402(b)-(e), became effective October 1, 1979 for all cases except those pending on September 30, 1979. See generally Klee, *Legislative History of the New Bankruptcy Code*, 54 AM. BANKR. L.J. 275, 275 n.1, 276 n.8 (1980) (setting forth brief history of various bankruptcy statutes). Congress made major amendments to the Bankruptcy Code in 1984 and 1986. R. JORDAN & W. WARREN, BANKRUPTCY 1 (2d ed. 1989).

149. 11 U.S.C. § 548 (1988). Section 548 is "derived in large part from section 67d of the Bankruptcy Act. It permits the trustee to avoid transfers by the debtor in fraud of his creditors." S. REP. NO. 989, 95th Cong., 2d Sess. 89, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5787, 5875.

Section 544(b) may also be used. It provides that the trustee may avoid any transfer by the debtor that is avoidable by an unsecured creditor under applicable law. 11 U.S.C. § 544(b) (1988). "Applicable law" under section 544(b) has been widely held to include state law. See 4 R. D'AGOSTINO & M. COOK, COLLIER ON BANKRUPTCY ¶ 544.03[1] at 544-16 (15th ed.

allows the trustee to avoid transfers of property where those transfers are deemed fraudulent.¹⁵⁰ This power enables the trustee to gather those assets which rightfully belong to the estate and distribute them equitably among the creditors.¹⁵¹ Under section 548 of the Bankruptcy Code, the FDIC might therefore be compelled to relinquish an asset acquired from a failed bank if the original transfer to the bank were deemed to have been fraudulent.¹⁵² In other words, the FDIC could thus incur fraudulent transferee liability in a suit by the trustee of a bankrupt debtor.

*Durrett v. Washington National Insurance Co.*¹⁵³ exemplifies one situation in which banks and ultimately the FDIC may be exposed to liability as a fraudulent transferee. In *Durrett*, the court found that a judicial foreclosure sale of certain real property constituted a fraudulent transfer.¹⁵⁴ The debtor had executed a note secured by a trust deed in favor of Southern Trust and Mortgage Company (Southern).¹⁵⁵ Southern assigned the trust deed to Washington National Insurance Company (Washington).¹⁵⁶ After the debtor subsequently became insolvent and

1979 & Supp. 1987). The majority of states have adopted the Uniform Fraudulent Transfer Act (UFTA). R. JORDAN & W. WARREN, *supra* note 148, at 502. Most that have not yet adopted UFTA rely upon its predecessor, the Uniform Fraudulent Conveyance Act (UFCA). *Id.* Where neither act is in effect, common law or state statute governs. *Id.*

Usually, the trustee will have satisfactory recourse under section 548 and will not have to resort to state law. *Id.* at 504. However, invocation of state law may be required where the transfer was made prior to the one-year limitation of section 548. *Id.* at 505. Under the UFTA, for example, a transfer may be avoided for up to four years after the transfer was made or the obligation incurred, or up to one year after the transfer or obligation was or could reasonably have been discovered. UNIF. FRAUDULENT TRANSFER ACT § 9, 7A U.L.A. 639, 665 (1985).

150. Courts may find a transfer fraudulent in one of two ways. Note, *Avoidance of Transfer: Section 548*, 3 BANKR. DEV. J. 389, 389 (1986). First, a transfer will be deemed fraudulent if made with the intent to hinder, delay, or defraud a creditor. 11 U.S.C. § 548(a)(1) (1988). Alternatively, a transfer will be deemed fraudulent if the debtor received less than reasonably equivalent value in exchange, *id.* § 548(a)(2)(A), and (1) was insolvent on the date of the transfer or became insolvent as a result of the transfer, *id.* § 548(a)(2)(B)(i); (2) was engaged in business or a transaction, or was about to, for which the debtor was left with unreasonably small capital following the transfer, *id.* § 548(a)(2)(B)(ii); or (3) intended to incur, or believed he or she would incur, debts beyond his or her ability to pay such debts as they matured. *Id.* § 548(a)(2)(B)(iii). In addition to transfers of property, the trustee can also avoid obligations incurred by the debtor. *Id.* § 548(a).

151. Note, *supra* note 150, at 389. For a thorough discussion of all of the trustee's avoidance powers, including the law of preferences, fraudulent transfers, and the "strong-arm clause," see Levin, *supra* note 17, at 173. See also *supra* note 22 and accompanying text.

152. See *Gallant v. Kanterman* (*In re Kanterman*), 97 Bankr. 768 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

153. 621 F.2d 201 (5th Cir. 1980).

154. *Id.* at 204.

155. *Id.* at 202.

156. *Id.*

defaulted on the note, Washington instituted foreclosure proceedings.¹⁵⁷ The only bid received at the foreclosure sale was equal to the amount owed on the note, but was less than sixty percent of the property's fair market value.¹⁵⁸

The debtor-in-possession¹⁵⁹ sued Washington to set aside the transfer of the property (resulting from the foreclosure) as a fraudulent transfer.¹⁶⁰ The *Durrett* court determined that the foreclosure sale price was less than a "fair equivalent" for the transfer of the property and that the sale was made at the time that the debtor was insolvent.¹⁶¹ Because the transfer had occurred within the necessary statutory period prior to the petition for bankruptcy,¹⁶² the court deemed the transfer avoidable.¹⁶³ Accordingly, the court ordered a rescission of the transfer.¹⁶⁴

If the FDIC had acquired such a mortgage from a failed bank and

157. *Id.* at 202-03.

158. *Id.* at 203.

159. The Bankruptcy Code allows a bankrupt debtor to function as a "trustee." See 11 U.S.C. § 321 (1988).

160. *Durrett*, 621 F.2d at 202.

161. *Id.* at 203-04. The court wrote:

We have been unable to locate a decision of any district or appellate court dealing only with a transfer of real property as the subject of attack under section 67(d) of the Act [the precursor to section 548 of the Bankruptcy Code], which has approved the transfer for less than 70 percent of the market value of the property.

Id. at 203.

162. Under the Bankruptcy Code, the trustee may avoid transfers made on or within one year of the filing of the petition for bankruptcy. 11 U.S.C. § 548(a) (1988). The court reasoned that although the actual transfer of title occurred in April of 1969, "transfer" within the contemplation of the Act, was not final until the day of the foreclosure sale, January 4, 1977." *Durrett*, 621 F.2d at 204.

163. *Durrett*, 621 F.2d at 204. The result in *Durrett* has been repeatedly criticized by members of the real property and commercial law bar. See generally Henning, *An Analysis of Durrett and its Impact on Real and Personal Property Foreclosures: Some Proposed Modifications*, 63 N.C.L. REV. 257, 272-83 (1985); Note, *The Big Chill: Applicability of Section 548(a)(2) of the Bankruptcy Code to Noncollusive Foreclosure Sales*, 53 FORDHAM L. REV. 813 (1985). Under the approach of the *Durrett* court, any purchase of property at a foreclosure sale entails uncertainty, as the property transfer might be avoided by a bankruptcy trustee for up to one year from the date of the sale. R. JORDAN & W. WARREN, *supra* note 148, at 512. This reduces both the level of participation and prices at foreclosure sales. *Id.* The lower price increases the probability that a court will find the price paid to be less than a reasonably equivalent value, and the purchased property may be lost. *Id.* This also limits the ability of lenders to effectively realize upon their security interests. *Id.* The *Durrett* result, however, has apparently been approved by Congress. In the 1984 amendments to the Bankruptcy Code, Congress included "involuntary" transfers in section 548. 11 U.S.C. § 548(a) (1988). Congress also amended section 101(50) to define a transfer as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including retention of title as a security interest and foreclosure of the debtor's equity of redemption." *Id.* § 101(50) (emphasis added).

164. *Durrett*, 621 F.2d at 204.

attempted to foreclose on the property, a court could impose fraudulent transferee liability on the FDIC and require the return of the property to the bankrupt debtor's estate. However, the FDIC would still be secured and as long as the value of the property exceeded the debt, it would be protected. A more difficult problem arises where a debtor fraudulently transfers within the statutory period, not the property, but rather the mortgage and promissory note.¹⁶⁵ Section 548 allows for the avoidance of both transfers of property and the entering into of obligations.¹⁶⁶ Thus, if the mortgage is avoided, the FDIC would lose its status as a secured creditor of the bankrupt debtor.¹⁶⁷ More problematic for the FDIC is that if the promissory note is avoided as an obligation incurred, the FDIC loses its status as a creditor of the bankrupt altogether.¹⁶⁸

These implications also manifest themselves in surety law.¹⁶⁹ Corporations regularly act as sureties for the debts of affiliates, and often grant security interests in their property to secure the debt.¹⁷⁰ If the guarantor corporation was insolvent at the time it granted the security interest or was rendered insolvent by the guaranty *and* received less than adequate consideration, a bankruptcy trustee can avoid the guaranty or security interest as a fraudulent transfer.¹⁷¹ Where a bank that subsequently fails makes a loan relying on the guarantor, and the guaranty is avoided by the bankruptcy trustee, the loss falls on the FDIC.¹⁷² The FDIC will most likely be unable to collect upon the asset from the actual debtor because if the debtor were able to pay, the bank would not have required a guarantor in the first place.

The trustee's power to avoid transfers of this sort is not unlimited, however. This Comment will analyze possible sources of FDIC protection outside the Bankruptcy Code, the extent to which they may shield the FDIC from fraudulent transferee liability, and their underlying rationale. Also, a limitation within the Bankruptcy Code itself may protect the FDIC where it has taken over a failed bank and is exposed to possible fraudulent transferee liability. As discussed later, section 550(b) of the Bankruptcy Code denies "recovery" by the trustee against a bona fide

165. See *Gallant v. Kanterman (In re Kanterman)*, 97 Bankr. 768, 772 (Bankr. S.D.N.Y.) (transfer of mortgage and promissory note), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

166. 11 U.S.C. § 548(a) (1988).

167. See R. JORDAN & W. WARREN, *supra* note 148, at 546.

168. *Id.*

169. See Carl, *Fraudulent Transfer Attacks on Guaranties in Bankruptcy*, 60 AM. BANKR. L.J. 109, 109 (1986).

170. *Id.*

171. *Id.*

172. The FDIC loses its contractual rights against the guarantor, and also loses its security interest in the property of the guarantor. R. JORDAN & W. WARREN, *supra* note 148, at 546.

purchaser for value, even where the transfer would otherwise be avoidable.¹⁷³ In some cases the FDIC may be such a bona fide purchaser for value.¹⁷⁴ The next section begins with a comparison of the competing underlying policies, and analyzes the various ways in which the FDIC might find protection.

III. ANALYSIS

A. Policy Clash and Conflict

Today, courts confront a conflict between the Bankruptcy Code's cause of action to avoid fraudulent transfers¹⁷⁵ and the protection afforded the FDIC by federal statutes¹⁷⁶ and federal common law.¹⁷⁷ This conflict actually represents a conflict in underlying policies. Two separate federal statutory schemes exist, each designed to protect (at least in part) a different class of creditors.¹⁷⁸ The powers Congress has granted to bankruptcy trustees are rooted in a desire to protect the unsecured creditors of a bankrupt debtor,¹⁷⁹ whereas the powers granted the FDIC stem from a desire to protect another group of unsecured creditors—the creditors and depositors of failed banks.¹⁸⁰

The conflict in policy interests arises where a debtor's fraudulent transfer is to a bank that has since failed and been taken over by the FDIC. A decision in favor of the FDIC, protecting it from fraudulent transferee liability, is detrimental to the interests of the unsecured creditors of the bankrupt debtor, creates uncertainty in lending, and may lead to a rise in interest rates.¹⁸¹ A decision in favor of the bankruptcy trustee

173. 11 U.S.C. § 550(b) (1988). The statute provides in pertinent part:

The trustee may not recover under subsection (a)(2) of this section from—(1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or (2) any immediate or mediate good faith transferee of such transferee.

Id.

174. For a discussion of the possible application of section 550(b) to the FDIC, see *infra* notes 354-431 and accompanying text.

175. 11 U.S.C. § 548 (1988).

176. See 12 U.S.C. § 1823(e) (as amended by FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989)).

177. See *supra* notes 62-87 and 105-25 and accompanying text.

178. Compare 11 U.S.C. §§ 101-1330 (1988) (providing for orderly collection and distribution of assets of bankrupts) with 12 U.S.C. §§ 1-4010 (1988) (regulating depository institutions).

179. R. JORDAN & W. WARREN, *supra* note 148, at 27. For a discussion of the rationale of bankruptcy law, see *supra* notes 131-35 and accompanying text.

180. Portis, *supra* note 48, at 259-60. For a discussion of the factors behind the creation of the FDIC, see *supra* notes 23-36 and accompanying text.

181. The bankruptcy trustee will be unable to recover assets that would otherwise be available for distribution to the unsecured creditors of the bankrupt debtor. As this occurs more

imposing fraudulent transferee liability on the FDIC further reduces the insurance fund and may impair the FDIC's ability to act as insurer. This conflict is exemplified in the recent case of *Gallant v. Kanterman (In re Kanterman)*.¹⁸²

In *Kanterman*, a bankruptcy trustee sought to avoid as a fraudulent transfer the debtor's execution of a mortgage on certain real property.¹⁸³ The soon-to-be-bankrupt debtor, Perri Kanterman, had mortgaged her house to secure a loan from First Inter-County Bank of New York (FICB) to Biegen, counsel for her husband's business, Gallant Securities, Inc. (GSI).¹⁸⁴ Biegen subsequently loaned a portion of the loan proceeds to GSI.¹⁸⁵

GSI subsequently defaulted on the note and FICB began foreclosure proceedings on the mortgaged property.¹⁸⁶ Kanterman then filed for bankruptcy.¹⁸⁷ Thereafter, FICB failed and was closed, and the FDIC was appointed receiver.¹⁸⁸

The FDIC, in its capacity as receiver, took over FICB's foreclosure

and more often, interest rates in the market may rise. See Schechter, *Judicial Lien Creditors Versus Prior Unrecorded Transferees of Real Property: Rethinking the Goals of the Recording System and Their Consequences*, 62 S. CAL. L. REV. 105, 125 n.64 (1988) ("to the extent that collection is uncertain, interest rates will rise overall").

182. 97 Bankr. 768 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

183. *Id.* at 770.

184. *Id.* at 771. FICB, the bank which later failed, refused to extend credit to Gallant Securities, Inc. (GSI). *Id.* at 770. FICB did, however, enter into an agreement whereby it loaned \$265,000 to Biegen, counsel for GSI. *Id.* Biegen loaned a portion of the funds to GSI, and used the balance to pay off an antecedent debt owed him by GSI. *Id.* Although Biegen thought the loan to him from FICB was to be unsecured, FICB demanded collateral and subsequently conditioned the loan on the assignment to FICB of a second mortgage on a house and land owned by Perri Kanterman. *Id.* at 771. Perri Kanterman was the wife of Donald Kanterman, who was one of GSI's two stockholders, and its Chairman of the Board. *Id.* at 770. On October 29, 1986, Kanterman executed a mortgage on the property and a mortgage note in favor of Biegen for \$265,000. *Id.* at 771. Biegen then assigned these to FICB and subsequently executed his note to FICB. *Id.* The mortgage was not recorded prior to its assignment. *Id.*

185. *Id.* at 770.

186. *Id.* In March 1987, after FICB twice returned a GSI check for insufficient funds, FICB demanded payment from Biegen for \$265,000 plus accrued interest. *Id.* at 771. Biegen in turn demanded payment from Kanterman, but to no avail. *Id.* FICB not only instituted foreclosure proceedings against the property, but also commenced a personal action against Biegen to recover on the note. *Id.* at 772.

187. *Id.* Kanterman filed a voluntary bankruptcy petition under Chapter 11 of the Bankruptcy Code. *Id.* The court later converted the case to a Chapter 7 liquidation. *Id.* Chapter 7 of the Bankruptcy Code deals with the liquidation of the assets of a debtor. 11 U.S.C. §§ 701-66 (1988). Chapter 11 of the Bankruptcy Code deals with the reorganization of the debtor's estate without a liquidation of all assets. 11 U.S.C. §§ 1101-74 (1988).

188. *Kanterman*, 97 Bankr. at 772. The New York Superintendent of Banks closed FICB on March 11, 1988, and appointed the FDIC receiver. *Id.*

action against Kanterman.¹⁸⁹ The bankruptcy trustee asserted a cross-claim, contending that the mortgage and mortgage note were voidable under New York's fraudulent conveyance law.¹⁹⁰ The trustee argued that Kanterman had given the note without fair consideration and that the execution of the note and the mortgage rendered Kanterman insolvent.¹⁹¹ Another cross-claim contended that Kanterman had conveyed the mortgage with the intent to defraud her creditors.¹⁹² Lastly, the trustee asserted that Biegen knew or should have known that Kanterman was insolvent at the time of the conveyance of the note and mortgage, or that the conveyance would render Kanterman insolvent.¹⁹³

The FDIC responded that both the *D'Oench, Duhme*¹⁹⁴ doctrine and section 1823(e) of the Federal Deposit Insurance Act¹⁹⁵ barred the trustee from avoiding the FDIC's interest in the mortgage.¹⁹⁶ The FDIC further argued that its status as a bona fide purchaser for value protected the mortgage lien even if the transfer were otherwise avoidable.¹⁹⁷ Finally, the FDIC contended that FICB was a holder-in-due-course of the mortgage note, and, under the shelter doctrine,¹⁹⁸ the debtor's obligation

189. *Id.*

190. *Id.* Sections 270 through 281 of the New York Debtor and Creditor Law contain the New York codification of the Uniform Fraudulent Conveyance Act. N.Y. DEBT. & CRED. LAW §§ 270-281 (Consol. Supp. 1989). Section 276 is similar to section 548(a)(1) of the Bankruptcy Code and provides: "Every conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors." *Id.* § 276. Section 273 is similar to section 548(a)(2)(B)(i) of the Bankruptcy Code and provides, "Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration." *Id.* § 273. Section 272 defines when consideration is fair:

a) When in exchange for such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed or an antecedent debt is satisfied, or b) When such property, or obligation is received in good faith to secure a present advance or antecedent debt in amount not disproportionately small as compared with the value of the property or obligation obtained.

Id. § 272. Section 275 is similar to section 548(a)(2)(B)(iii) of the Bankruptcy Code and provides, "Every conveyance made and every obligation incurred without fair consideration when the person making the conveyance or entering into the obligation intends or believes that he will incur debts beyond his ability to pay as they mature, is fraudulent as to both present and future creditors." *Id.* § 275.

191. *Kanterman*, 97 Bankr. at 772.

192. *Id.*

193. *Id.* at 772-73.

194. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942).

195. 12 U.S.C. § 1823(e) (1988).

196. *Kanterman*, 97 Bankr. at 773-74.

197. *Id.* at 773.

198. See generally U.C.C. § 3-305 & comment 1 (1987) (holder-in-due-course rule applies equally to any transferee who acquires rights).

could not be avoided.¹⁹⁹

Kanterman raises all of the factors courts confront in seeking to resolve problems in this area: the extent of the trustee's avoidance powers;²⁰⁰ possible application of *D'Oench, Duhme* and section 1823(e);²⁰¹ possible holder-in-due-course status for the FDIC;²⁰² and use of a bona fide purchaser for value defense under section 550(b) of the Bankruptcy Code.²⁰³ Underlying any analysis of these problems is the concern that if neither Congress nor the courts protect the FDIC, possible fraudulent transferee liability will impair the FDIC's ability to perform its role as insurer.²⁰⁴ The role of the bankruptcy trustee in the representation of unsecured creditors, however, perhaps merits equivalent concern.²⁰⁵

The judiciary must reconcile the competing statutory goals by deciding to what extent the FDIC should be protected from fraudulent transferee liability under the Bankruptcy Code. To do so, courts must determine the relative weight to be accorded the underlying policies in conflict, paying particular attention to discernible congressional intent.

The federal policy in favor of the FDIC is clear. Congress has consistently emphasized the importance of the FDIC's role.²⁰⁶ Courts, ac-

199. *Kanterman*, 97 Bankr. at 773.

200. *Id.* at 777.

201. *Id.* at 775-76.

202. *Id.* at 775.

203. *Id.* at 777-80.

204. For a discussion of the effect of fraudulent transferee liability on the FDIC as insurer, see *infra* notes 448-73.

205. One commentator notes that, "[i]n a collective proceeding the trustee, in the name of order and economy, may act as agent for creditors in asserting the various rights different creditors have, many of which may overlap." T. JACKSON, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* 80 (1986).

206. The federal legislation creating the FDIC declares as its purpose: "To provide for the safe and more effective use of the assets of banks, to regulate interbank control, to prevent the undue diversion of funds into speculative operations and for other purposes." Banking Act of 1933, Pub. L. No. 73-66, ch. 89, 48 Stat. 162, 162 (codified in scattered sections of 12 U.S.C.).

The legislative history of the 1950 amendments to the Federal Reserve Act note that the "results since [the creation of the FDIC] bespeak the outstanding record the [FDIC] has achieved in bringing to depositors sound, effective, and uninterrupted operation of the banking system with resulting safety and liquidity of such deposits." H.R. REP. NO. 2564, 81st Cong., 2d Sess. 1, reprinted in 1950 U.S. CODE CONG. & ADMIN. NEWS 3765, 3765-66.

The legislative history of FIRREA chronicles recent congressional concern. It notes that, "[c]onsumer confidence in the nation's savings and loan system has been declining rapidly over the last several months; consumer fears about the stability of the system have resulted in record withdrawals." H.R. REP. NO. 54(I), 101st Cong., 1st Sess. 305, reprinted in 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 101. The House Report goes on to state:

Low depositor confidence in savings and loans as evidenced by record deposit outflow, the need to combat fraud and insider abuse, coupled with the severe insolvency of FSLIC, make the immediate resolution of the crisis imperative The need for this legislation is clear. The Administration and the Congress must restore public

knowledging this, have noted the compelling nature of the federal policy to promote stability and confidence in the United States banking industry.²⁰⁷

The Bankruptcy Code embodies equally important federal policies.²⁰⁸ Without it, creditors have an incentive to attempt to collect as much as possible individually, to the detriment of the debtor and other creditors.²⁰⁹ This federal statutory scheme is predicated on collectivism²¹⁰ and solving the problem of creditors depleting the "common pool."²¹¹

confidence in the savings and loan industry . . . "Never Again," the theme of the committee's deliberations, is reflected by numerous provisions of the bill which provide for the early detection of problems in financial institutions and the prevention of losses to the deposit insurance fund and the United States Treasury.

Id. at 305-10, reprinted in 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 101-06.

207. See, e.g., *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 442, 457 (1942); *Holt v. FDIC (In re CTS Truss)*, 859 F.2d 357, 361 (5th Cir. 1988), modified in part, 868 F.2d 146 (5th Cir. 1989); *FDIC v. McClanahan*, 795 F.2d 512, 515 (5th Cir. 1986); *FDIC v. Wood*, 758 F.2d 156, 160 (6th Cir.), cert. denied, 474 U.S. 944 (1985); *FDIC v. Gulf Life Ins. Co.*, 737 F.2d 1513, 1517 (11th Cir. 1984); *Gunter v. Hutcheson*, 674 F.2d 862, 870 (11th Cir.), cert. denied, 459 U.S. 826 (1982); *Howell v. Continental Credit Corp.*, 655 F.2d 743, 746 (7th Cir. 1981); *Chatham Ventures, Inc. v. FDIC*, 651 F.2d 355, 363 (5th Cir. Unit B July 1981), cert. denied, 456 U.S. 972 (1982); *First State Bank v. United States*, 599 F.2d 558, 562 (2d Cir. 1979), cert. denied, 444 U.S. 1013 (1980); *FDIC v. Godshall*, 558 F.2d 220, 221 (4th Cir. 1977); *Doherty v. United States*, 94 F.2d 495, 497 (8th Cir.), cert. denied, 303 U.S. 658 (1938).

208. Bankruptcy law must be federal in nature, due to the constitutional limits on the territorial power of state courts under our federalist system. T. JACKSON, *supra* note 205, at 3 n.4. The rights of creditors would otherwise be difficult to resolve because a typical credit transaction may involve a debtor residing in one state, owning property in another, and a lender from a third. *Id.*

209. *Id.* Creditors able to collect from the debtor first have an advantage over late-comers. As one commentator notes: "It is like buying tickets for a popular rock event or opera: the people first in line get the best seats; those at the end of the line may get nothing at all." *Id.* See also R. POSNER, *supra* note 133, at 375-76. Unfortunately, "[t]his decision by numerous individual creditors . . . may be the wrong decision for the creditors as a group. Even though the debtor is insolvent, they might be better off if they held the assets together." T. JACKSON, *supra* note 205, at 12. The aggregate value of assets is often higher when they are kept together in groups, such as a printing press with custom dies. *Id.* at 15.

210. "Collectivism" refers to the underlying basis for bankruptcy law, the advantages of a collective and compulsory adjudication of the debtor's rights. T. JACKSON, *supra* note 205, at 13.

211. T. JACKSON, *supra* note 205, at 10-19. The "common pool" problem is the tendency of each creditor to act to the detriment of other creditors by harassing and attacking the debtor in an effort to collect more than anyone else. *Id.*

A typical common pool example involves the hunting of whales. If one person owned the property rights to all whales, care would be taken to avoid the hunting of them to the point of extinction, so as to avoid the depletion of the resource and ensure continued financial return in the future. However, where no single person has exclusive rights to hunt whales, each whale-hunter has an incentive to kill as many as possible, before others do. See *id.* at 11-12. This is highly inefficient and means that "there will be no [whales]—and no money—in future years." *Id.* at 12.

This "common pool" justification, a justification critical to the policies behind bankruptcy laws, arguably does not extend to the law of fraudulent transfers.²¹² Bankruptcy, most notably in the law of preferences, protects creditors vis-a-vis other creditors.²¹³ In contrast, the ability to avoid fraudulent transfers protects creditors from actions of the debtor.²¹⁴ Thus, it has been argued that fraudulent transferee liability "does not spring from a need to implement bankruptcy's collective proceedings," but rather only adjusts the rights of creditors vis-a-vis the debtor.²¹⁵

Concededly, it may be more convenient to adjudicate all claims against the debtor in one judicial proceeding, and therefore the fraudulent transfer provisions of the Bankruptcy Code are well placed.²¹⁶ However, even though these provisions are found in the federal statute, when weighing the federal policies behind each of the statutory schemes that conflict in *Kanterman*, courts should consider that fraudulent transferee liability is rooted in a more traditional state-law justification, determining debtor-creditor rights, rather than the overriding federal interests of resolving the "common pool" problem found in other Bankruptcy Code provisions.²¹⁷ As one commentator notes, fraudulent conveyance law is "part of the warp and woof of debtor-creditor relations; in terms of bankruptcy law it should be seen as part of the initial establishment of entitlements, not as something that bankruptcy policy should itself have anything to say about."²¹⁸ If so, the overriding federal interests in protecting the FDIC should prevail over the traditional justifications which underlie bankruptcy law in general.

The United States Supreme Court resolved a similar conflict under the Bankruptcy Code in *Midlantic National Bank v. New Jersey Department of Environmental Protection*.²¹⁹ There, the Court held that section

212. *Id.* at 146.

213. *Id.*

214. *Id.* This is fundamentally a state-law concern with debtor-creditor relations and the interests in keeping monitoring costs down to creditors.

215. *Id.* The argument continues:

[S]ince fraudulent conveyance law springs from an entirely different source, its separate existence in a bankruptcy statute is more problematic. It would then need to be justified on the ground of administrative convenience: that, like claims estimation procedures, it unified and simplified the rules of fifty discrete states. Yet this justification still depends on bankruptcy law's implementing state policy in a rule-oriented fashion, not deliberately changing it.

Id. at 147.

216. *Id.*

217. *Id.* at 146-50.

218. *Id.* at 148.

219. 474 U.S. 494 (1986).

554(a) of the Bankruptcy Code, which authorizes a trustee to abandon any property burdensome to the estate,²²⁰ does not allow a trustee to abandon property containing hazardous waste in violation of state health and safety laws.²²¹ Section 554(a), the court observed, was unambiguous on its face,²²² but conflicted with important state and federal interests.²²³ The Court noted that pre-Code doctrine, for the purpose of protecting legitimate state or federal interests, limited the trustee's authority to dispose of property.²²⁴

However, the *Midlantic National Bank* holding did not "rest solely, or even primarily, on a presumption of continuity with pre-Code practice."²²⁵ Rather, the Court concluded that a contrary interpretation of section 554(a) would be inconsistent with other sections of the Code which support the principle that "the trustee is not to have *carte blanche* to ignore nonbankruptcy law."²²⁶ The Court also noted Congress' repeated emphasis on the importance of environmental legislation, both state and federal, in protecting against toxic pollution.²²⁷ Allowing such abandonment would be "an extraordinary exemption from nonbankruptcy law."²²⁸ Before this exemption can occur, the Court stated, there must be an extremely clear expression of congressional intent.²²⁹

Similar reasoning should be employed to determine the extent of the FDIC's protection from fraudulent transferee liability. Like the Bankruptcy Code section at issue in *Midlantic National Bank*, section 548 is unambiguous on its face.²³⁰ Yet using section 548 against the FDIC conflicts with an important federal interest, i.e., ensuring the viability of the

220. 11 U.S.C. § 554(a) (1988).

221. *Midlantic Nat'l Bank*, 474 U.S. at 507.

222. *Id.* at 505.

223. *Id.* at 506-07.

224. *Id.* at 500.

225. *United States v. Ron Pair Enters.*, 109 S. Ct. 1026, 1032 (1989) (explaining basis for *Midlantic Nat'l Bank* holding).

226. *Midlantic Nat'l Bank*, 474 U.S. at 502.

227. *Id.* at 505.

228. *Id.* at 501.

229. *Id.*

230. Section 548 provides in pertinent part:

- (a) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily
 - (1) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud [a creditor] . . . ; or
 - (2)(A) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
 - (B) (i) was insolvent on the date that such transfer was made or such obligation was incurred or became insolvent as a result . . . ;

FDIC. While Congress could legislate which federal policy should prevail, it would seem that Congress, by repeatedly emphasizing the importance of the federal interest advanced by the FDIC, has acted in this area with sufficient clarity for the courts to resolve the matter.²³¹ Under the rationale of *Midlantic National Bank*, it would be inappropriate to permit a bankruptcy trustee to undermine the purpose behind the FDIC by subjecting it to fraudulent transferee liability without clear congressional intent. The following sections analyze the various ways in which the FDIC might find shelter from such liability.

B. Does the D'Oench, Duhme Doctrine Bar FDIC Liability?

The court in *Gallant v. Kanterman (In re Kanterman)*²³² faced a question of first impression: whether *D'Oench, Duhme*²³³ protection of the FDIC precludes a trustee in bankruptcy from setting aside, as a fraudulent conveyance, a mortgage held by the FDIC as the receiver of a failed bank.²³⁴ The *Kanterman* court noted other courts' application of both *D'Oench, Duhme* and section 1823(e)²³⁵ to preclude "assertion of defenses based on separate secret agreements in actions brought by the FDIC seeking to enforce unconditional notes and guarantees."²³⁶ However, the court determined that since the FDIC had sued in its capacity as receiver and had not alleged that it had purchased the mortgage and promissory note in its corporate capacity,²³⁷ section 1823(e) did not apply.²³⁸ While true at the time of the court's decision, this is no longer the case, as Congress has extended the protection of section 1823(e) to the FDIC as receiver.²³⁹

(ii) was engaged in business . . . for which any property remaining with the debtor was an unreasonably small capital; or

(iii) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

11 U.S.C. § 548 (1988).

231. See generally FIRREA, Pub. L. No. 101-73, 103 Stat. 183 (1989) (reforming savings and loan industry). In congressional hearings, Representative Leach expressed concern over the size of the FDIC's insurance fund, noting, "the insurance fund is the last defense protecting the taxpayer from an industry's balance sheets. Once the fund is depleted, taxpayers become liable for all future losses. Therefore, it's imperative the Congress ensure that the fund has adequate resources." *Hearings, supra* note 1 (statement of Rep. Leach).

232. 97 Bankr. 768 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

233. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942).

234. *Kanterman*, 97 Bankr. at 774-75.

235. 12 U.S.C. § 1823(e) (1988).

236. *Kanterman*, 97 Bankr. at 775 (citation omitted).

237. *Id.* at 772.

238. *Id.* at 774.

239. See FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823(e)). Previously, courts had reasoned that

In attempting to apply the *D'Oench, Duhme* doctrine, the court found "contours limiting [the doctrine's] application" primarily to situations involving a secret agreement.²⁴⁰ The court could find only one case where the FDIC had sued on a note as receiver and where the court had extended *D'Oench, Duhme* "beyond arrangements characterized as secret agreements."²⁴¹

In the case cited by the court, *FDIC v. McClanahan*,²⁴² the FDIC sued on a promissory note which the maker had recklessly signed when blank and had delivered to a man known to have been convicted of bank fraud.²⁴³ The Fifth Circuit held that by this conduct the maker lent himself to a "scheme or arrangement" likely to mislead the FDIC.²⁴⁴ Similarly, in *Kanterman*, since the FDIC sought to invoke estoppel in the absence of a secret agreement, applicability turned upon the defendant's behavior.²⁴⁵ The *Kanterman* court started with the proposition that where the defendant was "wholly innocent and not reckless," *D'Oench, Duhme* protection would not apply.²⁴⁶ The court's statement apparently stems from the underlying rationale of *D'Oench, Duhme*, which allowed estoppel where the defendant "lent himself to a scheme or arrangement whereby the banking authority on which respondent relied in insuring the bank was or was likely to be misled."²⁴⁷

Following this reasoning, the *Kanterman* court refused to give the

[w]hen the FDIC is functioning as receiver of a state bank it is not entitled to the protection of the FDIC in its corporate capacity, acting as insurer of a failed bank. If the FDIC took over the Bank as receiver, the FDIC merely steps into the bank's shoes and can only assert the same defenses [as are] available to the bank.

Evans v. Robbins (*In re Robbins*), 91 Bankr. 879, 888 (Bankr. W.D. Mo. 1988) (citation omitted). Accordingly, the *Kanterman* court looked only to the common-law *D'Oench, Duhme* doctrine. *Kanterman*, 97 Bankr. at 774.

240. *Kanterman*, 97 Bankr. at 775-76. The court in *FDIC v. McClanahan* noted the existence of these "contours." 795 F.2d 512, 515 (5th Cir. 1986). There the court wrote:

D'Oench, Duhme has not been read to mean that there can be no defenses at all to attempts by the FDIC to collect on promissory notes. For example, the FDIC does not contend that it could have sued McClanahan on the \$86,000 note to which his signature had been forged. Similarly, where the note imposes bilateral obligations on the parties, rather than creating a unilateral obligation by the maker to pay a sum certain, courts have held that the maker may defend himself by contending that the bank breached its obligations under the note.

Id. The court went on to hold that the defendant was estopped from defending himself on grounds of failure of consideration, due to the recklessness of his conduct. *Id.* at 516-17.

241. *Kanterman*, 97 Bankr. at 776 (citing *FDIC v. McClanahan*, 795 F.2d 512 (5th Cir. 1986)).

242. 795 F.2d 512 (5th Cir. 1986).

243. *Id.* at 513.

244. *Id.* at 517.

245. *Kanterman*, 97 Bankr. at 776.

246. *Id.*

247. *D'Oench, Duhme*, 315 U.S. at 460.

FDIC *D'Oench, Duhme* protection in the context of a fraudulent conveyance by a now-bankrupt debtor.²⁴⁸ This conclusion, the court stated, rested on the fact that the trustee's right of recovery did not depend upon the existence of a secret agreement.²⁴⁹ The court noted that a trustee's right to avoid a transfer of a property interest under the Bankruptcy Code arises by operation of law,²⁵⁰ and "not due to an agreement or a condition to an agreement."²⁵¹ Accordingly, as the trustee was a "wholly innocent" representative of the debtor's creditors, the court held there was no support for an application of estoppel to the trustee.²⁵²

The analysis used in *Kanterman* produced a result contrary to the congressional intent supporting the federal policy enunciated by the United States Supreme Court in *D'Oench, Duhme*.²⁵³ This policy embodied a desire to protect the FDIC in both its corporate capacity and as receiver.²⁵⁴ The recent amendment to section 1823(e), extending protection to the FDIC as receiver, evinces this desire.²⁵⁵ Thus, the result reached by the *Kanterman* court is insupportable.

As set out in *Kanterman*, the test to determine *D'Oench, Duhme*'s applicability has two parts.²⁵⁶ First, a court must determine whether a

248. *Kanterman*, 97 Bankr. at 777.

249. *Id.*

250. *Id.* (citing N.Y. DEBT. & CRED. LAW §§ 270-281 (Consol. Supp. 1989)).

251. *Id.* This conclusion was echoed by the district court on appeal. *Gallant v. Kanterman* (*In re Kanterman*), 108 Bankr. 432, 434 (S.D.N.Y. 1989).

252. *Kanterman*, 97 Bankr. at 776. In *FDIC v. Meo*, 505 F.2d 790 (9th Cir. 1974), the court employed similar reasoning. In *Meo*, the FDIC sued upon a promissory note it held as receiver of the failed San Francisco National Bank (SFNB). *Id.* at 791. The obligor on the note, Meo (along with three associates), had executed the note to finance a purchase of 1000 shares of SFNB's common stock. *Id.* SFNB, however, failed to properly execute the stock order and instead issued 1000 voting trust certificates in the name of the purchasers. *Id.* The bank held these certificates as collateral for the loan. *Id.* Neither Meo, nor his associates, ever saw them. *Id.* Later, when Meo and his associates became concerned with the bank's solvency, they considered selling their stock. *Id.* Although Meo's three associates did sell, Meo (unaware of the misexecution of the stock purchase order) executed a new note for his share of the balance on the original note. *Id.*

The Ninth Circuit refused to apply *D'Oench, Duhme* protection to the FDIC and did not estop Meo from asserting a failure of consideration. *Id.* at 791-92. The court found that Meo was a bona fide purchaser-borrower, observing that, "he did not enter into any scheme or secret agreement whereby the assets of the bank would be overstated; he was wholly innocent of the wrongful action of SFNB in issuing voting trust certificates instead of common stock shares . . ." *Id.* at 792. Thus, *D'Oench, Duhme* protection, by its own terms, did not apply. *Id.*

253. See *D'Oench, Duhme*, 315 U.S. at 459.

254. *Id.* at 457.

255. See FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823).

256. See *Kanterman*, 97 Bankr. at 775-76.

secret agreement likely to mislead banking authorities exists.²⁵⁷ Second, if there is no secret agreement, the court must determine whether the behavior of the obligor was "wholly innocent."²⁵⁸ If there is no secret agreement and the obligor is "wholly innocent," the FDIC may not raise *D'Oench, Duhme*.²⁵⁹ As the following discussion shows, the *Kanterman* court erred in its application of both parts of the analysis.

1. Are fraudulent transfers "secret agreements" within the meaning of the *D'Oench, Duhme* doctrine?

The *Kanterman* court began by noting that section 1823(e) did not protect the FDIC in its capacity as receiver.²⁶⁰ However, the court then went on to apply section 1823(e) by looking for evidence of "secret agreements."²⁶¹ The broader protection which *D'Oench, Duhme* and its progeny afford the FDIC, however, extends not only to secret agreements, but also to "scheme[s] or arrangement[s] whereby the [FDIC is] or [is] likely to be misled."²⁶² The question thus becomes whether a debtor's avoidable fraudulent transfer could (or should) be characterized as part of a "scheme or arrangement" likely to mislead the banking authorities.

Where a debtor transfers an interest in property and the transfer is later deemed fraudulent and thus avoidable, the effect of the transfer is to mislead the banking authorities, and as such it falls within the rubric of a "scheme or arrangement" as contemplated by the *D'Oench, Duhme*

257. *Id.*

258. *Id.* at 776.

259. *Id.* The FDIC appealed the decision of the bankruptcy court in *Kanterman*. *Gallant v. Kanterman (In re Kanterman)*, 99 Bankr. 208, 210 (S.D.N.Y. 1989) (granting leave to appeal). The decision was later affirmed in a brief opinion by the district court. *Gallant v. Kanterman (In re Kanterman)*, 108 Bankr. 432 (S.D.N.Y. 1989). The district court used the same two-part test. *Id.* at 434-35. The court first held that the trustee's claims did not rest upon any agreement, secret or otherwise. *Id.* at 434. The court held, "when the trustee is asserting claims for fraudulent conveyance, those defenses arise by operation of law and not on account of any secret agreement between the debtor and the bank." *Id.* While noting other courts' application of the second part of the test, the court declined to rule as to whether the debtor had engaged in reckless conduct or whether that conduct could be attributed to the trustee. *Id.* at 435. The court's refusal to consider the question was due to the FDIC's failure to allege any facts on this point in its summary judgment motion. *Id.*

260. *Kanterman*, 97 Bankr. at 776. Section 1823(e) now applies by virtue of the amendments contained within FIRREA. Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823(e)).

261. *Kanterman*, 97 Bankr. at 776-77.

262. *D'Oench, Duhme*, 315 U.S. at 460; see *Black v. FDIC*, 640 F.2d 699 (5th Cir. Unit B Mar.) (oral agreement that bank would make construction loans unenforceable against FDIC), *cert. denied*, 454 U.S. 838 (1981); *Chatham Ventures, Inc. v. FDIC*, 651 F.2d 355 (5th Cir. Unit B July 1981) (oral joint venture agreement that bank would advance obligors additional funds unenforceable against FDIC), *cert. denied*, 456 U.S. 972 (1982). For a discussion of the scope of the statute's protection, see *supra* notes 88-104 and accompanying text.

Court.²⁶³ Although the usual *purpose* behind a debtor's fraudulent transfer of property is to deceive the debtor's creditors and not the FDIC,²⁶⁴ the transfer's *effect* is to mislead the banking authorities. The possible avoidance of a debtor's fraudulent transfer means that any FDIC reliance on the lending bank's books for the true value of the bank's assets may be misplaced. The *D'Oench, Duhme* Court noted that "[t]he test is whether the note was designed to deceive the creditors or the public authority, or would tend to have that effect."²⁶⁵ The Court went on to emphasize that whether the FDIC was actually misled was irrelevant.²⁶⁶ Hence, a debtor's fraudulent transfer, the *effect or possible effect* of which is to mislead banking authorities in the appraisal of the bank's assets, should accordingly trigger *D'Oench, Duhme* protection. Such a rule is consistent with *D'Oench, Duhme*'s purpose—to permit the FDIC to make accurate appraisals of the value of a bank's assets based on the bank's records.²⁶⁷

2. Is the obligor's conduct relevant?

Even where a court declines to characterize the debtor's fraudulent transfer as a "secret agreement" or a "scheme or arrangement" likely to mislead banking authorities, correct application of the second part of the analysis will still provide *D'Oench, Duhme* protection to the FDIC. In *D'Oench, Duhme*, the Court focused on the conduct of the "maker" of

263. A fraudulent transfer cannot possibly be characterized as the "ordinary and good-faith commercial transactions" of which the *D'Oench, Duhme* Court wrote. *D'Oench, Duhme*, 315 U.S. at 474 (Jackson, J., concurring).

264. See generally 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 548.02, at 548-33 to -37 (discussing nature of intent required). Since actual intent to defraud is rarely easy to show, the UFTA incorporated eleven "badges of fraud" as factors a court may consider. UNIF. FRAUDULENT TRANSFER ACT § 4(b), 7A U.L.A. 639, 652-53 (1985). These "badges" are: (1) whether the transfer was to an insider; (2) whether the debtor retained possession or control of the property; (3) whether the transfer was disclosed or concealed; (4) whether before the transfer was made, the debtor had been sued or threatened with suit; (5) whether the transfer was of substantially all of the debtor's assets; (6) whether the debtor absconded; (7) whether the debtor removed or concealed assets; (8) whether the consideration was a reasonable equivalent; (9) whether the debtor was insolvent or becomes insolvent shortly before or after the transfer; (10) whether the transfer occurred shortly before or after a substantial debt was incurred; and, (11) whether the debtor transferred the essential assets of the business to a lienor who then transferred them to an insider. *Id.*

265. *D'Oench, Duhme*, 315 U.S. at 460 (emphasis added). The defendant's conduct in *D'Oench, Duhme* proved to have a "direct and independent" effect on the FDIC, thus supporting application of estoppel. *Id.* at 474 (Jackson, J., concurring).

266. *Id.* at 459. In fact, at the time the defendant in *D'Oench, Duhme* executed the note in place of the defaulted bonds, the Act creating the FDIC had not even been passed. *Id.*

267. *Id.* at 472 (Jackson, J., concurring).

the note.²⁶⁸ The *Kanterman* court wrote that in the absence of a secret agreement, courts should look to the behavior of the *defendant*.²⁶⁹ As evidenced by *Kanterman*'s facts, though, in later litigation involving the enforceability of a note, the defendant will not always be the "person" who originally misled the banking authorities.²⁷⁰ Even where the defendant is not that "person," however, the policy behind *D'Oench, Duhme* still mandates the doctrine's application to this different defendant.

Although in the absence of a secret agreement *D'Oench, Duhme* protection is premised on the debtor's behavior, courts do not protect the FDIC in order to punish the debtor.²⁷¹ The protection issues, rather, to ensure that the FDIC can rely on its valuation of a bank's assets.²⁷² In *D'Oench, Duhme*, the United States Supreme Court applied federal common law specifically chosen to further the policies behind the FDIC.²⁷³ The Court emphasized that those policies would be furthered *only* if the FDIC could "rely on the integrity of banking statements and banking assets."²⁷⁴ In *D'Oench, Duhme*, the FDIC sued on a note that was an asset of the bank at the time the FDIC insured the bank.²⁷⁵ The FDIC was thus not only deceived "for the single day on which the note was delivered; [the note's] purpose *and its effect* were to operate as a continuing inducement to existing creditors, and to those who might become creditors, to rely on this note"²⁷⁶ In order to defend against such deception and due to the "comprehensive public character of its function," the FDIC holds more rights than an ordinary creditor.²⁷⁷

The policy allowing for FDIC reliance is no less compelling where a bankruptcy trustee subsequently seeks to avoid a note.²⁷⁸ If the policy

268. *Id.* at 460.

269. *Kanterman*, 97 Bankr. at 776.

270. *Id.* at 773. In *Kanterman*, the defendant was the trustee of the bankrupt debtor's estate. *Id.*

271. In fact, the Court in *D'Oench, Duhme* noted that obligors have been held liable even where they "had no positive idea of committing fraud upon anyone, . . . were very ignorant and ill-informed of the character of the transaction, . . . and may not have intended to deceive any person" *D'Oench, Duhme*, 315 U.S. at 458-59 (citations omitted).

272. *Id.* at 472 (Jackson, J., concurring).

273. *Id.* (Jackson, J., concurring).

274. *Id.* (Jackson, J., concurring).

275. *Id.* at 454.

276. *Id.* at 472-73 (Jackson, J., concurring) (emphasis added).

277. *Id.* at 474 n.15 (Jackson, J., concurring); Norcross, *supra* note 6, at 323-24; Portis, *supra* note 48, at 262.

278. The district court in *Kanterman* noted, before ruling against the FDIC, that the "trustee's ability to avoid a facially valid mortgage *may mislead the banking authorities* when evaluating the credit worthiness of an insured banking institution" *Kanterman*, 108 Bankr. at 435 (emphasis added).

has any force, it must apply uniformly whenever wrongful behavior in the making of the note is manifest, regardless of who is later named as defendant.²⁷⁹ The *D'Oench, Duhme* opinion supports this view, as evidenced by the Court's focus on the likelihood that the misleading "acts" would interfere with important federal policies; the Court did not focus on the identity or personal responsibility of the perpetrators.²⁸⁰ The Court emphasized that "it is the 'evil tendency' of the acts to contravene the policy governing banking transactions which lies at the root of the rule [extending protection to the FDIC]."²⁸¹

C. Does Section 1823(e) Bar FDIC Liability?

As noted above,²⁸² the court in *Gallant v. Kanterman (In re Kanterman)*²⁸³ refused to apply section 1823(e) because the FDIC had brought suit in its capacity as receiver.²⁸⁴ However, following the enactment of FIRREA, section 1823(e) is directly on point and should be applied whether the FDIC sues in its corporate capacity or as receiver.²⁸⁵

1. Are fraudulent transfers "secret agreements" within the meaning of section 1823(e)?

When seeking to apply section 1823(e), courts must answer a question similar, but not identical, to the one facing courts attempting to apply the common-law *D'Oench, Duhme* doctrine: Is a debtor's avoidable fraudulent transfer a "secret agreement" within the meaning of section 1823(e)?²⁸⁶

The United States Supreme Court has extended the definition of "agreement" under section 1823(e) so that it is at least as inclusive as that under the common-law *D'Oench, Duhme* doctrine.²⁸⁷ In defining

279. The district court in *Kanterman* expressly declined to rule on whether reckless behavior by the debtor, if proved, could be imputed to the trustee due to the FDIC's failure to allege such reckless conduct. *Id.*

280. *D'Oench, Duhme*, 315 U.S. at 459.

281. *Id.* (emphasis added).

282. See *supra* note 237-38 and accompanying text.

283. 97 Bankr. 768 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

284. *Id.* at 774.

285. FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823(e)).

286. See *Langley v. FDIC*, 484 U.S. 86 (1987) (defining term "agreement" in section 1823(e)).

287. *Id.* at 92-93. In *Langley*, the Court wrote: "We can safely assume that Congress did not mean 'agreement' in [section] 1823(e) to be interpreted so much more narrowly than its permissible meaning as to disserve the principle of the leading case applying that term to FDIC-acquired notes." *Id.* Furthermore, section 1823(e) is not limited to situations in which

"agreement" under the statute, the Court has attempted to ensure that section 1823(e) advances its intended purposes.²⁸⁸ One of these purposes, as noted above,²⁸⁹ is to allow the FDIC to "rely on a bank's records in evaluating the worth of the bank's assets."²⁹⁰ Other courts, in interpreting the meaning of the statute, have considerably extended the holding of *D'Oench, Duhme* and the protection afforded by the statute.²⁹¹

The bankruptcy court in *Kanterman*, however, in a view echoed by the district court on appeal,²⁹² found that a fraudulent transfer could not be a "secret agreement" since it arose by operation of law and not through a transaction between the debtor and the bank.²⁹³ This view, however, ignored the obvious. The term "secret agreement" must be defined with reference to the purpose of the statute, namely the avoidance of "a scheme or arrangement whereby the banking authority . . . [is] or [is] likely to be misled."²⁹⁴ Accordingly, the analysis in this Comment's preceding section, concluding that fraudulent transfers are "secret agreements" which are likely to "mislead banking authorities,"²⁹⁵ applies with equal force to section 1823(e). A court's refusal to extend the definition in the fraudulent transfer context defeats the statute's goal of preventing the inaccurate valuation of bank assets.²⁹⁶

a deceptive scheme is involved as it simply disallows enforcement of oral agreements. Portis, *supra* note 48, at 264.

288. *Langley*, 484 U.S. at 91.

289. *See supra* notes 101-03 and accompanying text.

290. *Langley*, 484 U.S. at 91.

291. *See, e.g., Holt v. FDIC (In re CTS Truss, Inc.)* 868 F.2d 146, 150 n.8 (5th Cir. 1989) ("holding of *D'Oench, Duhme* has been extended considerably by courts in interpreting the plain meaning of 12 U.S.C. § 1823(e)" (citations omitted)). *See also* *FDIC v. First Mortgage Investors*, 485 F. Supp. 445, 452 (E.D. Wis. 1980) ("Congress, in passing . . . 1823(e), expanded on the protections afforded to the FDIC by *D'Oench*."). One commentator has written that Congress' attempt to codify the *D'Oench, Duhme* doctrine was in fact an attempt to limit the Supreme Court's holding. Norcross, *supra* note 6, at 328. The legislative history shows that the statute's authors never meant to grant the FDIC a position stronger than that of the failed bank. *Id.* (citing 86 CONG. REC. 10,731 (1950) (statement of Rep. Walter)). For a summary of the legislative history of section 1823(e), see Note, *supra* note 5, at 275-79.

292. *See* *Gallant v. Kanterman (In re Kanterman)*, 108 Bankr. 432, 434 (S.D.N.Y. 1989).

293. *Kanterman*, 97 Bankr. at 776-77.

294. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 460 (1942).

295. *See supra* notes 260-67 and accompanying text.

296. *See Langley*, 484 U.S. at 91-92 (purpose of section 1823 is to allow bank examiners to rely on bank's records). The district court in *Kanterman*, however, interpreted *Langley* differently and narrowed the definition of agreement under the statute. 108 Bankr. at 434. The court quoted the Supreme Court's language that the "common meaning of the word 'agreement' must be assigned to its usage in [section] 1823(e)." *Id.* (quoting *Langley v. FDIC*, 484 U.S. 86, 91 (1987)). Accordingly, the *Kanterman* court looked for a meeting of the minds between the parties involved, or some sort of explicit or implicit understanding. *Id.* Finding none, the court held that section 1823(e) did not protect the FDIC. *Id.* at 435.

2. Is the conduct of the obligor relevant?

If the *trustee's* misconduct does not matter (as opposed to the *bankrupt-debtor's* misconduct) when courts apply the common-law *D'Oench, Duhme* doctrine,²⁹⁷ the defendant's misconduct should be equally irrelevant when a court proceeds under section 1823(e).²⁹⁸ A careful reading of the statute supports this result.²⁹⁹ Congress, in codifying the common-law *D'Oench, Duhme* doctrine in section 1823(e), eliminated the need to show any "reckless" behavior or fraudulent intent.³⁰⁰ Section 1823(e) instead disallows the enforcement of all agreements that are not written and created at the same time as the obligation, approved by the bank's board of directors, and maintained in the records of the bank, without regard to the culpability of the debtor.³⁰¹

In recognizing a clear congressional intent to protect the FDIC, the court in *Gunter v. Hutcheson*³⁰² wrote:

Although *D'Oench* went no further than to enforce the liability of one who had "lent himself" to a scheme to defraud, the case provides a general basis for a federal policy to protect the FDIC. . . . [A]lthough both *Deitrick* and *D'Oench* required an element of fault on the part of the obligor, [section] 1823(e), which was the Congressional response to the *D'Oench* holding, eliminated any fault requirement. These events chronicle a broadening protection for the FDIC founded on federal policies of protecting the banking system"³⁰³

Congress intended to give the FDIC a significant, rather than illusory, amount of protection by promulgating section 1823(e).³⁰⁴ Accordingly, courts have consistently applied section 1823(e) to block defenses to FDIC claims, without regard to *who* is raising the defense.³⁰⁵ One

297. *Gunter v. Hutcheson*, 674 F.2d 862, 872 n.14 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982).

298. 12 U.S.C. § 1823(e) (1988). As the court in *Kanterman* noted, "[t]he focus under [section] 1823(e) is merely whether the defense asserted falls within the rubric of 'agreement' as that term is there employed." *Kanterman*, 97 Bankr. at 776 n.8.

299. For the text of 12 U.S.C. § 1823(e), see *supra* note 89.

300. *Gunter*, 674 F.2d at 872 n.14.

301. 12 U.S.C. § 1823(e) (1988).

302. 674 F.2d 862 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982).

303. *Id.* at 872 n.14.

304. *Howell v. Continental Credit Corp.*, 655 F.2d 743, 747 (7th Cir. 1981) (quoting *Riverside Park Realty Co. v. FDIC*, 465 F. Supp. 305, 313 (M.D. Tenn. 1978)).

305. See, e.g., *Langley*, 484 U.S. at 96 (condition to payment of note is "agreement" under section 1823(e)); *Holt v. FDIC (In re CTS Truss)*, 859 F.2d 357, 361-62 (5th Cir. 1988) (oral side agreement to extend additional financing), *modified in part*, 868 F.2d 146 (5th Cir. 1989); *FDIC v. The Cremona Co.*, 832 F.2d 959, 964 (6th Cir. 1987) (partnership agreement limiting

court has held that, "[t]he statutory protection of section 1823(e) shields the FDIC from defenses or claims raised with respect to 'any asset acquired by it under this section.'"³⁰⁶ Section 1823(e) would thus seem to bar fraudulent transferee liability.

If the FDIC cannot obtain protection from fraudulent transferee liability under either *D'Oench, Duhme* or section 1823(e), it may still find refuge under a related doctrine of federal common law that affords the FDIC holder-in-due-course status.³⁰⁷ The next section analyzes the application of this separate common-law doctrine to the FDIC.

D. Does Other Federal Common Law Bar FDIC Liability?

The FDIC is also protected by a different federal common-law doctrine than the one stemming from *D'Oench, Duhme*.³⁰⁸ As noted above, United States Courts of Appeals in the Fifth, Sixth, and Eleventh Circuits have concluded that where the FDIC takes a note in good faith and without actual knowledge of any defense against the note, it takes the note free of all defenses which would not prevail against a holder-in-due-course.³⁰⁹ Generally, holder-in-due-course status has been granted to protect the FDIC from varying state law of which the FDIC is not aware.³¹⁰

In extending holder-in-due-course status to the FDIC, courts have

liability of partner on partnership promissory note), *cert. dismissed sub nom.* Gonda v. FDIC, 485 U.S. 1017 (1988); FDIC v. Lattimore Land Corp., 656 F.2d 139, 150 (5th Cir. Unit B Sept. 1981) (oral agreement for future loans); Chatham Ventures, Inc. v. FDIC, 651 F.2d 355, 361-62 (5th Cir. Unit B July 1981) (oral joint-venture agreement); FDIC v. Hoover-Morris Enters., 642 F.2d 785, 787 (5th Cir. Unit B Apr. 1981) (oral accord and satisfaction agreement); Black v. FDIC, 640 F.2d 699 (5th Cir. Unit B Mar.) (oral agreement to make construction loans), *cert. denied*, 454 U.S. 838 (1981); FDIC v. Sarvis, 697 F. Supp. 1161, 1164 (D. Colo. 1988) (oral agreement to pay loan amount to holding company rather than defendant); FDIC v. Rodenberg, 571 F. Supp. 455, 459 (D. Md. 1983) (defense of fraud in the inducement); FDIC v. Kucera Builders, Inc., 503 F. Supp. 967, 971 (N.D. Ga. 1980) (defense of fraud in inducement); FDIC v. Willis, 497 F. Supp. 272, 277-78 (S.D. Ga. 1980) (defenses of fraud in inducement, estoppel and waiver); FDIC v. Rosenthal, 477 F. Supp. 1223, 1227 (E.D. Wis. 1979) (defense of fraud in inducement), *aff'd*, 631 F.2d 733 (7th Cir. 1980); FDIC v. Vogel, 437 F. Supp. 660, 663 (E.D. Wis. 1977) (oral loan commitment); Dasco, Inc. v. American City Bank & Trust Co., 429 F. Supp. 767, 770 (D. Nev. 1977) (oral agreement of conditional liability).

306. *Chatham Ventures, Inc.*, 651 F.2d at 359.

307. *See supra* notes 105-25 and accompanying text.

308. *Gallant v. Kanterman (In re Kanterman)*, 97 Bankr. 768, 775 (Bankr. S.D.N.Y.), *aff'd*, 108 Bankr. 432 (S.D.N.Y. 1989).

309. *See, e.g.*, FDIC v. Gulf Life Ins. Co., 737 F.2d 1513, 1517 (11th Cir. 1984) (waiver, estoppel, unjust enrichment).

310. *Gunter v. Hutcheson*, 674 F.2d 862, 869 (11th Cir.) (fraud), *cert. denied*, 459 U.S. 862 (1982).

applied the multi-part analysis of *United States v. Kimbell Foods, Inc.*³¹¹ First, the applicable law, state or federal, must be determined.³¹² If federal law is applicable, content must then be given to that law.³¹³ Whether a uniform national rule is necessary rests on three factors: (1) whether the federal program by its nature requires a uniform national rule; (2) whether adopting the state law would frustrate the objectives of the federal program; and, (3) whether adoption of a uniform national rule would disrupt commercial expectations based on state law.³¹⁴

The court in *Gunter v. Hutcheson*³¹⁵ considered a claim against the FDIC of securities violations and fraud on the part of the failed bank.³¹⁶ Applying the threshold inquiry to determine applicable law, the court found that under *D'Oench, Duhme & Co. v. FDIC*,³¹⁷ "federal law controls the rights and obligations of the FDIC"³¹⁸ They supported this by noting that the FDIC functions to "protect and stabilize the national banking industry" under a federal statutory scheme promulgated by Congress in the exercise of its constitutional power.³¹⁹ In order to give content to that federal law the court considered the three *Kimbell Foods* factors and found that a uniform national rule granting the FDIC holder-in-due-course status was required.³²⁰

First, the *Gunter* court held that the federal program at issue, national insurance of the banking industry, by its very nature required a uniform national rule.³²¹ Second, the court concluded that there was a need for uniformity to prevent state law from frustrating the objectives of the deposit insurance system.³²² The *Gunter* court reasoned that this need for uniformity stemmed from the necessity for "overnight decisions in dealing with a failed bank."³²³ These decisions involve choosing between a liquidation or purchase and assumption of the bank's assets.³²⁴ In the absence of a uniform national rule, the FDIC would be subject to the "additional burden of considering the impact of possibly variable

311. 440 U.S. 715 (1979). For the court's application of the multi-part analysis of *Kimbell Foods*, see *Gunter*, 674 F.2d at 868-69.

312. *Gunter*, 674 F.2d at 868.

313. *Id.*

314. *Id.*

315. 674 F.2d 862 (11th Cir.), cert. denied, 459 U.S. 862 (1982).

316. *Id.* at 866.

317. 315 U.S. 447 (1942).

318. *Gunter*, 674 F.2d at 869.

319. *Id.*

320. *Id.* at 868-72.

321. *Id.* at 869.

322. *Id.* at 872-73.

323. *Id.*

324. *Id.*

state law on the rights involved" thus significantly impairing its ability to choose between a liquidation and a purchase and assumption transaction.³²⁵ Lastly, considering the third *Kimbell Foods* factor, the *Gunter* court concluded that potential "interference with the federal goals of stability and confidence in the national banking system" far outweighed the potential damage to commercial expectations by affording the FDIC holder-in-due-course status.³²⁶ This conclusion is supported by the fact that the FDIC "carr[ies] a shield no greater than that possessed by a holder in due course—a much more likely transferee than the FDIC."³²⁷

Does this federal common law apply where a bankruptcy trustee seeks to avoid the fraudulent transfer of an asset now held by the FDIC? First, the applicable law must be determined. When the FDIC sues or is sued in its capacity as receiver of an insolvent national bank, federal rather than state law is used to determine its rights and obligations.³²⁸ Furthermore, where the trustee's right of recovery stems from section

325. *Id.* at 869.

326. *Id.* at 872. Other courts have followed this reasoning with respect to state-law fraud claims, applied federal common law, and granted the FDIC holder-in-due-course status. *See, e.g.,* *FDIC v. Wood*, 758 F.2d 156, 160 (6th Cir.), *cert. denied*, 474 U.S. 944 (1985). In *Wood*, the court wrote:

When an insured bank goes into receivership, the FDIC in most cases will in fact be a good-faith holder of its notes. If the FDIC had no knowledge, prior to receivership, of defenses to the notes, and if it otherwise acted in good faith, it cannot be said that the FDIC is not innocent. If it is true that the state's bright-line requirements prevent the FDIC from being a holder in due course, then it is inappropriate to apply those requirements to a government agency crucial to the existence of the modern banking system when they are without purpose.

Id. at 160. *See also* *FDIC v. Rosenthal*, 477 F. Supp. 1223 (E.D. Wis. 1979) (court declined to use notice under Wisconsin law to strip FDIC of holder-in-due-course status), *aff'd*, 631 F.2d 733 (7th Cir. 1980).

327. *Gulf Life Ins. Co.*, 737 F.2d at 1517-18. In *Gunter*, the court expressed doubt that the "eventuality of a bank failure plays a significant role in the ordinary commercial expectations of the parties to negotiable instruments." *Gunter*, 674 F.2d at 872. For criticism that this reasoning overlooks the true manner in which purchase and assumption transactions are carried out, see Note, *supra* note 5, at 304-05.

328. *Official Unsecured Creditors' Comm. v. Capistrano Nat'l Bank (In re Hescon Developers, Inc.)*, 91 Bankr. 916, 920 (Bankr. S.D. Cal. 1988). *See also* 12 U.S.C. § 1819 (as amended by FIRREA, Pub. L. No. 101-73, § 209, 103 Stat. 183, 216 (1989)). The statute provides in pertinent part: "[A]ll suits of a civil nature at common law or in equity to which the [FDIC], in any capacity, is a party shall be deemed to arise under the laws of the United States" *Id.* Justice Jackson, in his concurrence in *D'Oench, Duhme*, interpreted this "arising under" language as not being merely jurisdictional, as shown by "the presence in the same section of the Act of the separate provision that the [FDIC] may sue and be sued 'in any court of law or equity, State or Federal.'" 315 U.S. at 467-68 (Jackson, J., concurring). He concluded that the "policy of the federal Act does not seem to me to leave dependent on local law the question whether one may plead his own scheme to deceive a bank's creditors and supervising authorities as against the [FDIC]." *Id.* at 474-75.

548,³²⁹ state law is not incorporated.³³⁰ However, where the FDIC has become the receiver of a state bank, state law, not federal, may govern in some circumstances.³³¹ Some courts have carried this idea a step further. These courts have held that since federal law grants the FDIC, as receiver of a state bank, all "rights, powers, and privileges"³³² granted by state law to the receiver of a state bank, the FDIC is also subject to any state-law defenses that could be asserted against a non-FDIC receiver.³³³

The conflict between federal protection of the FDIC and the bankruptcy trustee's federal statutory cause of action is most pronounced when determining the applicable substantive law, as courts are not faced with the traditional choice between state or federal law.³³⁴ The trustee is not raising a state-law defense. Rather, the applicable federal law, the Bankruptcy Code,³³⁵ explicitly authorizes the trustee's right of recov-

329. 11 U.S.C. § 548 (1988).

330. *Hescon Developers*, 91 Bankr. at 920. Section 548 is a purely federal cause of action with no "provision making state law applicable under the Code." *Id.*

331. 12 U.S.C. § 1819 (as amended by FIRREA, Pub. L. No. 101-73, § 209, 103 Stat. 183, 216 (1989)) provides in pertinent part:

Except as provided in subparagraph D, all suits of a civil nature at common law or in equity to which the [FDIC], in any capacity, is a party shall be deemed to arise under the laws of the United States . . .

. . . .

(D) any action (i) to which the [FDIC], in the [FDIC's] capacity as receiver of a State insured depository institution by the exclusive appointment by state authorities, is a party *other than as plaintiff* (ii) which involves *only* the preclosing rights against the State insured depository institution, or obligations owing to depositors, creditors, or stockholders by the State insured depository institution, *and* (iii) in which only the interpretation of the law of such state is necessary shall not be deemed to arise under the laws of the United States.

Id. (emphasis added). See also, e.g., *FDIC v. Leach*, 525 F. Supp. 1379, 1384 (E.D. Mich. 1981) (where FDIC sues as receiver under state law, applicable substantive law is state, not federal).

332. 12 U.S.C. § 1821(e) (1988).

333. See, e.g., *In re Selden*, 58 Bankr. 667, 678 (Bankr. D. Neb. 1986). In *Selden*, the court held that the FDIC was subject to a state-law defense that the creditor had permitted the waiver of a security interest through practice and procedure, rather than agreement or misrepresentation. *Id.*

334. Judge Posner, writing for the court in *FDIC v. Braemore Associates*, addressed the determination of substantive law in cases involving the FDIC:

We expressed recently and remark once again our queasiness at being asked to decide an appeal without being told by the district court what substantive law to apply—state or federal In some cases insistence on an explicit statement of the source of law would be pedantic, but not here. Maybe the "arising under" language of [section 1819 of Title 12] is just a redundant way of conferring jurisdiction on the federal courts rather than a direction to those courts to create a common law of rights and obligations of the FDIC; but an unbroken line of decisions beginning with *D'Oench, Duhme & Co. v. FDIC*, holds that the substantive law to be applied in suits to which the FDIC is a party is indeed federal common law, not state law.

686 F.2d 550, 553 (7th Cir. 1982) (citations omitted).

335. 11 U.S.C. §§ 101-1330 (1988).

ery.³³⁶ Moreover, the federal statute itself allows application of state law under section 544(b)³³⁷ in certain circumstances.³³⁸ Thus it might be argued that the "policy to protect the federal agency from the vagaries of state law affords no basis to exempt the FDIC from a federal statutory cause of action, provided to assure equitable distribution of an insolvent debtor's assets to its creditors."³³⁹ Though there may be no need to protect the FDIC from "the vagaries of state law," a second justification for protecting the FDIC may be found through application of the multi-part *Kimbell Foods* analysis.³⁴⁰

As explained by the *Gunter* court, in suits involving the FDIC, its national character is best served by a uniform national rule.³⁴¹ Additionally, the important federal interests in stabilizing the economy and protecting bank depositors which originally led to the formation of the FDIC would be frustrated through application of the federal fraudulent transfer provision.³⁴² Under the rationale of the Supreme Court in *Kimbell Foods*, the FDIC should be immune from the application of a law, regardless of its local or national character, where federal interests are threatened.³⁴³ The court in *FDIC v. Gulf Life Insurance Co.*³⁴⁴ explains the FDIC's only options:

Were the FDIC subject to these defenses it would have to pursue one of two unpalatable courses. First, it could conduct its evaluations of the failed banks' assets with its current speed and detail, but be unable to make the informed judgment that is a statutory prerequisite to its participation in a purchase and assumption agreement, due to the possible existence of unknown

336. *Id.* § 548. For a discussion of section 548, see *supra* notes 149-50.

337. 11 U.S.C. § 544(b) (1988). For a discussion of the trustee's ability to use state law under section 544(b), see *supra* note 149.

338. See 12 U.S.C. §§ 1819, 1821(e) (1988) (authorizing FDIC as receiver of failed state banks, with rights and privileges state law grants to receivers of state banks, and mandating that state law be applied); 11 U.S.C. § 544(b) (1988) (allowing trustee to invoke rights of creditor under applicable state law).

339. *La Mancha Aire, Inc. v. FDIC (In re La Mancha Aire)*, 41 Bankr. 647, 649 (Bankr. S.D. Fla. 1984).

340. See *Wood*, 758 F.2d at 159 (granting protection to FDIC since contrary holding would "frustrate important objectives of the federal program").

341. *Gunter*, 674 F.2d at 869.

342. *Wood*, 758 F.2d. at 159-60. For a discussion of the reasons behind the formation of the FDIC, see *supra* notes 23-36 and accompanying text.

343. *Gunter*, 674 F.2d at 869. See also *Wood*, 758 F.2d at 159-60. For an argument against granting the FDIC holder-in-due-course status, see Miller & Meacham, *The FDIC and Other Financial Institution Insurance Agencies as "Super" Holders in Due Course: A Lesson in Self-Pollinated Jurisprudence*, 40 OKLA. L. REV. 621 (1987).

344. 737 F.2d 1513 (11th Cir. 1984).

claims to which it nonetheless would be vulnerable. Second, it could evaluate the assets much more slowly and exhaustively, probing beyond the bank's records to the extent possible, at the risk of losing the going concern value of the failed bank and the public confidence that it reflects. Even then, the FDIC might not be able to form the necessary opinion. Under either branch of this . . . choice the FDIC's ability to enter purchase and assumption agreements would be seriously circumscribed. This in turn would frustrate the *overriding policy of promoting stability and confidence* with respect to the nation's banking system.³⁴⁵

The federal cause of action of section 548 impairs the FDIC's ability to carry out its statutory mandate, by making it impossible for the FDIC to estimate its possible liability in a purchase and assumption transaction as required by statute.³⁴⁶ Thus, the purchase and assumption option is effectively foreclosed.³⁴⁷ This interference is similar to that threatened by the state-law fraud claims rejected by the *Gunter* court.³⁴⁸

Lastly, the third *Kimbell Foods* factor, the impact on settled commercial expectations, must be considered.³⁴⁹ Arguably, the same reasoning as applied by the *Gunter* court could be used in the fraudulent transfer context.³⁵⁰ In order for the protection of the FDIC from fraudulent transfer liability to disrupt reasonable commercial expectations, creditors of the bankrupt debtor would have to anticipate the debtor's

345. *Id.* at 1517 (emphasis added).

346. 12 U.S.C. § 1823(k) (as enacted by FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 258 (1989)). The FDIC may authorize a purchase and assumption transaction only "if it determines that such authorization would lessen the risk to the FDIC." *Id.* Further, section 1823(c)(4)(A) provides:

No assistance shall be provided under this subsection [permitting the FDIC to purchase the assets of a failed bank to facilitate a purchase and assumption by another bank] in an amount in excess of that amount which the [FDIC] determines to be reasonably necessary to save the cost of liquidating . . . [unless] continued operation of such insured depository institution is essential to provide adequate depository services in its community.

Id. § 1823(c)(4)(A) (as amended by FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 255 (1989)). In other words, a purchase and assumption transaction can be entered into only where it has been determined that its cost will be less than that of a liquidation. Barnett, Horvitz & Silverberg, *supra* note 61, at 310. In assessing the costs, FIRREA provides that the FDIC shall take into account both, "the immediate and long-term obligations of the [FDIC] with respect to such assistance, including contingent liabilities, and . . . the Federal tax revenues foregone by the Government, to the extent reasonably ascertainable." FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 255 (1989).

347. See *Gunter*, 674 F.2d at 870 (state-law fraud claims).

348. *Id.* at 869-70.

349. *Kimbell Foods*, 440 U.S. at 728-29.

350. *Gunter*, 674 F.2d at 872-73.

bankruptcy, the fraudulent transfer of the asset to the bank before that bankruptcy, and the failure of the bank and subsequent seizure by the FDIC.³⁵¹ This may be too remote to effect reasonable commercial expectations.³⁵² Thus, protecting the FDIC from a *federal* fraudulent transfer claim, where the fraudulent transfer was unknown to the FDIC at the time it took over the failed bank, would protect the FDIC from conflicting federal law and promote its express statutory objectives.

A court could conclude that neither section 1823(e) nor federal common law, under either *D'Oench, Duhme* or *Kimbell Foods*, afford protection for the FDIC where a trustee seeks to avoid a fraudulent transfer. However, the FDIC might still find refuge from fraudulent

351. See *FDIC v. Kucera Builders, Inc.*, 503 F. Supp. 967, 973 (N.D. Ga. 1980) (reasonable reliance on state law only altered in extremely rare case of failure of payee bank, default on note, and need to raise defense).

352. A second argument, beyond the possible impact on settled commercial expectations, is that protecting the FDIC from fraudulent transferee liability will raise interest rates charged by creditors. To evaluate this argument entails looking at interest rates on both an individual basis and in the aggregate market.

The individual creditors at issue are those of the bankrupt debtor now represented by the trustee. Judge Posner notes that interest rates have three principal components. R. POSNER, *supra* note 133, at 180. The first is the opportunity cost of capital, a comparison with what the capital could earn in alternative investments. *Id.* The second is the risk premium necessary to compensate the creditor for the possibility that he will lose his capital. *Id.* It is this second component, affected by the creditor's attitude toward risk, that might increase. *Id.* The third is the anticipated inflation rate over the loan period. *Id.* Posner also states that interest rates will

reflect the risk of default as that risk is estimated when the loan agreement is signed, but thereafter the [borrower] may increase the risk of default, for example by obtaining additional loans not subordinated to the first loan or by transferring assets to its shareholders without full consideration. By doing these things the borrower unilaterally reduces the interest rate it is paying for the loan, a rate negotiated with reference to an anticipated level of risk that is lower than has come to pass.

Id. at 371 (emphasis added). Even with this in mind, it seems too attenuated to think that the debtor's individual creditors, at the time they extend credit and set the interest rate, will anticipate the default of the borrower, the fraudulent transfer of assets to a bank by the borrower, and the failure of the bank and subsequent seizure by the FDIC.

One commentator anticipates that market interest rates charged by creditors will rise as "the riskiness of subsequent collection, including the risk of unrecorded transfers, must also [in addition to secured creditors] affect the price that unsecured creditors will charge in connection with all unsecured transactions." Schechter, *supra* note 181, at 125 n.64. This reasoning is applicable where the trustee, representing unsecured creditors, is unable to avoid the fraudulent transfer of assets now held by the FDIC.

However, if the FDIC is not protected, it would be "amenable to a greater number of note rescission suits and would undoubtedly lose many more of these suits." Note, *Federal Deposit Insurance Corporation v. Wood: The FDIC, the Failed Bank, and the Seemingly Insurmountable Presumption*, 17 U. TOL. L. REV. 693, 706 (1986). This increased cost would be passed on to member banks through the form of higher insurance premiums. *Id.* Banks would compensate by charging higher interest rates. *Id.* Thus, any increase in interest rates should not be a factor in deciding whether or not to protect the FDIC.

transferee liability under section 550(b) of the Bankruptcy Code, which disallows recovery from bona fide purchasers for value.³⁵³

E. Is the FDIC Protected as a Bona Fide Purchaser For Value Under Section 550(b) of the Bankruptcy Code?

A trustee's right to recover avoidable transfers is limited by the express provisions of section 550 of the Bankruptcy Code,³⁵⁴ not by state law.³⁵⁵ Section 550 provides that a trustee may not recover from an "immediate or mediate" transferee of the initial transferee if (1) that "immediate or mediate" transferee takes for value; (2) in "good faith;" and, (3) without knowledge of the voidability of the transfer in question.³⁵⁶ If the FDIC satisfies the elements of section 550, the FDIC could be deemed a subsequent bona fide purchaser for value, and will have no liability as the transferee of an avoided transfer.³⁵⁷

Section 550 proves to be similar to the federal common-law protection afforded the FDIC by *United States v. Kimbell Foods Inc.*,³⁵⁸ and its progeny.³⁵⁹ Under the *Kimbell Foods* rationale, courts have held that

353. 11 U.S.C. § 550(b) (1988).

354. Judge Easterbrook, writing for the court in *Bonded Financial Services, Inc. v. European American Bank*, provided both an example of and the underlying rationale for these statutorily imposed limits:

If the recipient of a fraudulent conveyance uses the money to buy a Rolls Royce, the auto dealer need not return the money to the bankrupt even if the trustee can identify the serial numbers on the bills. The misfortune of the firm's creditors is not a good reason to mulct the dealer, who gave value for the money and was in no position to monitor the debtor.

838 F.2d 890, 892 (7th Cir. 1988).

355. *Smith v. Mixon (In re Mixon)*, 788 F.2d 229, 231 (4th Cir. 1986).

356. 11 U.S.C. § 550 (1988). The statute provides in pertinent part:

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section . . . 548 . . . of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or (2) any immediate or mediate transferee of such initial transferee. (b) The trustee may not recover under subsection (a)(2) of this section from—(1) a transferee that *takes for value, including satisfaction or securing of a present or antecedent debt in good faith, and without knowledge of the voidability of the transfer avoided*; or (2) any immediate or mediate good faith transferee of such transferee.

Id. (emphasis added).

357. See *Osherow v. First RepublicBank San Antonio (In re Linen Warehouse, Inc.)*, 100 Bankr. 856, 860 (Bankr. W.D. Tex. 1989) (FDIC shielded from liability as good faith transferee for value under section 550(b)). *Contra* *First City Fin. Corp. v. FDIC (In re First City Fin. Corp.)*, 61 Bankr. 95, 97 (Bankr. N.M. 1986) (FDIC not protected by section 550(b) as matter of law).

358. 440 U.S. 715 (1979).

359. See *FDIC v. Wood*, 758 F.2d 156 (6th Cir.), *cert. denied*, 474 U.S. 944 (1985); *Gunter v. Hutcheson*, 674 F.2d 862 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982). For a discussion of

although section 1823(e) does not specifically authorize holder-in-due-course status for the FDIC, state law that precludes the FDIC from attaining this status would frustrate federal objectives and is, therefore, inapplicable.³⁶⁰ Hence, where the FDIC acts in its corporate capacity through a purchase and assumption transaction and acquires a note in good faith and without actual knowledge of any defense, the FDIC takes the note free of all defenses that would not prevail against a holder-in-due-course.³⁶¹

While Congress did not enact section 550 to codify this federal common-law rule,³⁶² section 550's definition of a bona fide purchaser for value is strikingly similar to that of a holder-in-due-course as defined in the Uniform Commercial Code.³⁶³ Accordingly, section 550(b) may mirror the impact that the *Kimbell Foods* doctrine has on FDIC liability under state law with respect to the FDIC's liability under the Bankruptcy Code.

1. Is the FDIC an "immediate or mediate" transferee?

To invoke section 550, the FDIC must be an "immediate or mediate" transferee of the initial transferee.³⁶⁴ Collier equates this with a "subsequent" transferee of the initial transferee.³⁶⁵ Whether the FDIC is in fact a subsequent transferee will depend upon the manner in which it acquires the asset being sued upon, and in what capacity the FDIC is suing.³⁶⁶

As noted above, the FDIC may acquire the assets of a failed bank in two ways: as receiver of the bank or through the arrangement of a

that federal common-law protection, see *supra* notes 105-25 and 309-53 and accompanying text.

360. See, e.g., *FDIC v. The Cremona Co.*, 832 F.2d 959, 964 (6th Cir. 1987), *cert. dismissed sub nom. Gonda v. FDIC*, 485 U.S. 1017 (1988).

361. *Wood*, 758 F.2d at 161.

362. The considerations underlying section 550 are the same as those behind the holder-in-due-course rule for commercial paper (UCC § 3-302) and the bona fide purchaser for value rule for chattels (UCC § 2-403(1)). *Bonded Fin. Servs.*, 838 F.2d at 892 ("[W]aste . . . would be created if people either had to inquire how their transferors obtained their property or to accept a risk that a commercial deal would be reversed for no reason they could perceive at the time . . ."). For a discussion of the rationale behind the federal common-law rule providing protection to the FDIC, see *supra* notes 309-27 and accompanying text.

363. Compare 11 U.S.C. § 550(b) (1988) with U.C.C. § 3-302 (1987).

364. 11 U.S.C. § 550(a)(2) (1988).

365. 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-10.

366. See generally *id.* ¶ 550.03, at 550-9 to -11 (discussing protected subsequent transferees).

purchase and assumption transaction.³⁶⁷ Both methods arise out of the FDIC's role as an insurer of banks who pays off the depositors of a failed bank.³⁶⁸

Where the FDIC has arranged a purchase and assumption transaction and subsequently acquires a "bad" asset, it sues in its corporate capacity.³⁶⁹ The method by which the corporate FDIC acquires a "bad" asset, through purchase from itself in its capacity as receiver, makes it a "subsequent transferee" since not only has the asset been "transferred" from the failed bank to the FDIC as receiver, but it has then been "transferred" from the FDIC as receiver to the FDIC in its corporate capacity.³⁷⁰

Where the FDIC acquires assets by appointment as receiver in the liquidation of a failed bank and sues as receiver, it generally stands in the shoes of the failed bank.³⁷¹ Thus, the FDIC might not be a "subsequent transferee" of any assets the bankrupt debtor fraudulently transferred to the bank. The difference between the FDIC acting as receiver for a failed bank and the FDIC acting in its corporate capacity was noted by the court in *Evans v. Robbins (In re Robbins)*.³⁷² The FDIC acting in its corporate capacity as insurer is more than "a successor-in-interest to the closed bank."³⁷³ The court reasoned that under these circumstances, the FDIC is entitled to greater protection than when the FDIC acts as receiver and "merely steps into the bank's shoes and can only assert the same defenses [as are] available to the bank."³⁷⁴ Thus, the court concluded, where the FDIC has "purchased and assumed assets of a bank, it may be able to assert [that] it is a good faith purchaser in its own right" in order to defend against post-petition avoidance actions by the trustee.³⁷⁵

"Transfer," however, is defined *very* broadly in the Bankruptcy

367. For a discussion of liquidations and purchase and assumption transactions, see *supra* notes 37-61 and accompanying text.

368. *Gunter*, 674 F.2d at 865.

369. See Note, *supra* note 5, at 261.

370. See *id.*

371. Official Unsecured Creditors' Comm. v. Capistrano Nat'l Bank (*In re Hescon Developers, Inc.*), 91 Bankr. 916, 919 (Bankr. S.D. Cal. 1988). The court in *Hescon Developers* wrote: "When the FDIC acts as receiver of an insolvent national bank it stands in the shoes of the insolvent bank and is required to marshal the assets of the bank for its shareholders and creditors." *Id.*

372. 91 Bankr. 879, 889 (Bankr. W.D. Mo. 1988).

373. *Id.* (quoting *FDIC v. Vogel*, 437 F. Supp. 660, 663 (E.D. Wis. 1977)).

374. *Id.*

375. *Id.*

Code.³⁷⁶ The legislative history of the Bankruptcy Code states that "transfer" was meant to include any "transfer of possession, custody or control."³⁷⁷ Further, the FDIC as receiver acquires the assets of a failed bank by operation of law.³⁷⁸ Accordingly, where the FDIC takes over a bank's assets and liabilities as receiver, assuming custody and control, it is a transferee and should fall within the protection of section 550(b).³⁷⁹ Additionally, where a failed bank would have been a "subsequent transferee" in its own right, the FDIC as receiver, stepping into the failed bank's shoes, would also be a "subsequent transferee."³⁸⁰

2. Is the FDIC a "purchaser" who "takes for value"?

Section 550(b)(1) requires that the subsequent transferee "took for value."³⁸¹ In other words, to meet this requirement, the FDIC must function as a "purchaser."³⁸²

Arguably, where the FDIC acquires assets as receiver in order to liquidate a failed bank, the FDIC is by definition not a "purchaser" who "takes for value." The FDIC is appointed by the appropriate banking authority and simply manages the liquidation of the bank's assets as provided by statute.³⁸³ The court in *Osherow v. First Republic Bank San Antonio (In re Linen Warehouse, Inc.)*,³⁸⁴ however, found that payment is not the exclusive means by which value can be given, and held that the FDIC as receiver was indeed a "purchaser for value."³⁸⁵ The *Linen*

376. "Transfer" is defined by 11 U.S.C. § 101(50) (1988) as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property"

377. H.R. REP. NO. 595, 95th Cong., 2d Sess. 314, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6271.

378. The FDIC as receiver is given the power to "realize upon the assets of such closed bank." 12 U.S.C. § 1821(d) (1988). Additionally, the FDIC as receiver is subrogated, upon payment to any depositor, to all the rights of the depositor against the closed bank to the extent of the payment. *Id.* § 1821(g).

379. *Linen Warehouse*, 100 Bankr. at 859. See also *Holt v. FDIC (In re Instrument Sales & Serv., Inc.)*, 99 Bankr. 742, 746 (Bankr. W.D. Tex. 1987) (FDIC is subsequent transferee under section 550). Judge Easterbrook, writing for the Seventh Circuit Court of Appeals in *Bonded Fin. Servs.*, took a more restrictive view. 838 F.2d at 893. After noting that the Bankruptcy Code does not define "transferee" and the lack of legislative history on the point, he concluded that the minimum requirement of status as a "transferee" is "dominion over the money or other asset, [and] the right to put the money to one's own purpose." *Id.*

380. One example is where the failed bank held a mortgage that had been assigned to it from another financial institution.

381. 11 U.S.C. § 550(b)(1) (1988).

382. *Bonded Fin. Servs.*, 838 F.2d at 897.

383. 12 U.S.C. § 1821(c)-(e) (1988).

384. 100 Bankr. 856 (Bankr. W.D. Tex. 1989).

385. *Id.* at 859.

Warehouse court pointed out that "value given" could also entail the rendering of services or the assumption of liabilities.³⁸⁶ The court ruled that the FDIC "takes for value" when it accepts the assets and liabilities of a failed bank as receiver, and performs "the FDIC's attendant duties, in accordance with the statutory banking insurance scheme."³⁸⁷

This expansive interpretation of "value" is in accord with the Uniform Commercial Code, which provides that "value" is "any consideration sufficient to support a simple contract."³⁸⁸ Thus, "value" need merely be a "cent or pepper corn."³⁸⁹ The amount of value given is immaterial. Unlike prior law, section 550 imposes no requirement that the value given by the transferee, the FDIC in its corporate capacity, be a fair equivalent to the value of the property transferred.³⁹⁰ Furthermore, the *Linen Warehouse* court's interpretation of "value" is in accord with congressional objectives in FIRREA, the 1989 reformation of banking industry regulation.³⁹¹

Is the FDIC a "purchaser" for value when it sues in its corporate capacity? The Seventh Circuit Court of Appeals recognized in *Bonded Financial Services v. European American Bank*,³⁹² that the federal statute does not say "value to the debtor," but rather, "value."³⁹³ Since the FDIC acts in its corporate capacity to give value to the FDIC as receiver in return for assets, it could also be viewed as a "purchaser" as the term is used in section 550.

It has been argued, however, that when the FDIC as receiver trans-

386. *Id.*

387. *Id.*

388. U.C.C. § 1-201(44)(d) (1987).

389. *Whitney v. Stearns*, 16 Me. 394, 397 (1839).

390. *See* Bankruptcy Act of 1898, ch. 541, § 67(e), 30 Stat. 544 (requiring both good faith and "present fair consideration").

391. Congressional objectives were laid out in the recent savings and loan bailout bill, FIRREA, Pub. L. No. 101-73, § 101, 103 Stat. 183, 187 (1989). The Act was designed to: (1) promote a safe and stable system of affordable housing finance through regulatory reform; (2) improve the supervision of the savings and loan industry; (3) curtail risky investments by S&Ls; (4) promote the independence of the FDIC; (5) ensure the solvency of federal deposit insurance funds; (6) establish an Office of Thrift Supervision; (7) establish the Resolution Trust Corporation to contain, manage and resolve failed S&Ls; (8) provide public and private funds to handle failed S&Ls; (9) strengthen the FDIC's enforcement powers; and, (10) strengthen civil and criminal penalties for defrauding depository institutions and their depositors. *Id.* § 101.

392. 838 F.2d 890 (7th Cir. 1988).

393. *Id.* at 897. The court further noted that "[a] natural reading [of the statute] looks to what the transferee gave up rather than what the debtor received." *Id.* *See also* 11 U.S.C. 550(b)(1) (1988) ("The trustee may not recover . . . from—a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided . . .").

fers an asset to itself in its corporate capacity, the FDIC is not a "purchaser" at all because it receives the asset from itself.³⁹⁴ The Sixth Circuit Court of Appeals answered this question in *FDIC v. Ashley*,³⁹⁵ holding that the fact that the FDIC purchases the asset from itself presents no problem.³⁹⁶

In *Ashley*, the FDIC had been appointed receiver of the Tri-City Bank of Warren, Michigan.³⁹⁷ The "unacceptable assets" of the bank, including certain causes of action, were subsequently assigned for value to the FDIC in its corporate capacity.³⁹⁸ When the FDIC in its corporate capacity brought suit against the directors of the bank for corporate mismanagement and waste, the bank directors claimed that the transfer of the causes of action was a sham.³⁹⁹ The *Ashley* court held that the validity of the FDIC as a purchaser of assets in its corporate capacity does not change merely because the FDIC, as appointed receiver of the bank, also acts as the seller.⁴⁰⁰ The court based its holding on a reading of the Federal Deposit Insurance Act⁴⁰¹ which provides that the FDIC may, and often must, act in two capacities simultaneously, those of a "receiver of a bank and as an insurance corporation."⁴⁰² Accordingly, where the FDIC in its corporate capacity purchases assets from itself in its capacity as receiver, it qualifies as a "purchaser" who "takes for value."⁴⁰³

3. Is the FDIC acting in "good faith"?

The next question is whether the FDIC acquired the asset upon which it is suing in "good faith."⁴⁰⁴ What this means, however, is unclear, as the Bankruptcy Code does not define the term "good faith."⁴⁰⁵

Collier,⁴⁰⁶ however, notes that courts have defined "good faith"

394. *FDIC v. Ashley*, 585 F.2d 157, 160 (6th Cir. 1978).

395. *Id.*

396. *Id.*

397. *Id.* at 158.

398. *Id.* at 159-60.

399. *Id.* at 160.

400. *Id.*

401. 12 U.S.C. §§ 1811-32 (1988).

402. *Ashley*, 585 F.2d at 160 (emphasis added) (quoting *FDIC v. Godshall*, 558 F.2d 220, 223 (4th Cir. 1977)).

403. *Id.*

404. 11 U.S.C. § 550 (1988).

405. 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-9.

406. The first edition of *Collier on Bankruptcy* was published in 1898 upon passage of the Bankruptcy Act of that same year. 1 R. BABITT, R. BROUDE & A. HERZOG, *COLLIER ON BANKRUPTCY* xiii (15th ed. 1979). Now, more than 90 years later, it is in its fifteenth edition and is recognized as "the foremost authority on the subject of bankruptcy." *Id.*

under prior law.⁴⁰⁷ Generally, the determinative inquiry by the courts is whether the transferee knew or should have known that he or she was not engaged in a normal transaction but rather one in which the debtor intended to defraud his creditors.⁴⁰⁸ In *Bonded Financial Services, Inc. v. European American Bank*,⁴⁰⁹ Judge Easterbrook recognized that "[v]enerable authority has it that the recipient of a voidable transfer may lack good faith if he possessed enough knowledge of the events to induce a reasonable person to investigate."⁴¹⁰

Congress attempted to explain its use of the phrase "good faith," but the legislative history of section 550 is not particularly helpful.⁴¹¹ Congress explained that:

The phrase "good faith" in this paragraph is intended to prevent a transferee from whom the trustee could recover from transferring the recoverable property to an innocent transferee, and receiving a retransfer from him, that is, "washing" the transaction through an innocent third party. In order for the transferee to be excepted from liability under this paragraph, he himself must be a good faith transferee.⁴¹²

The notes that accompanied the proposed statute of the Commission on the Bankruptcy Laws of the United States are no more helpful. The notes state that "good faith" is a familiar phrase that courts can best interpret on a case-by-case basis.⁴¹³ Consequently, courts have had little guidance in applying "good faith" to FDIC actions.

The Sixth Circuit Court of Appeals in *FDIC v. Wood*⁴¹⁴ held that where the FDIC in its corporate capacity brings suit on a note, a presumption of "good faith" exists.⁴¹⁵ The court reasoned that if the FDIC lacked knowledge of defenses to the notes *prior to receivership*, then "it cannot be said that the FDIC is not innocent."⁴¹⁶ The court explained

407. 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-9 & n.3. "[T]he good faith to be considered is that of the transferee and not the intent of the transferor." *Id.* at ¶ 550.03, at 550-9 n.3.

408. *Id.* (citing *In re Messenger*, 32 F. Supp. 490, 494 (E.D. Pa. 1940)).

409. 838 F.2d 890 (7th Cir. 1988).

410. *Id.* at 897-98. See *Dokken v. Page*, 147 F. 438, 441-42 (8th Cir. 1906) (lack of good faith where knowledge that debtor was transferring almost all assets).

411. See S. REP. NO. 989, 95th Cong., 2d Sess. 90, reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 5787, 5876.

412. *Id.*

413. COMM'N ON THE BANKRUPTCY LAWS OF THE U.S., REPORT OF THE COMM'N ON THE BANKRUPTCY LAWS OF THE U.S., PART II, H.R. DOC. NO. 137, 93d Cong., 1st Sess. 180, para. 4 (1973).

414. 758 F.2d 156 (6th Cir.), *cert. denied*, 474 U.S. 944 (1985).

415. *Id.* at 162.

416. *Id.* The court went on to grant the FDIC holder-in-due-course status, and thus pro-

that while the FDIC in its corporate capacity may be aware of the note's potential avoidability at the time the FDIC purchases the note from itself as receiver, that knowledge did not necessarily exist when the FDIC originally acquired the note.⁴¹⁷ Courts have extended the *Wood* court's reasoning to the FDIC bringing suit as receiver and have also found "good faith" under these circumstances.⁴¹⁸ These decisions finding that the FDIC acted in "good faith," implicitly recognize that the FDIC may have knowledge of potential avoidability at the time the asset is transferred to the corporate FDIC. They nevertheless find that application of a strict interpretation of "good faith" to the FDIC seems inappropriate, due to the FDIC's role as a "government agency crucial to the existence of the modern banking system"⁴¹⁹

4. Does the FDIC have "knowledge of the voidability of the transfer"?

Finally, section 550(b) requires that a transferee be without "knowledge of the voidability of the transfer avoided"⁴²⁰ Courts interpret this requirement as meaning actual "knowledge" as opposed to "constructive notice" of the voidability of the transfer.⁴²¹ The court in *Wood* declared that the FDIC is "under no duty, in either of its capacities, to examine the assets of a failed bank before it agrees to execute a purchase and assumption transaction."⁴²² This approach precludes charging the FDIC with constructive knowledge of a defense just because that information could be found in the bank's files.⁴²³

Judge Easterbrook, writing for the Seventh Circuit Court of Appeals in *Bonded Financial Services*, concluded that a lesser amount of knowl-

tection, under the *Kimbell Foods* common-law doctrine. *Id.* at 161. For a discussion of the *Kimbell Foods* line of cases and their possible applicability to fraudulent transfers, see *supra* notes 105-25 and 308-52 and accompanying text. See also *Gunter*, 674 F.2d at 873-74 (FDIC acts in good faith where it acquires note from itself as receiver); *Gilman v. FDIC*, 660 F.2d 688, 695 n.11 (6th Cir. 1981) (citing *FDIC v. Ashley*, 585 F.2d 157 (6th Cir. 1978)) (sale of note from FDIC as receiver to FDIC as corporate insurer is "intra-FDIC transaction" and satisfies good faith criterion of innocent-purchaser defense of section 29(c) of Security Exchange Act of 1934).

417. *Wood*, 758 F.2d at 162. The court wrote, "our explicit holding . . . [is] that the FDIC is under no duty, in either of its capacities, to examine the assets of a failed bank before it agrees to execute a purchase and assumption transaction." *Id.*

418. See *Linen Warehouse*, 100 Bankr. at 859.

419. *Wood*, 758 F.2d at 160.

420. 11 U.S.C. § 550(b) (1988).

421. *Mixon*, 788 F.2d at 232.

422. *Wood*, 758 F.2d at 162.

423. *Id.*

edge would defeat a section 550(b) defense under the Code.⁴²⁴ Noting that while requiring "receipt of a lawyer's opinion that such a transfer is voidable" is too strict a standard, he suggests that some knowledge less than actual knowledge will do.⁴²⁵ However, he declines to impose a duty to investigate as the transferee need not be a "monitor for [the] creditors' benefit when nothing known so far suggests that there is a fraudulent conveyance in the chain."⁴²⁶

Collier treats the "without knowledge" requirement as redundant when taken in conjunction with the "good faith" requirement, and most courts have agreed.⁴²⁷ Collier explains that the "knowledge" language was derived from section 4-609(b)(1) of the draft statute filed with Congress⁴²⁸ by the Commission on the Bankruptcy Laws of the United States.⁴²⁹ The phrase was included solely as an illustration of a transferee who could not have taken in "good faith."⁴³⁰ Collier's interpretation makes it easier for the FDIC to claim status as a bona fide purchaser for value, a result in accord with Congress' efforts to protect the FDIC.⁴³¹

A court deciding possible FDIC fraudulent transferee liability must carefully evaluate each of the issues discussed above. The court, after finding a fraudulent transfer, must in turn consider whether the FDIC is protected by the *D'Oench, Duhme* doctrine, section 1823(e), federal common law, or federal statute (as a bona fide purchaser for value). Each step in this process presents an opportunity for the court to manipulate the analysis to protect the FDIC and many courts have done so.⁴³²

424. *Bonded Fin. Servs.*, 838 F.2d at 898.

425. *Id.* Judge Easterbrook writes: "Some facts strongly suggest the presence of others; a recipient that closes its eyes to the remaining facts may not deny knowledge." *Id.* See *Federman v. Falcone (In re Nevada Implement Co.)*, 22 Bankr. 105, 106 (Bankr. W.D. Mo. 1982) (knowledge of voidability does not mean complete understanding of all facts; lesser knowledge will do).

426. *Bonded Fin. Servs.*, 838 F.2d at 898.

427. See 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-10; Countryman, *The Trustee's Recovery in Preference Actions*, 3 BANKR. DEV. J. 449, 475-482 (1986) (courts need not attempt to discern difference). See also, e.g., *Holt v. FDIC (In re Instrument Sales & Serv.)*, 99 Bankr. 742, 745-46 (Bankr. W.D. Tex. 1987).

428. 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-10. The Commission on the Bankruptcy Laws of the United States filed a proposed statute in 1973. See H.R. DOC. NO. 137, 93d Cong., 1st Sess. pt. II (1973). This proposed statute was accompanied by detailed notes interpreting its provisions. *Id.* However, the proposed statute, introduced in the ninety-third Congress as H.R. 10792 and S. 2565, did not have accompanying notes. *Id.*

429. 4 R. D'AGOSTINO & M. COOK, *supra* note 149, ¶ 550.03, at 550-10 n.4.

430. *Id.*

431. For the purposes behind the passage of FIRREA, see *supra* note 391.

432. The following cases provided protection to the FDIC. See, e.g., *Langley v. FDIC*, 484 U.S. 86, 96 (1987) (FDIC protected from defense of failure of condition to payment of note);

While the results in these cases are supportable, it can be argued that courts need not engage in such manipulation because subjecting the FDIC to fraudulent transferee liability will not prevent the FDIC from carrying out its statutory duties. The next section evaluates this argument.

F. Do Fraudulent Transfers Somehow Differ from Secret Agreements?

Arguably, the policy behind protecting the FDIC from secret agreements should not be extended to protecting the FDIC from fraudulent transferee liability if there is a fundamental difference in the way fraudulent transfers and secret agreements impact the FDIC.⁴³³ In particular, while secret agreements affect the FDIC's role as both regulator and insurer, fraudulent transferee liability may not. To evaluate the soundness of such an argument it is necessary to examine the concerns underlying the "secret agreement" protection afforded the FDIC and compare the impact of fraudulent transferee liability on those concerns.

Beyond the traditional justification that FDIC protection in general is necessary to protect the soundness of the nation's banking system,⁴³⁴ two more specific concerns exist. The first is the FDIC's ability to perform its function as regulator;⁴³⁵ the second is the FDIC's ability to act as insurer.⁴³⁶ As shown below, imposition of fraudulent transferee liability impairs the FDIC's ability to function effectively in either role.⁴³⁷

1. The FDIC as regulator

Imposition of fraudulent transferee liability on the FDIC would impede the FDIC's ability to perform its regulatory function.⁴³⁸ For the FDIC to effectively regulate banking, it must be able to accurately evalu-

FDIC v. Leach, 772 F.2d 1262, 1267 (6th Cir. 1985) (FDIC protected from defense of no consideration); FDIC v. Gulf Life Ins. Co., 737 F.2d 1513, 1517 (11th Cir. 1984) (FDIC protected from defenses of waiver, estoppel and unjust enrichment); *Gunter*, 674 F.2d at 869 (FDIC protected from fraud defense); *Chatham Ventures, Inc. v. FDIC*, 651 F.2d 355, 361-62 (5th Cir. Unit B July 1981) (FDIC protected from oral joint venture agreement), *cert. denied*, 456 U.S. 972 (1982).

433. See *FDIC v. McClanahan*, 795 F.2d 512, 515 (5th Cir. 1986) (recognizing limits to protection afforded to FDIC).

434. *Gunter v. Hutcheson*, 674 F.2d 862, 870 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982).

435. *Id.* at 871.

436. *Id.* at 871-72.

437. See *infra* notes 438-73 and accompanying text.

438. As regulator, the FDIC's Division of Bank Supervision supervises insured banks, ensures compliance with banking laws, oversees enforcement actions, reviews applications for insurance, and reviews proposed mergers. FDIC, *supra* note 1, at 21. In its supervisory role, the FDIC conducts four types of examinations: safety and soundness; compliance with consumer protection and civil rights laws; performance of fiduciary responsibilities in trust depart-

ate banks' solvency.⁴³⁹ A transfer of a property interest to a bank that a trustee can later avoid will result in the FDIC overvaluing bank assets and lead to erroneous solvency determinations.⁴⁴⁰ The Court in *D'Oench, Duhme & Co. v. FDIC*⁴⁴¹ noted that "[t]he genuineness of assets ostensibly held by a bank is certainly germane to a determination of solvency."⁴⁴² Fraudulent transferee liability would result in the FDIC not being able to regulate in the most informed, and presumably most efficient, manner.⁴⁴³ Protection will allow the FDIC to rely on its own valuations of the bank's assets in that the assets represented on a bank's books would be those, theoretically at least, upon which the FDIC could collect.⁴⁴⁴ Thus, protecting the FDIC from fraudulent transfer liability allows the FDIC to best perform its regulatory function.

Secret agreements affect the FDIC's ability to regulate effectively in a manner similar to imposition of fraudulent transferee liability. Secret agreements that do not appear in the bank's records have the effect of overstating solvency as they are actually hidden restrictions on the bank's ability to collect upon assets.⁴⁴⁵ *D'Oench, Duhme* protection eliminates any incentive to enter into secret agreements because the agreements will be disregarded.⁴⁴⁶ Further, any agreements that are entered into will be unenforceable.⁴⁴⁷ Thus, *D'Oench, Duhme* protection results in more accurate valuation of assets, and enables the FDIC to place more reliance on its valuations in making regulatory decisions. This ability to evaluate a bank's assets accurately and rely on that valua-

ments; and adequacy of internal controls in electronic data processing. *Id.* at 3. The FDIC conducted 3,751 safety and soundness examinations in 1988. *Id.* at 4.

439. *Gunter*, 674 F.2d at 870. Insolvency occurs when a bank's liabilities exceed its assets. *Burgee*, *supra* note 53, at 1150. This usually manifests itself when the bank is unable to meet the demands of depositors and other creditors. *Id.* Solvency determinations are based on examination reports prepared by bank examiners which analyze asset values and the bank's liquidity position. *Id.*

440. *See Gunter*, 674 F.2d at 870.

441. 315 U.S. 447 (1942).

442. *Id.* at 460.

443. Admittedly, though, refusal to impose such fraudulent transferee liability on the FDIC will not discourage fraudulent transferors from their actions. The only remedy a trustee may assert upon avoidance of a fraudulent transfer is recovery of the transferred property. 11 U.S.C. §§ 548, 550 (1988). Thus, the bankrupt debtor is not deterred from trying to transfer property.

444. *Gunter*, 674 F.2d at 870.

445. *See, e.g., D'Oench, Duhme*, 315 U.S. at 454 (agreement not to call for payment on note).

446. *Id.* at 459. For a discussion of the protection *D'Oench, Duhme* affords, see *supra* notes 62-87 and 232-81 and accompanying text.

447. *D'Oench, Duhme*, 315 U.S. at 459.

tion leads to better regulatory decisions. To this extent, enforceable secret agreements and fraudulent transferee liability are similar.

2. The FDIC as insurer

A second distinct concern is the effect of fraudulent transferee liability on the FDIC's ability to act as insurer. The core of the argument against protecting the FDIC from fraudulent transferee liability is that such liability does not affect the FDIC's role as insurer in the same way as does allowing the enforcement of secret agreements.⁴⁴⁸ This assumes that the main function of the FDIC as insurer is to arrange purchase and assumption transactions and that imposition of fraudulent transferee liability would not interfere with the FDIC's ability to do so.⁴⁴⁹ Two considerations dictate the FDIC's success in implementing purchase and assumption transactions: (1) the FDIC, by statute, must first determine that the cost of a purchase and assumption transaction is less than the cost of a liquidation;⁴⁵⁰ and, (2) the FDIC must be able to find a willing, healthy bank to acquire the failed bank.⁴⁵¹

448. The court in *La Mancha Aire, Inc. v. FDIC (In re La Mancha Aire, Inc.)*, addressing a trustee's claim that the debtor's grant of a security interest to a bank now in FDIC receivership was a preference under the Bankruptcy Code noted:

The statute is designed to protect the FDIC both as insurer and as receiver from the effect of secret agreements between an insured bank and its obligors. It resembles a dead man's statute and serves much the same purpose. The only effect of the statute, however, is to render certain secret agreements unenforceable against the FDIC. It has no application to the facts here, where no one is attempting to enforce a secret agreement against the FDIC.

41 Bankr. 647, 649 (Bankr. S.D. Fla. 1984).

449. There has been some criticism of the FDIC's willingness to arrange for purchase and assumption transactions in the majority of cases, and of the deposit insurance system in general. E. KANE, *THE GATHERING CRISIS IN FEDERAL DEPOSIT INSURANCE* 46-47 (1985). Critics charge that this preference "extends an implicit government blessing not only to uninsured deposits but also to nondeposit debt and to affiliated corporations of all sorts." *Id.* at 47. This results in 100% de facto insurance and shifts the burden of risky investments from deposit institutions and their creditors to "the insurance system's implicit guarantors: the general taxpayer and conservatively managed institutions able to survive whatever crisis might unfold." *Id.* The recent savings and loan crisis shows that this is exactly what has happened, with disastrous results. The legislative history of FIRREA notes:

As long as the federal government was responsible for picking up the tab for a failed state-chartered thrift, there was no great incentive for many state legislatures to deny the sweeping demands for additional investment powers made by the thrift industry [following deregulation]. The results were tragic. [Seventy percent] of all FSLIC expenditures during 1988 went to pay for problems created by high-risk, ill-supervised, state-chartered thrifts

H.R. REP. NO. 54(1), 101st Cong., 1st Sess. 297, reprinted in 1989 U.S. CODE CONG. & ADMIN. NEWS 86, 93.

450. 12 U.S.C. § 1823(c), (k) (1988). For a discussion of this mandate, see *supra* note 346 and accompanying text.

451. The larger the failed bank is, and the more restrictive the branching laws under which

The court in *Gunter v. Hutcheson*⁴⁵² held that allowing defendants to assert unknown state-law fraud claims against the FDIC would disrupt the purchase and assumption mechanism because the FDIC would be unable to estimate its potential loss from a purchase and assumption transaction and make the required statutory judgment.⁴⁵³ Imposition of fraudulent transferee liability on the FDIC would similarly effect the FDIC's ability to carry out purchase and assumption transactions.⁴⁵⁴ The FDIC would be unable to evaluate accurately its liability in a purchase and assumption transaction due to the possible existence of avoidable fraudulent transfers.⁴⁵⁵

One commentator argued that the FDIC has much more latitude in deciding whether to arrange a purchase and assumption transaction or a liquidation than section 1823 would seem to allow.⁴⁵⁶ The FDIC does

it operates, the more difficult it is for the FDIC to find a willing purchaser. E. KANE, *supra* note 449, at 48.

452. 674 F.2d 862 (11th Cir.), *cert. denied*, 459 U.S. 826 (1982).

453. *Id.* at 870. In order to determine the cost of a purchase and assumption transaction, the FDIC evaluates the bank's assets. *Id.* The Court in *D'Oench, Duhme* held that allowing the enforcement of secret agreements makes it more difficult for the FDIC to value the assets of a bank accurately. 315 U.S. at 460. Justice Jackson also emphasized that the FDIC could accomplish its purposes only if it could rely on bank records. *Id.* at 472 (Jackson, J., concurring).

454. The assumption that the presence of hidden defenses makes a purchase and assumption transaction more expensive than a liquidation has been criticized on the basis that regardless of which option is chosen, the uncollectible asset still comes out of the insurance fund. Note, *supra* note 5, at 282. While true, this reasoning would seem to validate the secret agreement precluded in *D'Oench, Duhme* and lends support to the position that the FDIC should be protected from *all hidden defenses which, if allowed, would cause a loss* to the insurance fund due to an uncollectible asset.

Additionally, to accept this argument, one must conclude that the judgment called for by the statute is unnecessary and therefore the FDIC is free to ignore it. As a consequence of accepting this argument, the FDIC would be free to choose an option on any basis or no basis at all. This is not the case. While the loss will eventually be borne by the insurance fund in either case, 12 U.S.C. § 1823(c)(4)(A) states that the FDIC *must* know that this will be the case *at the time the FDIC is deciding how to handle the failed bank*. 12 U.S.C. § 1823(c)(4)(A) (1988). It cannot ignore this statutory mandate. If the FDIC is unaware of hidden defenses, it will underestimate its potential liability, and implement a purchase and assumption when the statute would otherwise require a liquidation of the failed bank. *Gunter*, 674 F.2d at 870.

Lastly, even if the only effect of these hidden defenses is to decrease the insurance fund, that impact could hurt the FDIC's ability to act as insurer in ways other than simply foreclosing the purchase and assumption option. For a discussion of the financial impact of fraudulent transferee liability on the FDIC's ability to act as insurer, see *infra* notes 466-73 and accompanying text.

455. The former chairman of the FDIC notes that "if the assets and contingent liabilities of the closed bank are too ill-defined for the FDIC to make a reasonable estimate of the comparative costs of an assumption versus a payoff," it may not enter into a purchase and assumption transaction. Barnett, Horvitz & Silverberg, *supra* note 61, at 310.

456. E. KANE, *supra* note 449, at 46.

not report the methods by which it estimates the costs of alternative approaches in sufficient detail to allow external critics to reproduce the alternative estimates.⁴⁵⁷ It is further argued that if a strictly economic accounting of the opportunity costs were actually being used by the FDIC, liquidations would be more frequent.⁴⁵⁸ Robert Barnett, former chairman of the FDIC, noted the persuasiveness of the argument that placing emphasis on cost in making the choice is not within the true meaning of section 1823.⁴⁵⁹ Barnett went on to emphasize that "there is a great degree of flexibility in the cost-based analysis; sufficient flexibility, in fact, that in most cases (not all) in which a [purchase and assumption] transaction is deemed to be the best solution, it can be accomplished."⁴⁶⁰ Under this view, the possible existence of either secret agreements or fraudulent transferee liability would not truly interfere with the FDIC's exercise of its statutory judgment in deciding how to deal with a failed bank.

The second consideration is whether secret agreements or possible fraudulent transferee liability deter healthy banks from entering into purchase and assumption transactions. A successor bank might be reluctant to purchase a note at face value (or would demand a substantial discount as is found in "whole-bank" purchase and assumptions⁴⁶¹) if the note were secretly unenforceable, thus diminishing the value of the bank's assets.⁴⁶² However, the purchasing bank is able to return to the FDIC, under the terms of the purchase and assumption agreement, all assets that were not of the highest banking quality.⁴⁶³ The FDIC, holding the "bad" asset, must sue on the note.⁴⁶⁴ Accordingly, fraudulent transferee liability would neither disrupt the FDIC's ability to choose the purchase and assumption mechanism, nor its ability to implement it.⁴⁶⁵

As shown above, an entirely plausible argument exists that neither fraudulent transferee liability nor secret agreements hurt the FDIC's ability to act as insurer. However, even if the FDIC's ability to perform purchase and assumption transactions is unimpaired, another consideration affecting its role as insurer may mandate protection. Both fraudu-

457. *Id.*

458. *Id.*

459. Barnett, Horvitz, & Silverberg, *supra* note 61, at 310 n.5.

460. *Id.*

461. *See supra* note 53 and accompanying text.

462. Portis, *supra* note 48, at 261 n.22.

463. *Gunter*, 674 F.2d at 865.

464. *Id.*

465. The FDIC was able to arrange 164 purchase and assumption transactions in 1988. FDIC, *supra* note 1, at 18.

lent transferee liability and enforcement of secret agreements have another—and more harmful—effect, the detrimental financial impact on the insurance fund.

A financial impact on the FDIC, whether from fraudulent transfer liability or the enforcement of a secret agreement, hurts the FDIC's ability to act as insurer.⁴⁶⁶ The FDIC's success as insurer depends on the size of the insurance fund the FDIC maintains.⁴⁶⁷ In turn, the insurance fund's size depends upon several factors, including the amount of insurance premiums paid by member banks,⁴⁶⁸ the FDIC's ability to collect from obligors of failed banks on assets the FDIC now holds,⁴⁶⁹ and the FDIC's success in finding healthy banks willing to participate in purchase and assumption transactions.⁴⁷⁰

Congressional legislation demonstrates that depletion of the insurance fund is detrimental to important federal interests.⁴⁷¹ Both fraudu-

466. *Hearings, supra* note 1 (statement of Rep. Annunzio).

467. Obviously, deposit insurance only prevents runs on banks through its own solvency and ability to pay claims. A shortage of deposit insurance funds could set off a nationwide run on troubled banks, exhausting all insurance reserves. E. KANE, *supra* note 449, at 4. This would be "politically disruptive" as Congress would have to do some "wild bureaucratic scrambling" to decide how to make good on its guarantees. *Id.* While theoretically the federal government could just print more money, that alternative could damage the economy in other ways. See generally R. BRYANT, *CONTROLLING MONEY: THE FEDERAL RESERVE AND ITS CRITICS* 109-12 (1983) (analyzing control of "money stock" as tool to achieve high employment, low inflation, and growth of GNP).

468. 12 U.S.C. § 1817(c) (1988). FIRREA has raised the insurance premiums for both the Bank Insurance Fund and the Savings Association Insurance Fund. FIRREA, Pub. L. No. 101-73, § 208(c), 103 Stat. 183, 208 (1989). The 1989 Bank Insurance Fund (BIF) rate was 8.3 cents for every 100 dollars of deposits. *Id.* In 1990 this rose to 12 cents and in 1991 it will rise to 15 cents. *Id.* The 1989 Savings Association Insurance Fund (SAIF) premium was 20.8 cents for every 100 dollars of deposits. *Id.* at 209. From 1991 to 1993 the SAIF premium will rise to 23 cents. *Id.* There will then be a decrease for the next three years to 18 cents per 100 dollars. *Id.* After 1998, the SAIF rate will be the same as that of the BIF, 15 cents. *Id.* The insurance premiums charged to member banks are passed on to depositors in the form of lower paying interest rates on deposits and higher interest rates on loans.

469. *Gunter*, 674 F.2d at 865.

470. *Id.* If the FDIC is unable to find a willing bank, the FDIC must instead liquidate the failed bank. *Id.* A liquidation entails large cash expenditures from the insurance fund to pay off the bank's depositors, and is one of the reasons the FDIC favors purchase and assumption transactions. Note, *supra* note 5, at 261. The FDIC estimates that it saved over \$3 billion in 1988 by arranging purchase and assumption transactions instead of liquidations. FDIC, *supra* note 1, at 9. The larger the failed bank is, and the more restrictive the branching laws under which it operates, the more difficult it is for the FDIC to find a willing purchaser. E. KANE, *supra* note 449, at 48. For a discussion of the FDIC's options when faced with a failed bank, see *supra* notes 37-61 and accompanying text.

471. 12 U.S.C. § 1823(e) (1988). Congressional intent to protect the FDIC is evinced by Congress' recent amendment of section 1823(e) to expand the section's coverage to the FDIC as receiver. FIRREA, Pub. L. No. 101-73, § 217, 103 Stat. 183, 256 (1989) (to be codified at 12 U.S.C. § 1823(e)).

lent transferee liability and enforcement of secret agreements deplete the insurance fund⁴⁷² because the FDIC cannot collect upon the "bad" asset, whether it is acquired through a liquidation or a purchase and assumption transaction.⁴⁷³ It is in this manner that both affect the FDIC's ability to function as insurer.

IV. RECOMMENDED LEGISLATION

The problem of FDIC fraudulent transferee liability may have a simpler solution than expecting judges to interpret conflicting statutes and policies correctly. A uniform rule, rather than a myriad of judicial devices, is the best way to protect the FDIC. Congress has repeatedly manifested its desire to protect the banking industry and the FDIC, as evidenced most recently by the provisions of FIRREA.⁴⁷⁴ It is time for Congress to speak again through clear and unambiguous legislation.

Congress codified the *D'Oench, Duhme*⁴⁷⁵ doctrine in section 1823(e) of Title 12,⁴⁷⁶ thereby protecting the FDIC from certain state-law defenses.⁴⁷⁷ Congress could similarly protect the FDIC from fraudulent transferee liability by adopting the reasoning of the *United States v.*

472. Judge Posner recognizes that when a person defrauds a bank whose deposits are insured by the FDIC, while some of the costs may be borne by stockholders, most will be borne by the federal government. R. POSNER, *supra* note 133, at 601.

473. Note, *supra* note 5, at 282.

474. Pub. L. No. 101-73, 103 Stat. 183 (1989). FIRREA includes many new regulatory provisions. First, savings institutions must meet tough new capital requirements. The core capital requirement is 3%. *Id.* § 301, 103 Stat. 304. The tangible capital requirement is 1.5%. *Id.* The intangible capital, including "goodwill," may not exceed a certain percentage of the total assets as follows:

Prior to January 1, 1992	1.500%
January 1, 1992 to December 31, 1992	1.000%
January 1, 1993 to December 31, 1993	0.750%
January 1, 1993 to December 31, 1995	0.375%
Thereafter	0%

Id. S&Ls failing to meet the requirements will be subject to strict restrictions. *Id.* at 307-08. Second, savings institutions must divest all junk bonds by July 1, 1994. *Id.* § 222, at 270. Third, enforcement powers over officers and directors are broadened to include consultants, joint venture partners, agents, independent contractors and others who deal with savings institutions. *Id.* § 901, at 446. Fourth, civil money penalties are authorized up to \$1 million. *Id.* § 951, at 498. Fifth, criminal penalties up to thirty years imprisonment are authorized and the statute of limitation for banking crimes is increased to ten years. *Id.* § 961, at 499. Sixth, the notification requirement prior to terminating an institution's deposit insurance is shortened from 120 to 30 days. *Id.* § 926, at 489-90. Finally, rewards for whistle-blowers are authorized up to \$100,000 or 25% of the assessed fine, whichever is less. *Id.* § 933, at 496.

475. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942).

476. 12 U.S.C. § 1823(e) (1988).

477. See *supra* notes 88-104 and 282-306 and accompanying text.

*Kimbell Foods, Inc.*⁴⁷⁸ line of cases⁴⁷⁹ and extending to the FDIC holder-in-due-course status whenever the FDIC sues upon the assets of a failed bank. Such congressional action would not only protect the FDIC from state-law defenses not precluded by *D'Oench, Duhme* or section 1823(e), but would also automatically bring the FDIC within the protection of Bankruptcy Code section 550(b).⁴⁸⁰

V. CONCLUSION

As more and more financial institutions fail, the FDIC's importance grows. Through passage of FIRREA, Congress has acted—at great cost to taxpayers—to ensure the continued vitality of the United States banking system.⁴⁸¹ Estimates of the cost of the federal bailout of the savings and loan industry run anywhere from 50 billion⁴⁸² to 500 billion dollars.⁴⁸³ Given these staggering costs, failure to protect the FDIC from fraudulent transferee liability could seriously undermine interests that Congress has resolved to defend.

Perhaps the banking industry deserves no protection at all. Without regulation, the market might provide both the incentives and balance the banking industry so desperately needs. Perhaps banks that are managed wisely and responsibly would succeed and those that are not would fail. In that situation, depositors would have the same recourse available to unsecured creditors when any other business fails.

This scenario, however, was not envisioned by Congress when it originally established the FDIC, nor is it consistent with Congress' hopes today.⁴⁸⁴ The recent passage of FIRREA leaves no room for judicial uncertainty about congressional intent. The United States Supreme

478. 440 U.S. 715 (1979).

479. See *supra* notes 105-25 and 308-52 and accompanying text.

480. Congress has authorized a study to determine the impact of the various state and federal bankruptcy exemptions on the insurance fund. FIRREA, Pub. L. No. 101-73, § 1001, 103 Stat. 183, 507-08 (1989). The study, to be conducted by the Secretary of the Treasury and submitted to Congress within eighteen months of the passage of FIRREA, is to include the feasibility of (1) uniform exemptions; (2) limits on exemptions when necessary to repay obligations owed to FDIC-insured depository institutions; and, (3) requiring borrowers from FDIC-insured depository institutions to post a personal or corporate bond when obtaining a real property mortgage. *Id.*

481. FIRREA, Pub. L. No. 101-73, 103 Stat. 183 (1989).

482. Rosenblatt, *Up to \$100 Billion Extra Sought for S&L Rescues*, L.A. Times, Nov. 1, 1989, at A1, col. 2.

483. Pine, *Keating Predicts S&L Bailout Will Cost \$500 Billion*, L.A. Times, Jan. 15, 1990, at D2, col. 2.

484. See generally FIRREA, Pub. L. No. 101-73, 103 Stat. 183 (1989); Federal Deposit Insurance Act, Pub. L. No. 81-797, 64 Stat. 873 (1950) (codified as amended at 12 U.S.C. §§ 1811-32 (1988)).

Court has long recognized the importance of the FDIC's role and the Court continues to do so.⁴⁸⁵ Until such time as Congress directly addresses the issue, the judiciary should not hesitate to protect the FDIC from fraudulent transferee liability.⁴⁸⁶

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485. *See, e.g.*, *Langley v. FDIC*, 484 U.S. 86 (1987) (FDIC protected by interpretation of federal statute); *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942) (FDIC protected by federal common law).

486. One commentator notes that in drafting a statute, Congress takes into account the issues that have been litigated during the preceding 20 or 25 years. G. GILMORE, *THE AGES OF AMERICAN LAW* 96 (1977). Characteristically, as has happened with respect to the FDIC, "the focus of litigation has a way of shifting unexpectedly and unpredictably. New issues, which no one ever dreamed of, present themselves for decision." *Id.* When that happens, "reformulation of an obsolete statutory provision is quite as legitimately within judicial competence as the reformulation of an obsolete common law rule." *Id.* at 97.

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