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Assets in Foreign Branches Off Limits to Domestic Judgment Creditors

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New York's high court announced last week that banking institutions with branches in New York are shielded from judgment creditors attempting to collect on customer assets held at foreign branches of the same bank. Specifically, the New York Court of Appeals affirmed the validity of a longstanding common-law doctrine known as the "separate entity" rule, which maintains that a bank's foreign branches should be treated as separate and distinct legal entities from its New York branches for purposes of pre-judgment attachments and post-judgment turnover notices. "In other words, a restraining notice or turnover order served on a New York branch will be effective for assets held in accounts at that branch, **but will have no impact on assets in other branches**." *Motorola Credit Corp. v. Standard Chartered Bank*, 2014 N.Y. Slip Op. 7199, at *2 (N.Y. Oct. 23, 2014) (emphasis added).

With the highest court in the state squarely addressing and upholding the age-old "separate entity" doctrine, banks can rest assured that assets held in their foreign branches are safe from claimants attempting to enforce New York judgments. Nevertheless, while the separate entity rule may now be a solid part of New York jurisprudence as it relates to the collection efforts of judgment creditors, the excoriating dissent authored by the newest member of the Court of Appeals, Associate Judge Sheila Abdus-Salaam, is sure to provoke legislative discussion that banks should closely monitor.

The two-judge dissent chastised the five-judge majority for engaging in "improper judicial legislation," *id.* at *6, and ratifying an "anachronistic rule" that ran afoul of prior Court of Appeals precedent, public policy and the ability of judgment creditors to obtain justice, *id.* at *7. The dissent's dissatisfaction was not reserved for the majority, but was directed at the banks and their supporting *amicus* as well. The dissent questioned the banks' "blind and unwavering adherence to legal norms birthed in the bygone era which that [separate entity] rule represents, for the government, banks and bank customers have shifted their practices and expectations to conform to a very different modern reality." *Id.* at *8. Issues of international comity and practical burdens in the tech-savvy, interconnected world could not support continued application of the separate entity rule, especially given the "complex and far-reaching government regulations" that banks are now subject to and that have not dissuaded them from continuing to do business in the U.S.

Case Background

Motorola Credit Corp. initiated litigation in 2003 over a $2 billion unpaid loan to a Turkish telecommunications company intended to finance a major expansion of the companies'

operations. Several members of a the Uzan family, a family of Turkish nationals that induced Motorola to loan the funds, defrauded Motorola by diverting a substantial portion of the loaned funds to themselves and other entities. Motorola obtained two judgments against the Uzans totaling over $3 billion in compensatory and punitive damages. Motorola also was able to freeze some $30 million of the Uzan's assets that were held in Standard Chartered Bank's (SCB) United Arab Emirates (U.A.E.) branch.

The asset freeze led to intervention by authorities in both the U.A.E. and Jordan, with the U.A.E. Central Bank unilaterally debiting about $30 million from SCB's own account. SCB subsequently moved for relief from the restraining order in the U.S. district court, which applied the separate entity rule and precluded Motorola from restraining the Uzan's assets at SCB's foreign branches. Motorola appealed and the U.S. Court of Appeals for the Second Circuit certified the issue of the validity of the separate entity rule to the New York Court of Appeals for decision.

Case Analysis

In certifying the question to the New York Court of Appeals, the Second Circuit acknowledged that New York's high court had never expressly adopted the separate entity doctrine. Quite the opposite; the Second Circuit questioned whether the doctrine was still good law following the New York Court of Appeal's 2009 decision in *Koehler v. Bank of Bermuda Ltd.*, 12 N.Y.3d 533 (N.Y. 2009). In *Koehler*, the Court of Appeals held that a judgment creditor could seek the turnover of stock certificates located outside the U.S. where the court had personal jurisdiction over the party in control of the property.

The New York Court of Appeals accepted the certified question and acknowledged the continued validity of the common-law separate entity doctrine. The majority's decision emphasized the benefits that the separate entity doctrine provided to international banks that opened branches in New York. *See Motorola*, 2014 N.Y. Slip Op. at *3. Those benefits included the limitation of competing claims that could otherwise be asserted against banks, the risk of double liability domestically and abroad, and the severe burden banks would otherwise face "to monitor and ascertain the status of bank accounts in numerous other branches." *Id.*

More importantly, however, the majority seemed to focus on the banks' expectation in and entitlement to the continued receipt of those benefits because the separate entity rule was a "firmly established principle of New York law" since at least 1916, notwithstanding the Court of Appeals' silence on the matter. *Id.* at *4. According to the majority: "Undoubtedly, international banks have considered the doctrine's benefits when deciding to open branches in New York, which in turn has played a role in shaping New York's status as the preeminent commercial and financial nerve center of the Nation and the world." *Id.* at *6.

The majority also discounted the role that technological advancements impacting centralized banking have on the considerations favoring the continued application of the separate entity rule. Rather, the majority focused on the fact that "courts have continued to recognize the practical constraints and costs associated with conducting a worldwide search for a judgment debtor's assets." *Id.* at *6.

Finally, the majority distinguished *Koehler* by explaining that the foreign bank in that case had failed to raise the separate entity rule and that the facts in that case involved neither bank branches nor assets held in bank accounts. Thus, the majority asserted that *Koehler* "did not analyze, much less overrule, the separate entity doctrine." *Id.* at *5.

The dissent sharply criticized each of the majority's rationales. The dissent took issue with the majority's failure to respect the legislatively enacted statutory scheme governing restraining notices and claimed the majority had engaged in improper legislative action. The dissent also focused on the "outmoded" and "obsolete" nature of the separate entity rule in an age where banks can easily obtain information concerning assets held at its various global branches. *Id.* at *6, *7. According to the dissent: "In broader terms, today's holding permits banks doing business in New York to shield customer accounts held in branches outside of this country, thwarts efforts by judgment creditors to collect judgments, and allows even the most egregious and flagrant judgment debtors to make a mockery of our courts' duly entered judgments." *Id.* at *7.