*To be Submitted by:*
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# New York Supreme Court

## Appellate Division—First Department

THE RECEIVERS OF SABENA SA,

*Plaintiff-Respondent-Cross-Appellant,*

– against –

DEUTSCHE BANK A.G. and DEUTSCHE BANK TRUST COMPANY AMERICAS,

*Defendants-Appellants-Cross-Respondents.*

## BRIEF OF *AMICUS CURIAE* THE CLEARING HOUSE ASSOCIATION L.L.C. IN SUPPORT OF THE APPELLANTS

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## PRELIMINARY STATEMENT

Any banking system requires certainty, which is fostered by clear rules. Article 4A of the Uniform Commercial Code ("U.C.C.") was enacted by the New York Legislature to "promote certainty and finality" in the banking system. *Grain Traders, Inc.* v. *Citibank, N.A.*, 160 F.3d 97, 102 (2d Cir. 1998). Legal developments that introduce ambiguity into Article 4A "[u]ndermin[e] the efficiency and certainty of funds transfers in New York [and] could, if left uncorrected, discourage dollar-denominated transactions and damage New York's standing as an international financial center." *Shipping Corp. of India Ltd.* v. *Jaldhi Overseas PTE Ltd.*, 585 F.3d 58, 62 (2d Cir. 2009). Moreover, it is particularly important to preserve certainty where, as with the U.C.C., one set of rules should apply uniformly across all fifty states.

The Clearing House Association L.L.C. ("The Clearing House") submits that the court below erred in its application of Article 4A of the U.C.C. and thus introduced uncertainty into banking in New York. The court found that a funds transfer[1] that was blocked by a presidential Executive Order and related

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[1] We will use the expression "funds transfer," rather than the shorthand "EFT" (which stands for "electronic funds transfer"), in these submissions, except when reciting direct quotations from the case law. Although the case law has often used the shorthand "EFT," the U.C.C. uses the more exact expression "funds transfer" (*see* N.Y. U.C.C. § 4A-104(a)), which is broader and conveys the reality that these transfers need not necessarily be made through electronic means. A funds transfer is "the series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order. The

regulations midstream at an intermediary bank was merely "interrupted" and, after the blocking order was lifted fourteen years later, should continue and funds should be paid to the intended beneficiary, Sabena S.A. ("Sabena," now represented by its receivers in bankruptcy). This legal conclusion runs contrary to Article 4A, which provides two clear and simple rules. First, until an intermediary bank accepts a payment order by executing it, that bank has no obligation to a beneficiary's bank (and none at all to an intended beneficiary, to whom it never has any liability). Second, transfers that are not promptly executed by an intermediary bank are "cancelled by operation of law at the close of the fifth funds-transfer business day of the receiving bank" (N.Y. U.C.C. § 4A-211(4)). In the event of a payment order cancellation, the intermediary bank then must refund any payment received to the bank that sent the payment order (N.Y. U.C.C. § 4A-402). This is precisely what Deutsche Bank Trust Company Americas ("DBTCA") did in the case at hand, yet the decision below held that it may be found liable to an intended beneficiary.

The court below apparently relied upon decisions which, respectfully, are either irrelevant to or in error on this point: *Bank of New York* v. *Norilsk Nickel*, 14 A.D.3d 140, 789 N.Y.S.2d 95 (N.Y. App. Div. 2004); *European American Bank* v. *Bank of Nova Scotia*, 12 A.D. 3d 189, 784 N.Y.S.2d 99 (N.Y.

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term includes any payment order issued by the originator's bank or an intermediary bank intended to carry out the originator's payment order." U.C.C. § 4A-104(1)

App. Div. 2004); and *Goodearth Maritime Ltd.* v. *Calder Seacarrier Corp.*, 387 Fed.Appx. 19 (2d Cir. 2010). In dealing with competing claims over transferred funds that remained in the hands of an intermediary bank, these cases started with a correct premise—that funds in the hands of an intermediary bank are not the property of the originator or of the beneficiary of the funds transfer and thus cannot be attached by the creditors of either—but then reached incorrect conclusions about where the amount of long-blocked funds transfers should go after the block was lifted. Each of these decisions is distinguishable from the present case, and moreover their results are not consistent with the law established by the New York Legislature in the U.C.C. The Clearing House urges this Court to reverse the decision below and find that DBTCA acted properly and consistently with the U.C.C.[2]

Well-established principles are available to guide this Court. First, the unambiguous provisions of a statute enacted by the Legislature must be applied by the courts. *See Caminetti* v. *U.S.*, 242 U.S. 470, 484 (1917); *U.S.* v. *Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241 (1989); *Dodd* v. *U.S.*, 545 U.S. 353, 359

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[2] Because none of the decisions relied on by the court below confronted and resolved the situation presented in this case, it may be that this Court finds that it has no need to overrule those earlier decisions. But if this Court believes that *Norilsk Nickel* or *European American Bank* actually held that an intermediary bank must send the amount of a long-blocked funds transfer to the beneficiary when the block is lifted, then this court has the authority to overrule its prior decisions when they clearly misinterpreted or overlooked a statutory provision or a binding precedent. *See, e.g.*, *George Campbell Painting* v. *National Union Fire Ins. Co. of Pittsburgh, PA*, 92 A.D.3d 104, 105-06, 937 N.Y.S.2d 164, 164-166.

(2005); *Lamie* v. *U.S. Trustee*, 540 U.S. 526, 534 (2004); *Central Trust Co., Rochester, N. Y.* v. *Official Creditors' Committee of Geiger Enterprises, Inc.*, 454 U.S. 359-360, 358 (1982). This is especially true with respect to Article 4A of the U.C.C., which was enacted precisely because the Legislature concluded that, prior to its enactment, "[j]udicial authority with respect to funds transfers [was] sparse, undeveloped and not uniform." N.Y. U.C.C. § 4A-102 (McKinney 2013), Official Comment, at p. 226. Indeed, "[i]n the drafting of Article 4A, a deliberate decision was made to write on a clean slate and to treat a funds transfer as a unique method of payment to be governed by unique rules that address the particular issues raised by this method of payment." *Id.* In other words, the Legislature intended that the express provisions of the U.C.C. would govern funds transfers. The courts must respect this clear intent when applying Article 4A.

Second, neither the originator nor the beneficiary of a funds transfer have any contractual or other legal rights against an intermediary bank, because they are not in privity with that bank. *See Export-Import Bank of U.S.* v. *Asia Pulp & Paper Co., Ltd.*, 609 F.3d 111, 121 (2d Cir. 2010) ("[A]n originator and intended beneficiary have no legal claim or contractual rights against an intermediary bank in the event that a funds transfer is not completed"); *Jaldhi*, 585 F.3d at 71; *Scanscot Shipping Services GmbH* v. *Metales Tracomex LTDA*, 617

F.3d 679, 682 (2d Cir. 2010); *Allied Maritime, Inc.* v. *Descatrade SA*, 620 F.3d 70, 75 (2d Cir. 2010).

Third, in enacting Article 4A of the U.C.C., the Legislature intended a funds transfer to be a predictable transfer mechanism that could be used to make orderly payments on an international scale. Consistent with this intent, a payment order that is not executed by an intermediary bank within five business days is cancelled by operation of law. N.Y. U.C.C. § 4A-211(4). This avoids the uncertainty that would arise from leaving stale payment orders unresolved between banks for indefinite periods of time.

Last, in the event that a payment order is cancelled, by operation of law or otherwise, the intermediary bank's only obligation is to provide a reimbursement in the amount of the cancelled order to the bank that sent it the payment order.[3] N.Y. U.C.C. § 4A-402(4).

Considered together, these principles lead to an inescapable conclusion: when government regulations such as the ones at issue in this appeal prevent an intermediary bank from executing a payment order for more than five business days, the payment order is cancelled by operation of the U.C.C. Thereafter, the intermediary bank's *only* obligation is to provide a reimbursement

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[3] The bank sending the payment order to the intermediary bank is often, as here, the originator's bank, but in the case of a funds transfer involving multiple intermediary banks in succession it would be another intermediary bank.

to the bank that sent it the payment order. These are not novel or untested propositions. Indeed, the United States Court of Appeals for both the Second Circuit and the D.C. Circuit have specifically recognized that when a funds transfer is blocked by regulations administered by the Office of Foreign Assets Control ("OFAC"), the payment order is cancelled and the intermediary bank's only obligation is to the bank that sent it a payment order.[4] *Calderon-Cardona* v. *Bank of New York Mellon*, --- F.3d ---, 2014 WL 5368880, at *6 (2d Cir. Oct. 23, 2014); *Hausler* v. *JPMorgan Chase Bank, N.A.*, --- F.3d ---, 2014 WL 5420141, at *2 (2d Cir. Oct 27, 2014); *Heiser* v. *Islamic Republic of Iran*, 735 F.3d 934, 941 (D.C. Cir. 2013).

In the decision below, the court should have applied these principles and found that DBTCA acted correctly in refusing to forward funds to the intended beneficiary of a funds transfer that had been blocked for over fourteen years. Instead, it relied on the notion of an "interruption" of a funds transfer. According to the lower court, an "interruption" temporarily restrains, but does not cancel, a transfer. This notion of an "interruption," however, is only a judicially-created concept with no statutory support in the U.C.C. or elsewhere. Under Article 4A of the U.C.C., the Legislature has determined that payment orders are either executed

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[4] As will be discussed below, the ruling on appeal is at odds with the Second Circuit's rulings on this issue and, as a result, threatens to create significant inconsistency within New York's court system.

within five days or cancelled. Funds transfers do not remain in limbo for indeterminate periods of time.

This judicial creation of a new rule for blocked funds transfers—one at odds with the express provisions of the U.C.C. enacted by the Legislature—ignores the well-established principles discussed above and undermines the goals of the statutory scheme. Article 4A of the U.C.C. "was enacted to provide a 'comprehensive body of law that defines the rights and obligations that arise from wire transfers.'" *Asia Pulp & Paper*, 609 F.3d at 118, citing *Banque Worms* v. *BankAmerica Int'l*, 77 N.Y.2d 362, 369, 568 N.Y.S.2d 541, 545 (1991). Its goals include "[n]ational uniformity in the treatment of electronic funds transfers," as well as "speed, efficiency, certainty … and finality." *Banque Worms*, 77 N.Y.2d at 372, 568 N.Y.S.2d at 547. As the court underscored in *Jaldhi*, 585 F.3d at 62, "efficiency is fostered by protecting the intermediary banks." The ruling on appeal does just the opposite, by holding that an intermediary bank could be liable to an intended beneficiary despite compliance with the U.C.C. It also undermines the certainty provided by the U.C.C.—under this precedent, intermediary banks can no longer rely on clear statutory provisions, and funds transfers originators and originators' banks can no longer rely on the assurance that their funds will be returned if an intermediary bank fails to execute a payment order.

For these reasons, The Clearing House asks the Court to "take this opportunity to … untangle the doctrinal knot" created by the decision below. *Jaldhi*, 585 F.3d at 64.

## BACKGROUND

### A. The Interest of The Clearing House

The Clearing House has a substantial interest in the issues raised by this case because it plays a key role in the domestic and international movement of funds. Established in 1853, The Clearing House is the oldest banking association and payments company in the United States. It is owned by the world's largest commercial banks, which collectively hold more than half of all U.S. deposits and which employ over one million people in the United States and more than two million people worldwide. The Clearing House is a nonpartisan advocacy organization that represents the interests of its owner banks by developing and promoting policies to support a safe, sound, and competitive banking system that serves customers and communities. Its affiliate, The Clearing House Payments Company L.L.C., which is regulated as a systemically important financial market utility, owns and operates the Clearing House Interbank Payments System ("CHIPS"), a funds-transfer system that serves 48 U.S. and foreign banks. Every day, CHIPS processes on average over 420,000 payment orders, with an average

daily value of 1.559 trillion dollars as of August 31, 2014.[5] Additionally, the members of The Clearing House routinely act as originators' banks, intermediary banks, and beneficiaries' banks in funds transfers.

It is no exaggeration to say that the ruling below threatens to have an adverse effect on the U.S. payments system. That ruling not only creates uncertainty and potential liability for an intermediary bank when it is forced to choose to follow either the applicable statute or the result below, it also throws a cloud of uncertainty over any clear statutory scheme by permitting a court to ignore existing legislation and create its own rules.

Consequently, The Clearing House has a vested interest in maintaining the statutory framework and the clarity that the U.C.C. provides to the rules that govern funds transfers. The Clearing House respectfully requests that the Court consider this memorandum of law addressing the important systemic banking issues raised by the appellants Deutsche Bank A.G. and DBTCA (the "Appellants"). As discussed above, clear rules ensure the continued efficiency of the transfer of funds. This is why The Clearing House is asking the Court to rectify a judicial interpretation of the U.C.C. which directly contravenes the statutory language and thereby introduces uncertainty not only to the directly relevant rule, but to the entire body of U.C.C. rules.

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5 *See* The Clearing House's website at https://www.theclearinghouse.org.

### B. The Mechanics of Funds Transfers

Many funds transfers, particularly international transfers, entail a series of transactions involving different counterparties. *See* N.Y. U.C.C. § 4A-104(1) (defining "Funds transfer").[6] The originator instructs its bank to transfer funds from the originator's account to the account of a beneficiary at the beneficiary's bank. In many international transactions, the originator's bank then asks an intermediary bank, at which the originator's bank has an account, to transfer funds from the originator's bank's account at the intermediary bank to the beneficiary's bank's account at the same intermediary bank or at another bank.

Importantly, Article 4A is designed to limit the exposure of intermediary banks. The originator and the beneficiary usually are in privity with one another in some underlying transaction, but neither is ever in privity with the

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[6] The court in *Jaldhi*, 585 F.3d at 61, n.1, summarizes a funds transfer as follows:

> An EFT is nothing more than an instruction to transfer funds from one account to another. ... If the banks [*i.e.*, the originator's bank and the beneficiary's bank, respectively] are not in the same consortium—as is often the case in international transactions—then the banks must use an intermediary bank. To use an intermediary bank to complete the transfer, the banks must each have an account at the intermediary bank (or at different banks in the same consortium). After the originator directs its bank to commence an EFT, the originator's bank would instruct the intermediary to begin the transfer of funds. The intermediary bank would then debit the account of the bank where the originator has an account and credit the account of the bank where the beneficiary has an account. The originator's bank and the beneficiary's bank would then adjust the accounts of their respective clients.

intermediary bank.[7] For this reason, "EFTs are neither the property of the originator or the beneficiary while briefly in the possession of an intermediary bank." *Jaldhi*, 585 F.3d at 71; *see also Asia Pulp & Paper*, 609 F.3d at 121; *Scanscot Shipping Services*, 617 F.3d at 682 ("After an EFT is initiated by an originator's bank, the funds at issue cease to be the property of the originator; the funds do not then become the property of the beneficiary until the EFT is completed by acceptance of a payment order by the beneficiary's bank"); *Allied Maritime*, 620 F.3d at 75. Thus, a funds transfer should be understood as an operation in which the intermediary bank plays a limited—albeit essential—role and takes on commensurately limited risk.

### C. The Present Proceedings

Sabena, the national airline of Belgium, provided aircraft repair services to Sudan Airways. As payment, on November 4, 1997, Sudan Airways asked its bank, the National Bank of Abu Dhabi, to originate a funds transfer in the sum of $360,500 to the benefit of Sabena. Bankers Trust Company (of which DBTCA is the successor) acted as the intermediary bank. When the funds transfer arrived at Bankers Trust Company, it was blocked under an Executive Order and

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[7] As will be discussed in more detail below, an intermediary bank can only ever be in privity (i) with the bank that sends it a payment order (which the intermediary bank will be obligated to reimburse if it does not execute the payment order—*see* N.Y. U.C.C. § 4A-402(4)) and, (ii) if it executes the payment order, with the beneficiary's bank (N.Y. U.C.C. § 4A-402(2)). The intermediary bank is thus effectively insulated from both the originator and the beneficiary.

regulations applying to "all property and interests in property of the Government of Sudan" within the United States. R., at 15. *See* Exec. Order No. 13067, November 3, 1997, 62 Fed. Reg. 59, 989; Sudanese Sanctions Regulations, 31 C.F.R. Part 538 (1998).

On March 5, 2012—more than fourteen years after the funds transfer had been originated—the U.S. government lifted the block on the funds. The Receivers of Sabena (Sabena had since filed for bankruptcy in Belgium) asked DBTCA to forward the amount of that funds transfer to them. DBTCA, relying on the relevant provisions of the U.C.C., instead returned the amount of the funds transfer to the originator's bank. R., at 18-19.

Sabena brought this action against the Appellants, who moved for dismissal of the complaint pursuant to N.Y. C.P.L.R. § 3211(a)(7). They relied on the arguments that, under the U.C.C., a payment order that is not executed is cancelled by operation of law and that, in any event, an intermediary bank could under no circumstances be found liable to an intended beneficiary. R., at 21. The court below disagreed and denied the motion to dismiss.

The Clearing House submits that DBTCA indisputably followed the proper course of action by adhering to the requirements of the U.C.C. and returning the funds at issue to the originator's bank. There is no ambiguity in the

U.C.C. on this matter and, therefore, no leeway for the court to come to a different conclusion. The court below erred by denying the motion to dismiss.

## ARGUMENT

### I. UNDER THE U.C.C., A PAYMENT ORDER IS CANCELLED BY OPERATION OF LAW IF NOT ACCEPTED BY EXECUTION WITHIN FIVE BUSINESS DAYS. AN INTERMEDIARY BANK THEN MUST REFUND ANY PAYMENT IT RECEIVED TO THE BANK THAT SENT THE PAYMENT ORDER AND HAS NO OTHER LIABILITY WITH RESPECT TO THOSE FUNDS.

In the case at hand, the U.C.C. determines the rights and obligations of the parties once the block on the funds is lifted. The Executive Order and the regulations involved did not conflict with the U.C.C. This is not a situation that triggers preemption because there is no conflict between federal and state law. The federal blocking order and the federal regulations have nothing to do with property interests in a funds transfer and the court's ultimate disposition of a funds transfer. State law controls on these matters, and therefore the only issue on appeal is the correct application of the U.C.C.[8]

The U.C.C. provides a clear and simple rule where an intermediary bank fails to execute a payment order it receives: the order "is cancelled by

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[8] The case on which the court below relied most heavily, *Norilsk Nickel*, 14 A.D.3d at 145-146, 789 N.Y.S.2d at 99-100, characterized the interplay between regulations like the ones at issue and state law as follows: "[W]hile the UCC determined title to the funds at issue, federal law impeded movement of those funds beyond the locus." It correctly found that the U.C.C. applies to determine who is entitled to the disposition of blocked funds. The court in *Norilsk Nickel* only erred subsequently in its analysis, when it allowed a long-blocked funds transfer to be paid to the intended beneficiary after the block was lifted (*see infra* Part II.A). *See also Ruth Calderon-Cardona* v. *JP Morgan Chase Bank, N.A.*, 867 F.Supp.2d 389, 400 (S.D.N.Y. 2011) ("Article 4-A of New York's Uniform Commercial Code ... delineates the extent of parties' property interests in blocked EFTs"), *aff'd in part*, *Calderon-Cardona*, 2014 WL 5368880, at *6; *Hausler*, 2014 WL 5420141, at *2.

operation of law at the close of the fifth funds-transfer business day." N.Y. U.C.C. § 4A-211(4). The court below and the cases it relied upon ignored this rule. These cases appear to create a judge-made exception that would apply in situations where an "interference"—such as a federal government freeze of funds or an attempted attachment—prevents an intermediary bank from executing a payment order. This is contrary to the well-established principle of statutory interpretation and application, that "the meaning of a statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain, and if the law is within the constitutional authority of the lawmaking body which passed it, *the sole function of the courts is to enforce it according to its terms*." *Caminetti*, 242 U.S. at 484 (emphasis added); NORMAN SINGER & J.D. SHAMBIE SINGER, SUTHERLAND STATUTES AND STATUTORY CONSTRUCTION § 46:1 (7th ed. 2007) ("Courts are not free to read unwarranted meanings into an unambiguous statute, even to support a supposedly desirable policy not effectuated by the act as written.")

### A. There is No Provision in New York Law Providing for a Transfer "Interruption".

The most compelling reason for rejecting the ruling of the court below is that it relies upon a judicially-created notion of a transfer "interruption" that is inconsistent with the plain statutory language. Indeed, the court below concluded its analysis of Appellants' arguments regarding Article 4A of the U.C.C. by holding that, "the Executive Order here did not cause the transfer of the Blocked

Funds to fail or be cancelled, the Executive Order was simply an 'interruption' of the transfer." R., at 24. In so doing, it adopted a concept that is entirely foreign and contrary to the provisions of the U.C.C.

Under Article 4A, payment orders in furtherance of a funds transfer have a short shelf-life. An intermediary bank has five business days to accept a payment order, which it can do only by executing the order. N.Y. U.C.C. § 4A-211(4). Indeed, it "accepts a payment order when it *executes* the order." N.Y. U.C.C. § 4A-209(1) (emphasis added). More specifically, "[a] payment order is 'executed' by the receiving bank when it issues a payment order intended to carry out the payment order received by the bank." N.Y. U.C.C. § 4A-301(1). Thus, a payment order is either executed by an intermediary bank within five days or is cancelled "by operation of law." N.Y. U.C.C. § 4A-211(4). The official comment to the U.C.C.—which has been recognized as "authoritative", *see Jaldhi*, 585 F.3d at 71—explains the rationale behind this rule:

> [Subsection 4A-211(4)] deals with *stale payment orders*. Payment orders normally are executed on the execution date or the day after. ... If a payment order is not accepted on its execution or payment date or shortly thereafter, it is probable that there was some problem with the terms of the order or the sender did not have sufficient funds or credit to cover the amount of the order. Delayed acceptance of such an order is normally not contemplated, but the order may not have been cancelled by the sender. [Subsection 4A-211(4)] *provides for cancellation by operation of law to prevent an unexpected delayed acceptance.*

(N.Y. U.C.C. § 4A-211 (McKinney 2013), Official Comment No. 7, at p. 281; emphasis added)

This comment is particularly relevant to the present case. Here, the funds were blocked for over fourteen years. It is difficult to imagine a more "stale" payment order, or a set of circumstances that could less conceivably be styled as a mere "interruption." The rule cancelling unaccepted payment orders after five days is categorical and does not allow for exceptions.

More fundamentally, there is no principled basis for courts to distinguish between events that cancel a payment order under § 4A-211 of the U.C.C. and events that merely "interrupt" the transfer, within the meaning of the judicial doctrine relied on below. Why should the sender's failure to keep sufficient funds in its account to cover the payment order or some clerical error in the order's terms cancel an order in progress, whereas regulations that block funds for over a decade will merely "interrupt" the transfer? These are all events that are beyond the control of the beneficiary, but the U.C.C. nevertheless provides that they cancel the transfer. In enacting this rule, the Legislature decided—as it was entitled to do—that any impact on beneficiaries created by cancelling payment orders that fail to be executed by an intermediary bank within five days is outweighed by the need to avoid harm to the originator and to create the certainty that no stale payment orders remain in the pipeline.

### B. Deutsche Bank Trust Company Americas Incurred No Liability To Sabena.

The error of the court below is further demonstrated by its holding that an intermediary bank could be found liable for damages to Sabena, the intended beneficiary of the funds transfer. This outcome runs patently against the Legislature's intent with respect to Article 4A of the U.C.C., under which no intermediary bank owes an obligation to a beneficiary.

As discussed above, an intermediary bank has limited exposure during the course of a funds transfer. It is only in privity with the bank that sends it the payment order (in the case at hand, with Sudan Airways' bank, the National Bank of Abu Dhabi) and, if it executes that payment order, with the beneficiary's bank. Section 4A-402(4) of the U.C.C. expressly provides that the intermediary bank must provide a refund for any funds debited from the account of the bank that sends it a payment order that it fails to execute (this is known as the "money-back guarantee"; *see* N.Y. U.C.C. § 4A-402 (McKinney 2013), Official Comment No. 2, at p. 299). This is the extent of the intermediary bank's liability for a non-executed payment order—it has no liability or duty to the beneficiary or even to the beneficiary's bank, to which the intermediary bank has no obligation unless it accepts a payment order (*see* N.Y. U.C.C. § 4A-402(2)).

An intermediary bank "does not ... have any duty to accept a payment order or, before acceptance, to take any action, or refrain from taking action, with

respect to the order." N.Y. U.C.C. § 4A-212. It "is not the agent of the sender or beneficiary of the payment order it accepts, or of any other party to the funds transfer." *Id.* And it is firmly established that neither the originator nor the beneficiary holds title to funds in the possession of an intermediary bank. *Jaldhi*, 585 F.3d at 71; *Asia Pulp & Paper*, 609 F.3d at 121; *Scanscot Shipping*, 617 F.3d at 681-682; *Allied Maritime*, 620 F.3d at 75.

These principles continue to apply when a funds transfer is blocked midstream by federal regulations. In two recent cases, the Second Circuit held that, "*[i]n the context of a blocked transaction,* ... the only entity with a property interest in the stopped EFT is the entity [*i.e.*, the originator's bank or another intermediary bank] that passed the EFT on to the bank where it presently rests." *Calderon-Cardona*, 2014 WL 5368880, at *6 (emphasis added); *Hausler*, 2014 WL 5420141, at *3. This conclusion is inevitable in light of the mechanics of funds transfers (*see supra* Background, Part A) and the rules that govern transfers. Indeed, "[b]ecause EFTs function as a chained series of debits and credits between the originator, the originator's bank, any intermediary banks, the beneficiary's bank, and the beneficiary, '*the only party with a claim against an intermediary bank is the sender to that bank, which is typically the originator's bank.*'" *Calderon-Cardona*, 2014 WL 5368880, at *6, quoting *Asia Pulp & Paper*, 609 F.3d at 119-120 (emphasis added). Likewise, in *Estate of Heiser* v. *Islamic*

*Republic of Iran*, 885 F.Supp.2d 429, 448 (D.D.C. 2012), *aff'd*, 735 F.3d at 941, the court explained that "OFAC blocking ... does not vest title in the beneficiary or the beneficiary's bank." In affirming that ruling, the D.C. Court of Appeals stated that, "claims on an interrupted funds transfer ultimately belong to the originator [if subrogated to the rights of its bank[9]], not the beneficiary or its bank." *Heiser*, 735 F.3d at 941. *See also U.S.* v. *BCCI Holdings (Luxembourg), S.A.*, 977 F.Supp. 12, 18 (D.D.C. 1997), *aff'd*, 159 F.3d 637 (D.C. Cir. 1998) ("When a funds transfer is not completed, the intermediary bank receiving payment is obligated to refund payment to the sender. ... [A]n intermediary bank has no legal obligation to the beneficiary.")

In other words, the mere fact that a funds transfer is blocked does not change the fundamental nature of the funds transfer or the rules that apply to it. Absent specific provisions in the blocking regulations that purport to allocate property interests to the funds differently than what is provided in the U.C.C. (and there are no such overriding provisions), the U.C.C. applies and its basic rules control. There is simply nothing in state or federal law on which to base liability of an intermediary bank to an intended beneficiary for a non-completed transfer, and the courts have no authority to override the U.C.C. with their own rule, much

[9] N.Y. U.C.C. § 4A-402(5) provides that an originator can be subrogated to the rights of its bank to receive a refund under the money-back guarantee in certain circumstances where the intermediary bank is unable to immediately provide a refund.

less one fundamentally at odds with provisions that protect intermediary banks from liability.

From a policy perspective, there are good reasons to limit the exposure of intermediary banks during the course of *all* funds transfers, including those that are stopped midstream. In *Grain Traders*, 160 F.3d at 102, the court explained why an intermediary bank's only liability should be to refund to its immediate sender the amount of an unexecuted payment order:

> One of Article 4–A's primary goals is to promote certainty and finality so that "the various parties to funds transfers [will] be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfer services appropriately." N.Y.U.C.C. Art. 4–A–102, cmt. To allow a party to, in effect, skip over the bank with which it dealt directly, and go to the next bank in the chain would result in *uncertainty as to rights and liabilities, would create a risk of multiple or inconsistent liabilities, and would require intermediary banks to investigate the financial circumstances and various legal relations of the other parties to the transfer.* These are matters as to which an intermediary bank ordinarily should not have to be concerned and, if it were otherwise, *would impede the use of rapid electronic funds transfers in commerce by causing delays and driving up costs.*
>
> (Emphasis added)

Thus, intermediary banks are essentially facilitators. An intermediary bank's function is mechanical: to execute a payment order, failing which it must return any payment it received with respect to the payment order to its sender (in this case the originator's bank). They do not investigate the payment orders that they receive and do not have advance warning that blocking regulations will apply

to an order. A judge-made rule that imposes on intermediary banks the ultimate responsibility for the non-completion of a funds transfer is inconsistent with this limited role. A failure to overturn the ruling below would expose intermediary banks to a dual-liability: to the beneficiary under New York state case law, and to the originator's bank under the express provisions of the statute.

## II. *NORILSK NICKEL* AND ITS PROGENY DO NOT APPLY HERE.

The Court should decline to follow the case law upon which the court below based its ruling. None of those decisions even mentioned § 4A-211(4) or the cancellation of stale payment orders required by the U.C.C. But to the extent that those cases are taken to stand implicitly for the proposition that § 4A-211(4) does not apply to transfers that have been blocked by regulation, they were wrongly decided. This Court has expressly overruled its own precedents when it realized, upon further deliberation, that it clearly misinterpreted or overlooked a statutory provision or a binding precedent. *See, e.g.*, *George Campbell Painting*, 92 A.D.3d at 105-106, 937 N.Y.S.2d at 164-166; *Fletcher* v. *Dakota, Inc.*, 99 A.D.3d 43, 50, 948 N.Y.S.2d 263, 264-265 (N.Y. App. Div. 2012). The Clearing House urges it to do so again here, if necessary.

### A. There Is No Binding Precedent For Holding an Intermediary Bank Liable To a Beneficiary.

The court below expressly identified three cases to support its conclusion that an intermediary bank could be found liable to Sabena for the incomplete transfer: *Norilsk Nickel*; *European American Bank*; and *Goodearth Maritime*. These cases lend no support to the court's conclusion. Indeed, none of those cases actually finds an intermediary bank liable to an intended beneficiary, and none of them squarely addresses § 4A-211(4) or the issue of whether a payment order is cancelled by operation of the U.C.C.

Properly understood, *Norilsk Nickel*—the cornerstone of the cases relied upon by the court below—stands merely for the proposition that the creditors of an originator could not attach funds in the hands of an intermediary bank. Following the unblocking of a funds transfer at an intermediary bank, that bank interpleaded the amount of the funds transfer, which was claimed by creditors of the originator and by the intended beneficiary. The issue in dispute was whether the regulations pursuant to which the funds transfer was blocked prevented title in the funds from passing from the originator (Genex), thus making the funds property that could be attached by the originator's creditors. The court found that the U.C.C.—not the regulations—applied to determine whether Genex had title to the funds at the time of the attempted attachment, and that title had passed from

Genex to the intermediary bank when the originator's bank executed the payment order that it had received from Genex. 14 A.D.3d at 146-148, 789 N.Y.S.2d at 99-102. The court therefore determined that the creditors' attachment was wrongful and that the creditors owed damages to the beneficiary for a wrongful attachment.

The problem with the *Norilsk Nickel* decision is that, in addition to that conclusion, the court cursorily determined, without reference to any actual provision of the U.C.C., that the U.C.C. required that the funds be paid to the intended beneficiary after the block was lifted:

> It is clear that, under the UCC, title to the funds in question passed from Genex to Midland Bank [the intermediary bank] in 1993, but federal law operated to prevent the movement of the funds from 1993 until 2003. When the hostilities in Yugoslavia ended, and the federal government had no further reason to block Genex's use of the funds, federal law unblocked the funds. *The UCC then required that the funds be transferred to the rightful owner, Norilsk* [the intended beneficiary].

(14 A.D.3d at 147, 789 N.Y.S.2d at 100-101; emphasis added)

Given that the funds had been interpleaded and the court had determined that the creditors' attachment was wrongful and damages were owed to the beneficiary, the issue of returning payment to the originator's bank was not the court's focus. The court never dealt with the U.C.C.'s provision (§ 4A-211(4)) that a delay in execution of five or more business days cancels an unaccepted payment order. The intermediary bank was discharged by the interpleader, and the court was presented with a dispute only between parties who had no claim against an

intermediary bank. *See Asia Pulp & Paper Company, Ltd.*, 609 F.3d at 121 ("[A]n originator and intended beneficiary have no legal claim or contractual rights against an intermediary bank in the event that a funds transfer is not completed.") The key ruling was that the creditors' attempted attachment was invalid, *not* that payment orders survive beyond their usual five-day lifespan when a funds transfer is blocked by federal regulations. This said, the court was manifestly in error when it stated that "[t]he UCC required" the funds to be paid to the beneficiary. It did not cite any relevant statutory provision, including § 4A-211(4), which cancels a non-executed payment order. Nor did it weigh the legal and systemic consequences of holding intermediary banks liable to an intended beneficiary. In light of the lack of analysis given to the issue, it is unlikely that the court intentionally set out to create a binding precedent that could justify holding intermediary banks liable to an intended beneficiary and, in so doing, depart completely from the express provisions of the U.C.C.

*European American Bank* also did not determine the effects of a block on a payment order. In that case, the court merely found that a levy by a beneficiary's judgment creditor could not be enforced against the funds held by an intermediary bank. The court cited § 4A-502(4) of the U.C.C., which exempts intermediary banks from, among other things, a levy by a beneficiary's creditors,

but did not mention § 4A-211 or the money-back guarantee provision, § 4A-402. *European American Bank*, 12 A.D. 3d at 190; 784 N.Y.S.2d at 100-101.

In fact, it was the Second Circuit in its unreported opinion in *Goodearth*, 387 Fed.Appx. at 21, rather than this Court, that formulated the proposition that an interference with a funds transfer may "interrupt", rather than cancel, a transfer. However, the Second Circuit qualified this proposition significantly.

In *Goodearth*, an originator sought to recover the amount of a funds transfer after it was improperly attached while in the hands of an intermediary bank. The intended beneficiary objected, contending that it should receive the funds after the attachment was released. The originator argued that the payment order was cancelled and that it was entitled to reimbursement of its funds under the money-back guarantee. The court rejected this argument, for two reasons: (i) the record showed that most of the funds had already been transferred to the beneficiary's bank, which suggested that the payment order had in fact been executed, and (ii) the originator itself did not have standing to rely on the money-back guarantee, because the money-back guarantee would benefit only the originator's bank. *Id.*

The court's ruling was highly specific to the unique facts before it and was based, in large part, on the perceived equities of the case. Importantly, the

court underscored that there was not an originator's bank making a claim to the funds at issue and left open the issue of how it would decide the case if there had been a different set of competing claims. *Id.* at 22 ("[T]he equities in this case … where the record contains no evidence of a legitimate competing claim for the funds from another party … favor releasing the funds to the beneficiary.") Faced with different factual circumstances, the Second Circuit has in fact come to a different conclusion. As discussed, two more recent decisions from the same court now have specifically found, in the context of a blocked transaction, that the only party with a claim against an intermediary bank is the entity that sent a payment order to the intermediary bank. *Calderon-Cardona*, 2014 WL 5368880, at *6; *Hausler*, 2014 WL 5420141, at *3.

Consequently, the three cases relied upon by the court below are not authority for the proposition that an intermediary bank can be found liable to a beneficiary for honoring the U.C.C.'s money-back guarantee and reimbursing an originator's bank. The court below went well beyond what the courts in these cases contemplated, and did so without meaningfully analyzing the applicable source of law, *i.e.*, the U.C.C. The Clearing House submits that the court below was in error when it held that an intermediary bank could be directly liable to an intended beneficiary for an unaccepted payment order. To the extent that *Norilsk Nickel* and its progeny were understood to compel that result, they are simply

wrong on the law and should be overruled. The ruling by the court below plainly contradicts the provisions of the U.C.C., which protect intermediary banks from liability to the beneficiary, and is not supported by these earlier decisions.

### B. The Equities of this Case do Not Favor Holding Deutsche Bank Trust Company Americas Liable to Sabena.

The driving force behind the ruling on appeal appears to be a concern that it would be unfair to stop a funds transfer from being completed on the basis of a transfer interference over which the beneficiary had no control. This is an unfounded concern.

Even when a payment order is cancelled as a matter of law and the funds transfer consequently fails to be completed, the underlying obligation remains and the intended beneficiary is at liberty to enforce its rights against the originator by any means available. In other words, when the U.C.C. cancelled the originator's bank's payment order, that cancellation did not deny Sabena any of its legal rights to obtain payment from the originator, Sudan Airways. The cancellation of a payment order does not extinguish the underlying obligation between the originator and the beneficiary. The underlying obligation is only discharged *if and when* the beneficiary's bank accepts the payment order. *See* N.Y. U.C.C. § 4A-406. Thus, "if an EFT is not completed … the originator … continues to have an underlying obligation to pay the beneficiary." *Estate of Heiser*, 885 F.Supp.2d at 448. This is one reason why the money-back guarantee

is so important: the originator may immediately seek to discharge its obligation by other means when a payment order fails to be executed, safe in the knowledge that it will recover funds from the failed transfer.

Fundamentally, a funds transfer is only a payment mechanism and intermediary banks are, as their name suggests, mere intermediaries. If the payment mechanism fails pursuant to the rules of the U.C.C., then the intended beneficiary must seek payment from the originator by other means. The ruling on appeal fails to recognize this and effectively creates an obligation by intermediary banks to beneficiaries; the banks become the guarantors of originators. The U.C.C. clearly intended no such result.

There is no unfairness in refusing to distort the provisions of the U.C.C. for the benefit of Sabena. By contrast, significant unfairness has been visited on the Appellants by the ruling now on appeal. DBTCA complied with an express provision of the U.C.C. by returning funds to the originator's bank. Nevertheless, it was found liable to Sabena under a judge-made rule for which there is no legal basis. Although the ruling below concludes that an intermediary bank has an obligation to pay over the amount of an "interrupted" funds transfer to the intended beneficiary, the U.C.C. requires that same payment to be made to the bank that sent the payment order to the intermediary bank.

Additionally, this unfairness against DBTCA is compounded by the fact that a different result would be reached in New York federal court. As discussed, the Second Circuit has now unambiguously recognized that, when funds are blocked by regulations administered by OFAC, the only party that an intermediary bank can be liable to is the entity that sent it a payment order. *See Calderon-Cardona*, 2014 WL 5368880, at *6; *Hausler*, 2014 WL 5420141, at *3. If this Court upholds the ruling below, then in this State the application of the U.C.C. to disputes between intended beneficiaries and intermediary banks will depend on the forum in which the action is brought, *i.e.*, state or federal court. Such a situation will induce forum shopping and create significant uncertainty for intermediary banks. These banks will be in a precarious position, where federal courts in New York apply the U.C.C. as intended by the Legislature, while state courts depart from the statute on the basis of erroneous case law.

In sum, the ruling below violates a clear statutory provision and creates confusion as to how New York law will be interpreted by its courts. It has serious potential systemic repercussions. Intermediary banks in New York will be forced to seriously reconsider their role and assess the risks to which they are exposed when undertaking what were—until now—routine transactions.

## CONCLUSION

For the reasons stated, The Clearing House respectfully urges the Court to grant the Appellants' appeal, overturn the ruling below, and enforce the applicable provisions of the governing statute, the U.C.C.

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Respectfully submitted,

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