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STATE OF NORTH DAKOTA

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

Baker Boyer National Bank,

Plaintiffs and Appellees,

vs.

JPF Enterprises, LLC,

Defendants and Appellants.

SUPREME COURT NO. 20180222
McKenzie County No. 27-2016-CV-00392

APPEAL FROM THE JUDGMENT ENTERED MARCH 21, 2018
PURSUANT TO THE LETTER OPINION DATED JANUARY 25, 2018

McKENZIE COUNTY DISTRICT COURT, NORTHWEST JUDICIAL DISTRICT
THE HONORABLE DANIEL S. EL-DWEEK

APPELLANT'S BRIEF

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[1] **I. TABLE OF AUTHORITIES**

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1. *Grinnell Mutual Insurance Company V Norman C. Thompson et al*, 2010 ND 22, 778 N.W. 2d 526 ..... ¶12

2. *American Bank Center v. Wiest* , 2010 ND 251, ¶ 31, 793 N.W.2d 172, 105 S. Ct. 1504 (1985) ¶17, ¶22, ¶23, ¶28, ¶30, ¶38

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NORTH DAKOTA STATUTES

1. N. D. R. Civ. P. Rule 56 ..... ¶12

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3, N.D.C.C.§ 9-03-01 ..... ¶29

FEDERAL STATUTES

1. 15 USC 1691(d)(2) ..... ¶14, ¶18, ¶30

2. 12 CFR 1002.9(a)(2) ..... ¶14, ¶17, ¶18, ¶32

Statement of the Issue

[¶2] The sole issue on appeal is whether the district court erred in its finding that there existed no genuine issue of material fact when the court granted Plaintiff's Motion for Summary Judgment and dismissed Defendant's Counterclaim.

Statement of the Case

[¶3] This is an appeal from summary judgment entered in an action which involved Baker Boyer National Bank (hereinafter referred to as "Bank") as lender and JPF Enterprises, LLC (hereinafter "JPFE") as borrower. Bank originally had a loan with third parties which had as its security mobile housing units for a mancamp. The loan was underperforming, and ultimately Bank induced JPFE to purchase the units and finance the sale through Bank. Bank initiated this action by the filing of a Summons and Complaint which alleged, among other things, that JPFE had defaulted upon the payment of the loan, and demanded possession of the collateral, the sale of collateral, and a deficiency judgment for the balance between what was recovered and the amount owed.

[¶4] JPFE Answered and Counterclaimed, admitting that the payments had not been made as agreed and alleging fraud by Bank in failing to disclose information to JPFE about the profitability of the mobile housing units and existing contracts which virtually made profitability of this venture an impossibility.

[¶5] Bank asserted that it had no duty to disclose to JPFE that Bank knew the projected cash flows of the venture were vastly overstated; that the company that it mandated JPFE contract with to manage the mobile housing units was insolvent; that the venture would never cash flow, let alone turn a profit, and moved to dismiss Defendant's Counterclaim and simultaneously moved for Summary Judgment.

[¶6] JPFE opposed the Motion to Dismiss and the Motion for Summary Judgment, arguing that there existed several genuine issues of material fact which necessitated a trial. As evidence of the knowledge by the Bank of the inevitability of failure of this venture, there exist several emails. The testimony of the sole owner of JPFE, James Foust, would also corroborate the emails and the knowledge by the Bank that the investment was doomed to fail, and only the strength of Foust's balance sheet could make a terrible loan into a good loan.

[¶7] The district court agreed with Bank that there existed no genuine issues of material fact, and Judgment was ultimately issued granting Bank's Motion for Summary Judgment and Dismissing Defendant's Counterclaim.

Statement of the Facts

[¶8] In April of 2013 Defendant JPFE was introduced to Chris Sentz of Baker Boyer Bank. Mr. Sentz outlined a business opportunity to purchase 30 mobile housing units currently owned by a Bank customer "Vindan". He also introduced me to another bank customer GreenFlex that was the manufacturer of the mobile housing units owned by Vindan. Mr. Sentz outlined a deal whereby I would buy the homes owned by Vindan, execute an agreement with GreenFlex that would provide a 7 year contractual guarantee to manage the units that would return $1500 per month for each of the 30 units for a period of 7 years. Bank would then roll over the existing $1,000,000 bad loan from Vindan to JPFE, thus financing the 60% of the purchase of the Vindan interest. JPFE would complete this transaction by injecting about $700,000 cash into the project.

[¶9] The Vindan loan with Bank was at that time near foreclosure. Discussion with GreenFlex was very enticing. The contract with Greenflex that would return $1500 per month for each of the 30 units for a period of 7 years would provide an income stream that would allow JPFE an exit strategy in selling the mobile housing units and provide cash flow to new investor.

[¶10] Bank knew that the $1500 per unit contract would never be paid because they knew, as evidenced by emails, that the

units were generating only $320 per unit, ($9600 monthly) yet Bank proceeded with the loan with JPFE which required a monthly payment of $14,928 per month.

[¶11] The Bank originally rejected the loan for reasons not divulged to JPFE but later learned by emails because the venture did not cash flow, then changed course to accept the loan for reasons not stated but later learned to based upon the balance sheet of James Foust, the guarantor of the loan.

Law and Argument

[¶12] This Court's standard of review on summary Judgment is well established:

> Under N.D.R.Civ.P. 56, summary judgment is a procedural device for promptly resolving a controversy on the merits without a trial if there are no genuine issues of material fact or inferences that can be easily drawn from undisputed facts, or if the only issues to be resolved are questions of law. The party moving for summary judgment must show there are no issues of material fact and that the case is appropriate for judgment as a matter of law. A district court's decision on a motion for summary judgment is a question of law that we review de novo on the record. In determining whether summary judgment was appropriately granted, we view the evidence in the light most favorable to the party opposing the motion, giving that party the benefit of all favorable inferences which can be reasonably be drawn from the record.

Grinnell Mutual Insurance Company v. Norman C. Thompson, et al, 2010 ND 22, 778 N.W.2d 526.

[¶13] Whether there exist genuine issues of material fact is the sole issue of this appeal.

[¶14] On September 24, 2013, JPFE, as buyer, entered into an asset purchase agreement (the "Purchase Agreement") with sellors Vindans, LLC ("Vindans") and Jason Sundseth

("Sundseth"), the managing member of Vindans. JPFE applied for financing from ("Bank") and was denied on or about August 20, 2013; this was relayed to JPFE by email from the Bank. See Defendant Exhibit 39. The denial email did not state a reason why JPF's loan application was being denied. Bank did not send a letter detailing why the loan was denied despite federal code and the federal regulations requiring Bank to do so. 15 USC 1691(d)(2); 12 CFR 1002.9(a)(2).

[¶15] The following references to Appellant's Appendix shows the chronological order of emails pertaining to this matter and providing the Court a more clear factual background. (Sentz is the Bank Officer, JPF is Foust, sole owner of JPFE, Cassidy and Eakin are Greenflex Housing (GFH):

App #	Date Time	From / To	Comments
App 39	5/22/2013 12:45	Eakin to Sentz	References high vacancy factor;
App 40	7/02/2013 3:43 p.m.	Sentz to Cassidy Eakin	Requests updated rent rolls. Bank notes that not all units are rented and is working on a new buyer. The bank is fully informed about underperforming rentals.
App 38	8/20/2013 11:11 a.m.	Sentz to JPF	Notice to Foust that loan is declined; states that bank will send declination letter.

App #	Date Time	From / To	Comments
App 41	8/20/2013 5:04 p.m	Sentz to Cassidy and Eakin	I don't know where things stand with Jim Foust as of today, but if that deal is to progress we will need to show the financial viability of the company [Greenflex Housing] providing the contract of guaranteed monthly payments.
App 43	8/20/2013 5:30 p.m.	Cassidy to Sentz, Eakin	GFH leased 66 units from 11 people and is currently in arrears in making payments. In fact, GFH was always in arrears, before and after JPFE's loan.
App 45	8/23/2013 3:04 p.m.	Cassidy to Sentz	Bank is informed that GFH is paying only $320 per unit
App 45	8/23/2013 4:31 p.m.	Cassidy to Sentz	Bank is again told that Vindan's 30 units (which Foust bought) was generating only $320/month x 30 = $9,600. Bank is also told GFH is accruing the liability of the lease rate minus $320 for everyone on a lease. So it appears GFH may be insolvent.

App #	Date Time	From / To	Comments
App 47	8/23/2013 6:08 p.m.	Cassidy to Sentz	States GFH does not know how to account for money Badlands has embezzled.
App 48	8/26/2013 1:30 p.m.	Sentz to JPF	"Some things have occurred which once again allow me to consider financing you ..." It also states an approximate monthly loan payment of $14,928 which is far above the $9,600 per month income generated by the units.
App 50	8/26/2013 6:07 p.m.	Sentz to Cassidy and Eakin	Mentions "your GF contracts" and states that "the contract is a key component of our financing..." He knew GFH was NOT paying the contract rate. It was a sham. Bank also asks for GFH's "Master Lease with RV Park"
App 51	9/04/2013	Sentz to JPF	Bank is showing Foust the extent of its investigation, leading Foust to believe it is covering the bases for him.

App #	Date Time	From / To	Comments
App 52	10/03/2013 3:33 pm.	Sentz to JPF	Mentions pending items and notes "this unique underwriting process." NOT the unique facts, the unique process. This was NOT an ordinary arms-length loan. Also, approximate loan payment is now up to $16,000.
App 53	11/15/2013 3:09 p.m.	Sentz to JPF	States that John Blackmon was the advocate for the loans, he is no longer with the bank, and the North Dakota loans were "way outside the box for our conservative little Bank." This was NOT an ordinary arms-length loan. This was a special, unique process to eliminate a known bad loan from their balance sheet.

[¶16] As seen above in Appellant's Appendix at 39 and 40, in May and July 2013 the bank was aware of underperformance by the North Dakota rentals. At least by July the bank knew that Mr. Sundseth (Vindans LLC) wanted out of the business. The bank was working on a loan for JPFE to buy out Vindans.

[¶17] On August 20 Mr. Sentz tells Foust at 11:11 a.m. his "requested financing for units in North Dakota is no longer a viable possibility" and that the bank will send a declination letter. App at 38. That letter is required to contain the reasons why the loan is declined. 12 CFR 1002.9(a)(2). That letter was never sent. On the same day at 5:04 p.m. Mr. Sentz emails to GFH about proving the financial viability of GFH in order to keep the Foust deal alive. App at 41. Three days later Sentz learned that the 30 units generated only $9,600 monthly income (30 x $320), then three days after that he offers a purchase money loan to Foust with a $14,928 monthly payment. Because the Bank not only knew it was a losing deal but the bank required a contract with this particular company (GFH), this was not an ordinary lender/borrower relationship. This was not an ordinary arms-length transaction. The bank had a duty to tell Foust what it knew about GFH, Badlands and the financial viability of the investment. *See*, American Bank Center v. Wiest , 2010 ND 251, ¶ 31, 793 N.W.2d 172. ("The relationship between a bank and its customers is viewed as a debtor-creditor relationship which does not ordinarily impose a fiduciary duty upon a bank.") (quoting First Nat'l Bank & Trust Co. v. Brakken , 468 N.W.2d 633, 637 (N.D. 1991)).

[¶18] Initially, the bank's actions in this matter were contrary to federal law. On August 20, 2013, Mr. Sentz of Baker Boyer Bank sent an email to Foust to inform him that the bank was declining his loan application and said an official declination letter

would follow by mail. App at 38. Federal law requires the bank to give the reason(s) for denying the loan. 15 USC 1691(d)(2); 12 CFR 1002.9(a)(2). The bank did not send the letter. The email is notice to the customer that the loan was declined. The bank was required by the federal code and the federal regulation to give the reasons. It failed to comply with those directives. Now Bank claims that it can do so with impunity. "A statement of reasons meets the requirements of this section only if it contains the specific reasons for the adverse action taken." 15 USC 1691(d)(3).

[¶19] Given what the bank knew about GFH and Badlands, LLC (Badlands), the underlying RV park leaseholder, declining the loan would be consistent with sound lending practices and existing bank policy. Had these known reasons for initially declining the loan been given to Foust, Foust would not have signed the loan on behalf of JPF Enterprises, LLC (JPF) nor on the personal guarantee.

[¶20] The Bank has argued that "[a] contract must be interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting so far as the same is ascertainable and lawful." *See*, Tallackson Potato Co., Inc. V. MTK Potato Co., 278 N.W. 2d 417, 421(ND 1979), which also states that no extrinsic evidence is permissible to ascertain the parties' intentions in a written contract if such intentions can be determined from the writing alone.

[¶21] JPFE has no quarrel with the terms of the contact, and agrees that the terms of the conract are what were agreed to. HOWEVER, it is abundantly clear from the emails between bank personnel that JPFE was not privy to (and that JPFE only became aware of as a result of this lawsuit) that the Bank led JPFE to believe that the return on investment would be roughly 5 times what the Bank expected the return to be. The Bank had a duty not to overtly mislead JPFE to undertake a loan that could not be serviced.

[¶22] If there were special circumstances as envisioned by North Dakota case law, then a duty to disclose is created. Am. Bank Ctr. at ¶ 32. The determination of whether "special circumstances" beyond normal banking existed between these parties is a question of fact. Id. citing Brakken, 468N.W.2d at 637. However, there must be some factual analysis to determine what relationship exists. Relevant law is stated by the Am. Bank Ctr. v. Wiest court. That case states in relevant part:

> The relationship between a bank and its customers is viewed as a debtor-creditor relationship which does not ordinarily impose a fiduciary duty upon a bank. Some courts have recognized that a fiduciary relationship may arise under circumstances which reflect a borrower's reposing of faith, confidence and trust in a bank with a resulting domination, control or influence exercised by the bank over the borrower's affairs. Furthermore, the borrower or party reposing the confidence must be in a position of inequality, dependence, weakness, or lack of knowledge.

Am. Bank Ctr. v. Wiest at ¶31 (quoting First Nat'l Bank & Trust Co. v. Brakken, 468 N.W.2d 633, 637 (N.D. 1991).

[¶23] Whether the Bank was in a fiduciary relationship with Foust must be determined at trial. By relying on the contract between Foust and GFH, which called for $1,500 per month per unit to be paid to JPFE, the Bank knowingly misled JPFE by overstating the projected income stream. The Bank required Foust to contract with GFH. Therefore, the Bank was in the role of an adviser, directing that JPFE continue to use GFH as his property manager, knowing that property manager was not able to collect $1,500 per unit per month.

The Am. Bank Ctr. v. Wiest court stated:

> In securing the $200,000 loan, Palmer continued to represent that it was necessary to keep the obligations of Glass Blast current to obtain an SBA loan. The district court found these payments only benefitted the Bank and were "of no benefit to Wiest." The court concluded that by failing to disclose theses circumstances to Wiest, Palmer had breached a fiduciary duty.
> Id. at ¶35

[¶24] The duty to disclose in a business transaction arises if imposed by a fiduciary relationship or other similar relationship of trust or confidence or if necessary to prevent a partial or ambiguous statement of facts from being misleading.

[¶25] JPFE argues that the duty to disclose here is necessary to prevent a partial or ambiguous statement of facts from being misleading. The Bank argues that JPFE did not provide "specific facts" because his declaration stated that the bank

"facilitated" the sale of Mr. Sundseth's housing units to JPFE. That is not all that JPFE presented. Numerous facts show that the bank misled JPFE regarding the feasibility of the investment.

[¶26] JPFE was not only told that it could expect $1,500 per unit net income, he had a contract to receive such. His contract with Greenflex Housing stated $1,500 rent per unit per month for 30 units. That would be $45,000 per month in gross rent. This is the contract that the bank required Foust to sign before they would make the loan to his company to purchase the units. It looks good on the surface.

[¶27] As seen in App at 39 and 40, in May and July 2013 the Bank was aware of under-performance by the North Dakota rentals. At least by July the bank knew that Mr. Sundseth (Vindans LLC) wanted out of the business. The bank was working on a loan to Foust to buyout Vindans.

[¶28] In this case the bank provided its customer JPFE with the "extra service" of picking for him his property manager and determining the financial viability of a company that the Bank required Foust to use (GFH). App at 41. Requiring that Foust use this particular company puts this case in a different realm than cases standard debtor-creditor relationships. For comparison, The Am. Bank Ctr. v. Wiest court found that the debtor placed his trust and confidence in the bank's vice president giving rise to a fiduciary duty and a duty of disclosure. *See,* Am. Bank Ctr. v. Wiest at ¶28.

[¶29] The relationship between JPFE and Bank are remarkably similar to that of Am. Bank Ctr and Wiest. Am. Bank Ctr. failed to inform Weist, the debtor, that the security in that case was never properly secured nor did Am. Bank inform Weist of Glass Blast's loans. See Am. Bank Ctr. v. Weist at ¶6. Here, the bank and its customer were involved in extended discussion and information sharing as evidenced by multiple email messages in the court record. It was the Bank that withheld critical information. Information that, if provided, would easily show that the project as structured was not viable. Information that would have caused Foust to terminate his involvement, not invest hundreds of thousands of dollars, in a venture that Bank knew to be destined to fail.

[¶30] The above referenced emails from Chris Cassidy of Greenflex Housing to Chris Sentz of Baker Boyer Bank informed the Bank that GFH is paying only $320 per unit to the owners. $9,600 per month is $35,400 less per month than JPFE's contract. The Bank knew of the substantial underperformance by GFH due to the Badlands problem. By requiring Foust to contract with GFH, thereby creating an obligatory relationship, the bank overstated the expected income from the units knowing it was a false number, and misled Foust into guaranteeing the loan. The Bank knew this before making the loan. The Bank knew the loan was not going to be paid without enormous cash contributions

from Foust. The bank did not tell JPFE, and that was a lie by ommission. That was fraudulent concealment. At that point the bank owed a duty to Foust. See, Am. Bank Ctr. v. Weist at ¶11. Here, as in the Am. Bank Ctr. v. Wiest, the bank overstated JPFE's GFH income, knew it was false, and thereby JPFE was induced into a loan that could not be paid, then ultimately commenced collection proceedings against JPFE. The Bank exceeded the conventional role as a lender, JPFE's harm was readily foreseeable by the Bank and its financial injury certain.

[¶31] Under North Dakota law, a valid contract requires parties capable of contracting, consent, a lawful object, and sufficient consideration. N.D.C.C. § 9-01-02; see Erickson v. Erickson, 2010 ND 86, ¶ 7, 782 N.W.2d 346. Section 9-03-01, N.D.C.C., requires the parties' consent to be free, mutual, and communicated by each to the other. Erickson, at ¶ 7. "A party's apparent consent is not free when it is obtained through fraud, and fraud can be either actual or constructive." Id. In Erickson, the North Dakota Supreme Court explained the application of actual or constructive fraud necessary to invalidate a contract:

> "Persons alleging actual or constructive fraud seek to invalidate contracts by arguing consent was not freely obtained. See N.D.C.C. § 9-03-01(1) (parties' consent to a contract must be free); § 9-03-03(3) (consent is not free when obtained through fraud); § 9-03-07 ('Fraud is either actual or constructive.'). The most significant difference between the two claims is that actual fraud requires proof of an intent to deceive, while constructive fraud requires no proof of such intent. N.D.C.C. §§ 9-03-08 and 9-03-09(1). Although

> actual and constructive fraud both invalidate a party's apparently free consent to a contract, the two types of fraud differ in the source of injury they address. Actual fraud confronts situations where one party intentionally misrepresents or conceals facts from another contracting party. N.D.C.C. § 9-03-08. Constructive fraud confronts situations where the source of the claimant's injury is the breach of an existing duty between the contracting parties. N.D.C.C. § 9-03-09(1)."

Erickson, id 2010 ND 86, ¶ 8, 782 N.W.2d 346.

[¶32] Here, there was a statutory duty on the bank to disclose the reasons for denying the loan to Foust. See 12 CFR 1002.9(a)(2)(i). The federal statute imposes a duty to disclose the specific reasons for loan denial. 15 USC 1691(d)(2) (Each applicant against whom adverse action is taken shall be entitled to a statement of reasons for such action from the creditor.) The bank did not comply with federal law. The reason(s) for the denial were not given to JPFE. The email from the bank stated that the loan was "no longer a viable possibility." *See*, App at 38. It also stated that an official declination letter would be sent by mail. The letter was required by federal law. It would have given JPFE the reasons for loan denial, such as the impossibility of the company paying rent to perform its contract. That would have been a good banking decision. Instead, the bank started looking for a way to show the financial viability of GFH. *See*, App at 41.

[¶33] Furthermore, JPFE was justifiably relying on the Bank's specialized knowledge of this particular property manager. The Bank was in regular contact with John Eakin and Chris

Cassidy of GFH. The Bank had made several similar loans.

[¶34] The Bank knew that Badlands had embezzled money from GFH. *See*, App at 47, knew that GFH had a lower than expected census on its rental occupancy, and knew that the contract between JPFE and GFH could not be performed as written. The Bank sent an email notice that a loan denial letter would be sent by regular mail and had a statutory duty to disclose reasons for loan denial. The Bank's manipulation of the underwriting process, described by the Bank as a "unique underwriting process," that required JPFE to contract with an entity (GFH) known to the bank to be insolvent and an "empty shell" creates the kind of special relationship that requires full disclosure under North Dakota case law. Foust has been injured and deserves a trial.

[¶35] It appears that even the bank officer Mr. Blackmon agrees that information was critical. Mr. Blackman says "As I remember this loan, without the personal guarantee the Banks only source of collection would have been the trailers and an otherwise empty LLC." *See*, Affidavit of John Blackmon, filed earlier in this case as Doc ID#59. He knew that there was nothing of substance going into this deal for Foust. The Bank would receive hundreds of thousands of dollars paid by Foust toward the purchase, eliminate a bad loan from their books, and set the groundword to harvest the equity from Foust's balance sheet when, not if, the loan could not be serviced by the rental income. The declaration of Chris Sentz is similar, stating that he thought it was

a good loan because of the strength of James Foust's personal financial statements. *See*, Affidavit of Chris Sentz, filed in this case as Doc ID#60.

Conclusion

[¶36] The bank has no right to engage in fraud, constructive fraud, fraudulent concealment, fraudulent inducement or bad faith. Viewing the record most favorably to JPFE, there exist material issues of fact. Therefore, the law requires that JPFE be granted a trial on both the Plaintiff's claim and Defendant's Counterclaim. Under the circumstances of this case, as it was in Am. Bank Ctr. v. Wiest, supra, it is a question of fact whether the bank had a duty to Foust.

[¶37] Most of these documents came from the Bank. They clearly show, together with other documents in the record, material issues of fact in this case.

[¶38] "A finding of fraud is a question of fact . . ." Am. Bank Ctr. v. Wiest at ¶13.

[¶39] Dated this 13th day of July, 2018.

Respectfully submitted,

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