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BANKING ALERT

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Federal Court Dismisses Breach of Contract Claim Against Credit Union

In *Folger v. Navy Federal Credit Union,* 22-cv-198 (D.N.J. Nov. 4, 2022), the district court dismissed a complaint filed by a customer of a credit union claiming that the credit union had improperly frozen his account and declined two deposit transactions.

In the complaint, the plaintiff Amy Folger ("Plaintiff") attempted to deposit four checks totaling approximately $71,000 into an account he maintained at defendant Navy Federal Credit Union ("NFCU") in October 2021. Plaintiff claimed that he received notification from NFCU that the checks had been deposited and were under review. Soon thereafter, Plaintiff received another notification from NFCU confirming the checks were accepted for deposit but subject to the standard two-day hold. Notwithstanding this notification, Plaintiff claims that NFCU froze his account on October 12, 2021, leaving him with only $2,000 available in his account. Plaintiff alleged that he then arranged for the payor of one of the checks, in the amount of $20,200.48, to be wired directly to the account. Plaintiff conceded that he ultimately also received the funds from one of the other checks in the amount of $10,000. The crux of Plaintiff's complaint was NFCU's alleged failure to make available to him the funds from the other two checks totaling approximately $41,000. Based on this alleged failure, Plaintiff asserted several tort claims, which included a request for punitive damages, as well as a breach of contract claim.

NFCU timely removed the action from state court to federal court and moved to dismiss. In opposition to the motion, Plaintiff withdrew his tort claims and his request for punitive damages, and argued that, as a result, the court lacked subject matter jurisdiction as the amount in controversy did not exceed $75,000. Plaintiff also argued that his breach of contract claim was properly stated and should be able to proceed to discovery.

In its decision, the district court first addressed the subject matter jurisdiction question, finding that while Plaintiff's abandonment of his tort claims and request for punitive damages likely capped his damages at $41,000, the fact that Plaintiff did so after removal did not deprive the court of jurisdiction.

Turning to Plaintiff's breach of contract claim, the court held that Plaintiff's failure to append a copy of the contract to the complaint and cite to any provision of the contract that was allegedly breached warranted dismissal of the breach of contract claim. The court

In This Issue

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further noted that while Plaintiff should be given an opportunity to amend, the contract, which NFCU provided on its motion, specifically permitted NFCU to restrict or suspend Plaintiff's access to his account based on conduct that it deemed suspicious or fraudulent and delay availability of funds for checks larger than $225.

The court also cast doubt on any claim by Plaintiff premised on NFCU's alleged failure to give him a reason for restricting his account or on the allegation that NFCU failed to return funds to one of the payors after the funds were removed from Plaintiff's account. As to the former, the court again noted that Plaintiff had not identified a specific contractual provision obligating NFCU to provide him a reason for restricting his account. As for the latter, the court questioned whether Plaintiff would have standing as the funds removed from his account belonged to the payor, not him, once they were removed.

Federal Court Dismisses Complaint Against Bank Relating to Embezzlement by Customer's Employee

In *LD Mgmt. LLC and Michael Lukacs v. First Republic Bank, Inc.*, 21-cv-18427 (D.N.J. Sept. 27, 2022), the district court dismissed plaintiffs' complaint without prejudice relating to the embezzlement of funds from plaintiffs' bank accounts at defendant First Republic Bank ("First Republic").

Plaintiff Michael Lukacs was the managing partner of plaintiff LD Management LLC ("LDM" and, together with Lukacs, "Plaintiffs"), a New Jersey LLC. Lukacs and LDM both held bank accounts at First Republic, a San Francisco-based financial institution. Plaintiffs' accounts, however, were managed by First Republic's New York City branch.

In 2014, a former LDM employee ("Doe") began a plot to embezzle funds from LDM by submitting two documents to First Republic adding herself as an authorized user to Plaintiffs' accounts. First, Doe submitted an Amended and Restated Company Agreement, which named Lukacs and Doe as company managers. Doe also submitted a New York Short Form Power of Attorney designating herself as Lukacs' power of attorney, a document that was notarized by Doe herself. From 2016 through 2020, Doe initiated several unauthorized transactions whereby she embezzled more than $1 million from Plaintiffs. Generally, Doe would request a cash withdrawal from First Republic's New York City branch to be picked up by her husband. Doe used a fraudulent signature stamp to process large cash withdrawals that would be picked up by a third-party. Occasionally, First Republic requested verbal confirmation of the withdrawals and third-party pickup, which was provided by Doe. Lukacs claims First Republic never informed him of these withdrawals. On other occasions, Doe would write checks from Lukacs' personal account to herself or to trusts she controlled. Upon discovery of the embezzlement, Doe's employment at LDM was terminated.

In October 2021, Plaintiffs filed a complaint in federal court in New Jersey alleging that First Republic breached various duties by allowing Doe to embezzle their funds over several years. Specifically, Plaintiffs asserted the following claims: (i) violation of N.J. Stat. Ann. §§ 12A:4A-202–203; (ii) negligence; (iii) breach of contract; (iv) breach of the covenant of good faith and fair dealing; (v) conversion pursuant to N.J. Stat. Ann. § 12A:3-420; and (VI) common law conversion. First Republic subsequently moved to dismiss all claims for failure to state a claim upon which relief can be granted pursuant to Federal Rule of Civil Procedure 12(b)(6).

The court noted that Counts I and V of the complaint asserted claims under New Jersey's version of the Uniform Commercial Code ("UCC"). However, the parties subsequently agreed that Count I was governed by California Law and Count V was governed by New York law. Thus, the court dismissed these claims and granted Plaintiffs leave to amend.

First Republic also argued that Plaintiffs' remaining common law claims were preempted by the UCC. While claims relating to unauthorized checks and wire transfers are generally preempted, the court recognized that claims alleging negligence in the opening of an account may proceed. Here, Plaintiffs' negligence claim was based solely on the unauthorized transfers allowed by First Republic. Thus, the court dismissed the negligence claim (Count II) as preempted. The court also dismissed Plaintiffs' breach of contract (Count III), breach of the covenant of good faith and fair dealing (Count IV) and Conversion (Count VI) as similarly falling within the purview of the UCC. The court noted, however, that its dismissal was without prejudice to the filing of a "properly supported motion to amend the complaint."

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