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RECORD RETENTION

New changes to Federal rules of evidence require companies involved in litigation to preserve their records, including electronic records and electronic communications. Any financial institution that becomes involved in a dispute that could possibly lead to litigation should consult with its attorneys about requirements to preserve records. Improper destruction of records could have serious adverse consequences in litigation.

Proper record retention should not be left to chance. All companies should have formal record retention and destruction policies, and should strictly abide by those policies. Keeping documents too long may result in damaging information being made available in litigation. But, haphazard destruction may raise an implication that the company tried to destroy damaging information.

TAX CREDIT FINANCING

State and federal tax credits are available for certain construction projects, and such credits can be pledged to secure financing of the project. State tax credits can be pledged outright. However, to have the benefit of historic tax credits the financial institution actually has to become a limited partner or limited liability company member of the entity that is earning the credits. Taking an interest in federal tax credits is a much more complicated process.

Taking a pledge of Missouri state tax credits is not difficult, but it is not done through the standard security agreement – UCC1 process. State tax credits are not perfected by filing a UCC1, and the state will not confirm a pledge of tax credits. An effective pledge of state tax credits involves a pledge agreement, powers of attorney to claim the credits, presigning credit applications, restrictions on the ability of consultants to certify completion of work, and monitoring construction to assure that the required work is done to earn the credits. State tax credits can be good collateral, but you need to know what you are doing to make them safe and enforceable collateral.

MAILING ACCOUNT STATEMENTS TO THE RIGHT PLACE

The time for a customer to discover and report unauthorized checks drawn on the customer's account begins to run when the account statement is delivered to the customer or made available to the customer. Therefore the time after which the bank is no longer liable for paying an unauthorized check will be delayed if the statements are not properly delivered. In the New York case of Robinson Motor Xpress, Inc. v. HSBC Bank, USA, the customer's account agreement provided that statements would be mailed to the address provided on the signature card unless that address was subsequently changed by an authorized signer on the account. The original signature card required that the statements be mailed to the office of the customer's accountants. Several months before the alleged forgeries began the bank began to mail the statements to the customer's office address even though there was no duly authorized change in address instruction. Apparently, a dishonest employee told the bank to send the statements to the customer's office so the employee could control the statements. Because the bank did not follow its own rules, the court held that the statements were never properly made available to the customer and the time period for the customer to discover and report unauthorized checks never even started running. As a result, the bank was liable for unauthorized checks for a significantly longer period of time than if statements were properly directed. Lesson learned – be sure that statements are being mailed to appropriate addresses and that such mailings comply with any standards established by the bank in its account agreements.

SETOFF v. SECURITY INTEREST

Most standard account agreements and pledge agreements give a bank a right of setoff against deposit accounts to pay defaulted loans. In most states this language is not necessary because there is an automatic right of setoff. But, these forms are missing the boat with respect to protecting the bank. A right of setoff is subject and subordinate to any claims that arise before the bank actually exercises the right of setoff, such as garnishments or tax levies, which means that the bank could lose the money to another creditor. What the bank should have in its security agreements and account agreements is a grant of a security interest in all deposits. When the bank has a security interest in deposits, the bank's rights to those funds will be superior to garnishments and tax levies.

The contents of this Update are for general information only. Consult your legal counsel before taking actions in reliance on anything contained in this law update. To cancel receipt of the Banking Law Update, send an e-mail and request "Cancel Update".

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