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New York Court Of Appeals Decision Significantly Affects Multinational Financial Institutions, Requiring that Customer Assets Held By a Bank Outside the United States Be Made Available In New York To Satisfy a Judgment Against the Bank's Customer

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In *Koehler v. Bank of Bermuda*,[1] a decision having significant consequences for national and multinational financial institutions doing business in New York, the New York Court of Appeals ruled in June that a court sitting in New York has the power to require a foreign bank over which the court has personal jurisdiction to satisfy a judgment against the bank's customer by delivering into New York assets that had been held by the bank outside the state, or even outside the country. This was the case even though neither the judgment creditor nor the judgment debtor had any relationship with New York, and the judgment itself had been obtained in another state, as noted by the dissent in the Court's split 4-3 decision.

The *Koehler* decision substantially increases the likelihood that banks, brokerage firms, insurance companies and other financial services firms having a presence in New York will find themselves involved in judgment enforcement proceedings in the New York courts. Creditors holding judgments against a financial institution's customers likely will employ the judgment enforcement mechanisms available under New York rules, and seek to compel the institution to deliver the assets to New York for the benefit of the judgment creditor assets held by the institution anywhere in the world.

In the six months since *Koehler* was decided, few courts yet have had an opportunity to address the implications of the Court of Appeals decision. In one recent decision, however, a federal district court declined to extend *Koehler* to a case involving a pre-judgment temporary restraining order enjoining transfer of the defendants' assets that had been served on a bank's New York branch, holding that under New York's "separate entity rule" each bank branch is treated as a separate entity and service of the TRO on the bank's New York branch did not reach an out-of-state branch that did not have actual notice of the order.[2] Further litigation over the scope of the *Koehler* decision, and the application of *Koehler* to particular facts and circumstances, should be expected.

The Facts of *Koehler*

In 1993, the plaintiff, Koehler, a resident of Pennsylvania, obtained a default judgment of approximately $2 million against his former business partner, Dodwell, a resident of Bermuda. The default judgment was obtained in an action filed in the United States District Court in Maryland.

Shortly thereafter, in October 1993, Koehler sought to enforce his judgment by filing a petition against Bank of Bermuda Ltd. (the "Bermuda bank") in the United States District Court for the Southern District of New York seeking an order compelling the Bermuda bank to turn over property belonging to Dodwell. In particular, Koehler sought to recover stock certificates in a Bermuda corporation owned by Dodwell that Dodwell had pledged to the Bermuda bank in return for a loan. Two days after the petition was filed, the court issued a turnover order compelling the Bermuda bank to deliver the stock certificates or pay sufficient money to satisfy the judgment.

Following entry of the turnover order, Koehler and the Bermuda bank engaged in litigation for 10 years on the issue of whether the Bermuda bank was subject to the personal jurisdiction of the New York courts. In commencing the proceeding in New York, Koehler had served process upon an officer of Bank of Bermuda (New York) Ltd., which Kohler claimed was a subsidiary and agent of the Bermuda bank. The Bermuda bank argued that service upon its New York subsidiary did not subject the Bermuda bank to personal jurisdiction. Ultimately, however, in late 2003, the Bermuda bank conceded that it was subject to personal jurisdiction in New York as of the time that Koehler had commenced the proceeding.

By the time the jurisdictional issue was resolved, the Bermuda bank no longer held the share certificates. Despite the turnover order that had been entered ten years earlier, the Bermuda bank had transferred the certificates to a Dodwell-related entity after the loan for which the certificates had been held as collateral was satisfied.

After learning that the shares were no longer held by the Bank, the District Court dismissed the petition in March 2005, ruling, among other grounds, that the court had no jurisdiction over Dodwell's shares.[3] Koehler appealed to the Second Circuit, which determined that there was no controlling New York precedent on the question of whether a court in New York has the authority to order a party other than the judgment debtor itself, to deliver assets into New York when the court has personal jurisdiction over that party but the assets are not located in New York.[4] In the absence of controlling authority, the Second Circuit certified this dispositive question for determination by the New York Court of Appeals.

The Majority's Reasoning

The Court of Appeals majority answered the certified question by ruling that under Article 52 of the New York Civil Practice Law and Rules (CPLR), the statute containing procedures for the enforcement of money judgments, a New York court does have the authority to order a bank over which it has personal jurisdiction to deliver stock certificates owned by judgment debtor or cash equal to their value to a judgment creditor, even where the stock certificates are located outside New York.

The Court began its analysis with the language of CPLR Section 5225 which authorizes a judgment creditor to enforce its judgment by commencing a special proceeding against a garnishee holding assets belonging to the judgment debtor, and obtain a "turnover order" or "delivery order" compelling the garnishee to deliver the property in which the judgment debtor has an interest, or to convert it to money for the payment of the debt. [5]

In considering a New York court's power over the garnishee with regard to property located outside the state, the Court found that CPLR Article 52 "contains no express territorial limitation" restricting a turnover order to property located in New York, and the Court determined that there was no basis to infer a territorial limitation "from the broad language presently in the statute."[6] The Court also concluded that the New York legislature intended CPLR Article 52 to have extraterritorial reach, relying on 2006 amendments to CPLR Section 5224 requiring disclosure of out-of-state material in response to information subpoenas served by judgment debtors. In addition, the Court found no reason under the statute to treat a garnishee differently than a judgment debtor, and the parties had acknowledged that a New York court has the power to compel the judgment debtor to bring property into the state when the judgment debtor is subject to the court's personal jurisdiction.

In ruling that a New York court had the power to compel a garnishee to deliver out-of-state property into New York, the Court differentiated between the procedures for enforcing money judgments as set forth in CPLR Article 52, with the procedures for obtaining a pre-judgment attachment under CPLR 62. In the case of an attachment of particular property, the Court acknowledged the well-established rule that the property "must be within the jurisdiction of the court issuing the process," but the Court found no reason to apply that rule to the enforcement of a money judgment where the court had personal jurisdiction over the garnishee.[7]

The Dissent

The dissent, written by Judge Smith, expressed concern that there were no New York contacts with the parties or the underlying dispute, except the amenability of the Bermuda bank, the garnishee, to personal jurisdiction in the state. In those circumstances, Judge Smith wrote that the majority opinion created a "forum shopping opportunity," for any judgment creditor trying to reach an asset of any judgment debtor held by a bank or other garnishee anywhere in the world, regardless of whether New York has any relationship with the judgment debtor, the judgment or the dispute.[8]

The dissent also expressed concern that banks and other financial institutions could find themselves subject to competing claims to the judgment debtor's assets in multiple jurisdictions, which Judge Smith characterized as a "recipe for trouble" likely to disrupt the business of banks with offices in several states or countries.[9]

In the absence of evidence that the legislature intended this result or to permit the garnishment of property outside of New York, the dissent would not have interpreted the CPLR 5225 to have extraterritorial effect.

Although the constitutional issue was not before the Court, the dissent also wrote that application of the majority's broad view of New York's garnishment remedy might exceed the limits on New York's jurisdiction under the Due Process Clause of the Federal Constitution. Where the judgment debtor itself did not have sufficient contacts with New York under the standards articulated in *International Shoe Co. v. Washington,*[10] the dissent reasoned that a New York court may not have the constitutional authority to compel the turnover of the judgment debtor's property notwithstanding its personal jurisdiction over the garnishee.

Limitations to *Koehler*

Although few courts yet have had an opportunity to address *Koehler*, one federal district court recently declined to extend the Court of Appeals rationale to a case involving a temporary restraining order enjoining a bank from transferring the defendant's assets. In *John Wiley & Sons, Inc. v. Kirtsaeng*,[11] plaintiff had obtained a prejudgment temporary restraining order and order of attachment, which it served on a Bank of America branch in New York City. Subsequently, the plaintiff sought to hold the bank in contempt when a different Bank of America branch, located in California, permitted the defendant to withdraw funds from his account.

In denying the motion for contempt, the district court ruled that the service of the temporary restraining order on the bank's New York branch was not effective to bind other branches in the absence of actual notice of the order by the other branch. Relying on New York's "separate entity rule," the district court held that "each branch of a bank is treated as a separate entity. . . in no way concerned with accounts maintained by depositors in other branches or at a home office."[12] Accordingly, the district court further held that notice received by one branch of a bank does not constitute even constructive notice to any other branch of the same bank.

The district court also distinguished *Koehler* as limited to post-judgment enforcement actions where the judgment creditor actually files an action against the bank, and obtains personal jurisdiction over the bank. In *John Wiley*, by contrast, it appeared that the plaintiff had merely provided one branch of the bank with notice of an order obtained in an action where the bank itself was not a party, and the plaintiff had not effectively obtained personal jurisdiction over the bank.

Ramifications for Financial Services Firms

As articulated by the dissent, the *Koehler* decision imposes significant obligations and risks on national and multinational financial services firms doing business in New York. A multinational bank having a New York branch, for example, may be the subject of an order from a New York court requiring it to deliver customer assets held anywhere in the world, if the bank's New York presence is sufficient to subject it to general *in personam* jurisdiction in the state. Future cases may involve substantial litigation over whether the New York courts have personal jurisdiction over the entity holding the judgment debtor's assets. Depending on the particular facts and circumstances, a foreign bank may be subject to personal jurisdiction in New York based on the presence of a branch office or agency operation in New York or, potentially, through a separately incorporated subsidiary doing business in New York whose nexus to the parent satisfies minimum jurisdictional requirements.

While the specific facts of *Koehler* involved a bank holding stock certificates as collateral, the Court's reasoning is by no means limited to those facts. Banks, broker-dealers, and other financial institutions may be named as parties in proceedings under CPLR Article 52 in which a judgment creditor seeks turnover of cash held on deposit, securities held pursuant to a custody agreement and other assets, anywhere in the world, as to which the financial institution has possession. Private investment funds having a New York presence, including offshore funds that conduct administrative or sales activity in New York, may also be the subject of turnover proceedings by creditors holding judgments against investors in the fund.

In many cases where a turnover order is sought, there may be other parties who claim an interest in the assets, and the financial institution may itself have such a claim. In these cases, the financial institution may seek to avoid the possibility of inconsistent judgments by joining all competing claimants to the turnover proceeding. In the event that the New York courts do not have jurisdiction over all claimants, the institution may seek dismissal of the New York action on the ground of *forum non conveniens,* in favor of litigation in a forum where all claimants can be joined. There is no certainty that such a motion will be granted in light of *Koehler*.

Although the *Koehler* decision addresses at length the extraterritorial effect of a turnover proceeding under CPLR Section 5225, the decision does not address the extraterritorial effect of other judgment enforcement mechanisms under Article 52, such as restraining notices as referred to in CPLR Section 5222. That section provides that a judgment creditor unilaterally may serve a restraining notice on a garnishee which is then required to freeze the judgment debtor's assets until a turnover order can be obtained. Citing *Koehler*, judgment creditors may argue that an institution served with a restraining notice in New York, and subject to personal jurisdiction in New York, is obligated to comply with the restraining notice with regard to assets located anywhere in the world. The federal district court's decision in *John Wiley & Sons, Inc. v. Kirtsaeng,* however, suggests otherwise. Uncertainty as to the scope and extent of *Koehler* may be clarified in future litigation.

[1] *Koehler v. Bank of Bermuda,* 12 N.Y. 3d 533, 833 N.Y.S.2d 763 (2009).

[2] *John Wiley & Sons, Inc. v. Kirtsaeng*, 2009 WL 3003242 (S.D.N.Y. 2009).

[3] 2005 WL 551115, 2005 US Dist. LEXIS 3760 (S.D.N.Y Mar. 9, 2005).

[4] 544 F. 3d 78 (2d Cir. 2008).

[5] 12 N. Y. 3d at 537.

[6] *Id.* at 539.

[7] *Id.* at 538-39 (citing *National Broadway Bank v. Sampson*, 179 N.Y. 213, 223 (1904), and other authorities).

[8] *Id*. at 543.

[9] *Id.* at 542.

[10] 433 U.S. 310 (1945).

[11] 2009 WL 3003242 (S.D.N.Y. 2009).

[12] 2009 WL 3003242, at *3 (*quoting Motorola Credit Corp. v. Uzan*, 288 F Supp. 2d 558, 560 (S.D.N.Y. 2003)).