UNITED STATES OF AMERICA
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
OFFICE OF HEARINGS AND APPEALS

In the Matter of: **nBank NA** Petitioner.	HUDOHA NO. 13-VH-0083-AO-003 Claim No. 7-207074860A August 19, 2013

DECISION AND ORDER

On December 3, 2012, nBank, N.A. ("Petitioner") was notified that pursuant to 31 U.S.C. §§ 3716 and 3720A, the Secretary of the U.S. Department of Housing and Urban Development ("HUD") intended to seek administrative offset of any federal payment due to Petitioner in order to satisfy Petitioner's alleged debt to HUD.

Applicable Law

The Office of Hearings and Appeals has jurisdiction to determine whether Petitioner's debt is past due and legally enforceable. 24 C.F.R. § 17.81 (b). This hearing is authorized by the provisions of the Deficit Reduction Act of 1984 (31 U.S.C. § 3716) and the Debt Collection Improvement Act of 1996, as amended (31 U.S.C. § 3720), and applicable HUD regulations. In an administrative offset proceeding, Petitioner bears the burden of proving that all or part of the alleged debt is not past due or not legally enforceable. 24 C.F.R. § 17.69 (b). This hearing shall be conducted in accordance with the procedures set forth at 24 C.F.R. §17.73, and 31 C.F.R. § 285.11, as authorized by 24 C.F.R. §17.81(a).

Procedural History

On January 30, 2013, Petitioner requested a hearing concerning the existence, amount, or enforceability of the alleged debt. Pursuant to 24 C.F.R. § 17.77, this Court stayed referral of the debt to the U.S. Department of the Treasury for administrative offset pending the outcome of this written decision. (*Notice of Docketing, Order, and Stay of Referral* ("*Notice of Docketing*"), dated February 4, 2013.) On February 20, 2013 and February 27, 2013, Petitioner filed his documentary evidence. On March 4, 2013, the Secretary filed his *Statement* along with documentary evidence. This case is now ripe for review.

Background

In September 2006, HUD's Quality Assurance Division/Lender Monitoring Team ("QAD") conducted a review of Petitioner's mortgage finance operation to determine whether Petitioner (a HUD-authorized Direct Endorsement mortgage lender) complied with HUD's rules and regulations when underwriting and issuing FHA-insured mortgages. (*Secretary's Statement*

("*Sec'y Stat.*") ¶ *2, filed March 4, 2013*; *Declaration of Michael C. DeMarco ("DeMarco Decl.")* ¶ *4.*) During its review, the QAD found that while underwriting the mortgage of Gary Baker (FHA Case No. 411-3916380), Petitioner engaged in non-compliant lending activities that exposed HUD to an unacceptable level of risk. (*Sec'y Stat.* ¶ *3*; *DeMarco Decl.* ¶ *4.*) To resolve the QAD's findings, Petitioner entered into an Indemnification Agreement with HUD, dated September 27, 2006. (*Sec'y Stat.* ¶ *4*; *DeMarco Decl.; Exhibit A, Indemnification Agreement.*) In the Indemnification Agreement, Petitioner agree to "indemnify HUD for losses which have been or may be incurred related to ... FHA Case Number 411-3916380 ... which is in default, or goes into default, through and up to five years from the date HUD executes this agreement..." (*Sec'y Stat.* ¶ *5, DeMarco Decl.; Exhibit A* ¶ *1.*) HUD signed the Indemnification Agreement on September 27, 2006.

On May 1, 2010, three years and eight months later, Gary Baker defaulted on his FHA-insured mortgage. (*Sec'y Stat.* ¶ *6, DeMarco Decl.* ¶ *5; Exhibit B, FHA Case Details report.*)

On June 3, 2011, Wells Fargo Bank, N.A. ("Wells Fargo") transferred the property to HUD.[1] (*Sec'y Stat.* ¶ *7, DeMarco Decl.* ¶ *5-6.*) HUD paid insurance benefits to Wells Fargo on June 9, 2011, and June 4, 2012, totaling $93,749.85 (*Sec'y Stat.* ¶ *7, DeMarco Decl.* ¶ *5-6.*) On April 9, 2012, HUD sold the property at a loss for $23,500. (*Sec'y Stat.* ¶ *8.*) As a result, HUD has calculated the Department's loss on this case as follows:

Partial Settlement (Part A Claim Payment)	$83,559.19
Final Settlement (Part B Claim Payment)	$10,190.66
Taxes	$2,871.70
Maintenance and Operation	$6,416.40
Sales Expenses	$1,637.50
Sales Price	($23,500.00)
Total loss/Total due HUD	$81,175.45

(*DeMarco Decl.* ¶ *6.*)

Since the sale of the property did not provide enough funds to cover all of HUD's expenses, HUD sought indemnification from the Petitioner for HUD's loss. (*Sec'y Stat.* ¶ *9, DeMarco Decl.* ¶ *7*). HUD has unsuccessfully attempted to collect on the claim from Petitioner. (*Sec'y Stat.* ¶ *9, DeMarco Decl.* ¶ *7.*) HUD alleges Petitioner is indebted to the Secretary on the claim in the following amounts:

(a) $81,175.45 as the unpaid principal balance as of January 31, 2013;
(b) $1,612.56 as the unpaid interest on the principal balance at 5.0% per annum through January 31, 2013;
(c) $4,946.99 as the unpaid penalties through January 31, 2013;

[1] Although a loan correspondent sponsored by Petitioner underwrote and originated Gary Baker's mortgage, at the time of default the mortgage and note were held by Wells Fargo Bank, N.A.

(d) $35.33 as the unpaid administrative costs through January 31, 2013; and
(e) interest on said principal balance from February 1, 2013, at 5.0% per annum until paid.

(*Sec'y Stat.* ¶ 10, *DeMarco Decl.* ¶ 7.)

A Notice of Intent to seek offset of federal payments due Petitioner was sent to Petitioner on December 3, 2012 (*Sec'y Stat.* ¶ *11, DeMarco Decl.* ¶ *8.*)

Discussion

Petitioner does not dispute the existence or amount of the debt incurred, or the fact that the debt is delinquent. Rather, Petitioner asserts that the alleged debt is unenforceable because: 1) effective June 25, 2007, Petitioner's charter to operate as a national bank was terminated by the Office of the Comptroller of the Currency ("OCC"); and, 2) the Indemnification Agreement ("Agreement") has expired.

Petitioner first claims that "If you will check the Office of Comptroller ("OCC") website, you will note that nBank surrendered its charter to the OCC in June 2007 and is no longer in business." (*Pet'r's Hr'g. Req.*) As support, Petitioner submitted a copy of the OCC Conditional Approval #807 dated June 8, 2007. (Id., Attachment A.) Petitioner also provided a copy of a webpage from OCC's online site showing, more specifically, that "nBank's N.A.'s charter was terminated on June 25, 2007." (*Letter from Petitioner, "Ptr.'s Feb. Ltr.,"* dated February 27, 2013). Based upon the evidence presented, Petitioner claims that nBank, N.A. is no longer liable for the debt that is the subject of this proceeding.

The Secretary counters by stating that the "termination of Petitioner's charter to operate as a national bank under the supervision of the OCC does not exempt Petitioner from liability under the terms of the Indemnification Agreement." (*Sec'y. Stat.*, ¶ 13.) "Petitioner's charter was terminated when it sought permission from the OCC to voluntarily liquidate its assets by selling substantially all of its assets and liabilities to First Covenant Bank of Woodstock, Georgia ("FCB") and merging nBank with its parent corporation nBank, Corp. ("NBC")." (*Sec'y Stat.*, ¶ 14, *Exhibit B.*) Pursuant to the terms of nBank's voluntary liquidation, FCB purchased substantially all of Petitioner's assets, *and* assumed "substantially all of its liabilities..." (emphasis added.) *(Sec'y. Stat.*, ¶ 15). As a result, "after the merger it was expected that NBC would "manag[e] any remaining assets and liabilities of nBank..." Id. at ¶ 16.

Generally, a purchasing corporation does not assume the liabilities of the seller. *Bullington v. Union Tool Corp.*, 328 S.E.2d 726, 727 (1985). "Georgia however, like most jurisdictions, has identified exceptions to the general rule and allows for successor liability where (1) there is an agreement to assume liabilities; (2) the transaction is, in fact, a merger; (3) the transaction is a fraudulent attempt to avoid liabilities; or, (4) the purchaser is a mere continuation of the predecessor corporation." *Tindall v. H & S Homes, LLC,* 5:10-CV-044 CAR, 2011 WL 4345189 (M.D. Ga. Sept. 15, 2011) (noting that successor liability could be used as a theory to establish the Defendant's liability).

The instant case falls under two of the four exceptions that permit successor liability. The transaction between NBC and Petitioner constituted a merger, and additionally, there was an agreement to assume liabilities between Petitioner and NBC and FCB. The Supreme Court of Georgia discussed the second exception to the general rule, a merger transaction, in *Mobley v. Hagedorn Const. Co.*, 147 S.E. 890 (1929). In *Mobley*, the Hagedorn Construction Company initiated a suit against the Bank of Chatsworth requesting a mandamus to compel the bank to pay a county warrant that Hagedorn claimed was owed. While the case was pending, the Bank of Chatsworth sold its assets to the Georgia State Bank of Atlanta. The plaintiff argued that the Georgia State Bank did not assume or intend to assume the liability of the Bank of Chatsworth to Hagedorn or to Murray County. Rather, the plaintiff argued that it only agreed to assume certain specified liabilities in a list of liabilities attached to the contract between the two banks. The Court rejected both arguments and determined that the contract constituted a merger between the two banks and that the Georgia State Bank assumed all the liabilities of the Bank of Chatsworth under the law relating to mergers. The Court further noted that:

> Where by reason of the consolidation of two corporations one of them goes entirely out of existence, and no arrangements are made respecting the liabilities of the one which ceases to exist, the corporation resulting from such combination will, as a general rule, be entitled to all the property *and [is] answerable for all liabilities of the corporation thus absorbed.*

(emphasis added.) *Id.* at 893.

Similarly in this case, the transaction between Petitioner and NBC constitutes a merger with approval by the OCC under Mergers and Consolidations with Subsidiaries and Nonbank Affiliates, 12 U.S.C. §215a-3. After approval of this transaction by the OCC, a certificate of merger was issued by the Georgia Secretary of State on June 22, 2007, listing NBC as the surviving entity. In its conditional approval, the OCC states "In the Merger, nBank will be merged into NBC. NBC will be the surviving entity, and nBank will cease to exist. The Merger is authorized under 12 U.S.C. Section 215a-3." (*Sec'y Stat., Exhibit B.*) Since the transaction between Petitioner and NBC was considered a merger, NBC became responsible for the payment of Petitioner's alleged debt because it assumed Petitioner's liabilities. This means that Petitioner cannot avoid liability for the subject debt based solely on the fact that as a result of the merger, it ceased to exist and as a result was released from its responsibility for existing debt obligations. See Laboratory Corp. of America v. Professional Recovery Network, 813 So. 2d 236, 269 (the basis for finding successor liability is founded upon the notion that "no corporation should be permitted to commit a tort or breach of contract and avoid liability through corporate transformation in form only." (citing Amjad Munim, M.D., P.A. v. Azar, 648 So.2d 145, 154 (Fla.Dist.Ct.App.1994)).

Even if the transaction between Petitioner and NBC did not constitute a merger, Petitioner still could be held liable for the subject debt because of the Purchase and Assumption ("P&A") Agreement entered into by Petitioner, NBC, and FCB to assume Petitioner's liabilities. In a similar case, FieldTurf USA Inc. v. TenCate Thiolon Middle E., the Northern District Court of Georgia found that a corporation could be liable for claims of fraud against a second corporation when the first corporation agreed to assume the second corporation's liabilities.

2013 WL 1963918 (N.D. Ga. May 10, 2013). In that case, Royal TenCate N.V. ("Royal") acquired certain assets of Mattex Leisure Industries ("Mattex") pursuant to an asset purchase agreement. Royal then nominated its rights and obligations under the Asset Purchase Agreement to TenCate Thiolon Middle East, LLC ("TenCate ME"). Id. The Court relied upon the terms of the asset purchase agreement to determine whether TenCate ME agreed to assume liability for the claims of fraud against Mattex. *Id.* After examining the agreement and parol evidence presented, the Court found that Mattex intended TenCate ME to assume all future liabilities for claims brought against it, and that TenCate ME had intended to assume these liabilities. Id. The Court also found that nothing in the asset purchase agreement precluded assumption of the fraud claims against Mattex by TenCate ME, and as a result, TenCate ME could be held liable for Mattex's fraudulent conduct. Id.

The case at hand presents a similar scenario but instead involves the assumption of liabilities. Here, Petitioner, NBC, and FCB entered into an agreement whereby NBC agreed to assume Petitioner's liabilities. (*See Sec'y. Stat.*, Exhibit B.) The OCC reviewed the proposed merger agreement between Petitioner and NBC and, in its approval, noted that "most of nBank's assets, all of its deposits, and most of its other liabilities will have been transferred to FCB." (Id.) The OCC further acknowledged that "NBC's sole activities will consist of managing any remaining assets *and liabilities* of nBank after the P&A transaction." (emphasis added.) Id. Such an agreement between Petitioner and NBC for NBC to assume Petitioner's liabilities is sufficient to establish that Petitioner shall remain responsible for the subject debt.

In addition, according to the Georgia Secretary of State Corporations Division, both NBC and FCB remain active as corporations licensed to do business in the state of Georgia. *(Sec'y. Stat.*, Exhibit C.) Petitioner, NBC, and even FCB made contingencies as a part of the voluntary liquidation of Petitioner in order to ensure that all of Petitioner's liabilities would be assumed either by NBC or FCB. (*Sec'y Stat.*, Exhibit B, p.4.) As a result, the termination of Petitioner's charter to operate as a national bank under the supervision of the OCC does not exempt Petitioner, NBC, or FCB from liability under the terms of the Indemnification Agreement. I find, therefore, that Petitioner remains legally obligated to pay the debt that is the subject of this proceeding.

Next, Petitioner argues that the Indemnification Agreement expired on September 27, 2011, five years after it was signed and as such, it is no longer obligated to abide by the terms of the Indemnification Agreement. Petitioner states that "In addition to the fact that nBank no longer exists, in reviewing the attached indemnification that nBank executed on the loan in question, please note that paragraph 1 of the Indemnification Agreement sets forth a five year period that expired on September 27, 2011." *(Pet'r's Hr'g. Req.)* However, Petitioner has misinterpreted the terms of the Agreement. The Agreement provides that "Petitioner would indemnify HUD should Mr. Baker default on his loan within five years." (*Sec'y. Stat.*, Exhibit A, *DeMarco Decl.*, Exhibit A, ¶ 1.) Here, Mr. Baker defaulted on the loan three years and eight months after it was signed, which by calculation falls within the five year period set forth in the terms of the Agreement. Such default also occurred before the Agreement's expiration date of September 27, 2011. The Agreement therefore had not expired before Petitioner defaulted on the loan. As a result, the Court finds that Petitioner's claim is meritless.

ORDER

Based on the foregoing, the Order imposing the stay of referral of this matter to the U.S. Department of Treasury for administrative offset is vacated.

The Secretary is authorized to seek collection of this outstanding obligation by means of administrative offset of any eligible Federal payments due to Petitioner. It is

SO ORDERED.

Vanessa L. Hall
Administrative Judge

Review of determination by hearing officers. A motion for reconsideration of this Court's written decision, specifically stating the grounds relied upon, may be filed with the undersigned Judge of this Court within 20 days of the date of the written decision, and shall be granted only upon a showing of good cause. Should a Decision and Order upon Reconsideration be issued thereafter it shall be considered final unless a party timely appeals the determination in accordance with 24 C.F.R. § 26.26 (2012). Any party may request, in writing, Secretarial review of the determination within 30 days after the hearing officer issues the determination in accordance with § 26.26 of this part.