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COMMENTARY

New York Puts Assets in Foreign Bank Branches Beyond the Reach of Judgment Creditors

Two weeks ago, the New York Court of Appeals issued a decision of great importance to global financial institutions. For the first time, the state's highest court confirmed that New York common law prevents a court from freezing a civil judgment debtor's assets held in foreign bank accounts. *Motorola Credit Corp. v. Standard Chartered Bank*.[1] In its highly anticipated decision, the court expressly adopted New York's nearly century-old "separate entity rule," which provides that even when a bank branch is subject to personal jurisdiction in New York, that bank's other branches are treated as separate entities for purposes of judgment enforcement, putting them beyond the reach of judgment creditors.[2]

Motorola is a particularly noteworthy decision for the international banking community because just five years ago, in *Koehler v. Bank of Bermuda*,[3] the court of appeals eschewed the separate entity rule in favor of one bank worldwide, enabling judgment creditors to reach far beyond New York's borders to grab debtors' assets. *Koehler* held that a bank subject to personal jurisdiction in New York could be ordered to deliver to a judgment creditor assets in a foreign branch even where the underlying litigation, the targeted assets, and the parties themselves bore no connection to New York. In the wake of *Koehler*, judgment creditors worldwide flocked to New York courts as a portal to reach assets all over the world, demanding that banks located in the state turn over a judgment debtor's assets in faraway places.

With *Motorola*, the court of appeals has dramatically curtailed (and perhaps gutted) *Koehler*, limiting its application drastically and emphasizing the strong policy considerations favoring recognition of the separate entity rule and the significant restrictions that longstanding doctrine (which was never specifically discussed in *Koehler*) places on efforts to reach foreign assets. Moreover, the strong policy arguments and considerations recognized by the Court of Appeals will undoubtedly feature in other settings where the specter of double liability, conflicting obligations in multiple jurisdictions, and international comity come into play, especially in the context of international banking.

Background

In 2003, the U.S. District Court for the Southern District of New York awarded plaintiff Motorola a multibillion-dollar judgment against members of Turkey's Uzan family, finding that the Uzans diverted for their personal benefit more than US$2 billion in loans Motorola

made to a Turkish company the family controlled. For the better part of a decade, Motorola has engaged in an international hunt for the Uzans and their assets.

In 2013, as part of Motorola's efforts to collect on this judgment, the district court issued a restraining order (pursuant to New York and federal law) freezing the Uzans' assets. Motorola served the restraining order on the New York branch of non-party Standard Chartered Bank ("Standard"), a multinational bank based in the United Kingdom. Although Standard had no Uzan assets at its New York branch, its branch in the United Arab Emirates ("UAE") held about US$30 million in deposits related to the Uzans. When Standard sought to freeze those assets in accordance with the restraining order, regulatory authorities in the UAE and Jordan intervened and debited US$30 million in Standard's account at the UAE Central Bank. The rationale for this action was that Standard could not dishonor its obligations to repay UAE deposits based on an order from a foreign court.[4]

Faced with conflicting obligations and the prospect of double liability under U.S. and foreign law, Standard sought relief from the district court. Standard argued that, under New York's separate entity rule, the restraining notice Motorola served on its New York branch could not restrain assets held in another Standard branch in the UAE. Motorola responded that *Koehler* allowed the restraint of assets in the UAE via Standard's New York branch. The district court found for Standard. On appeal, the U.S. Court of Appeals for the Second Circuit certified to New York's high court the question of whether the state's separate entity rule precludes a judgment creditor from ordering a garnishee bank operating branches in New York to restrain a debtor's assets held in foreign branches of the bank. The Court of Appeals answered that it did.

Pro-Bank Policy Considerations Keep an Old Doctrine Alive

In a 5–2 decision, the Court of Appeals held that "service of a restraining notice on a garnishee bank's New York branch is ineffective under the separate entity rule to freeze assets held in the bank's foreign branches." The longstanding common law doctrine, the court held, was firmly rooted and very much alive in New York, citing state and federal decisions applying the rule for nearly a century. Driving the court's decision was the fundamental policy for the separate entity rule. Acknowledging the multiple *amicus curiae* submissions by sovereigns, regulators, and trade groups, the court recognized that allowing U.S. courts to restrain assets overseas would undermine international comity. The rule, the court held, also eliminates competing claims on the same assets and protects banks from double liability. Moreover, the rule avoids placing banks in the "difficult position of attempting to comply with the contradictory directives of multiple sovereign nations," as Standard had faced. Finally, the court recognized that directing banks to process restraint orders for foreign assets imposes an "intolerable burden" by forcing banks to identify and monitor assets in numerous foreign branches. International banks, the court held, have long relied on the benefits afforded by the separate entity rule "when deciding to open branches in New York, which in turn has played a role in shaping New York's status as the preeminent commercial and financial nerve center of the Nation and the world."

But what about *Koehler*? Just a few years ago, this same Court of Appeals held in that case that a bank subject to personal jurisdiction in New York could be ordered to deliver a judgment debtor's stock certificates located in a non-U.S. branch of the bank. The *Motorola* court rejected the argument that *Koehler* effectively overruled the separate entity rule. It noted that the parties did not raise, and the court did not address, the doctrine in that case. Moreover, the court explained, *Koehler* involved the repatriation of stock certificates and was therefore inapposite to the assets (deposit accounts) here.

An impassioned two-judge dissent argued that the majority opinion could not be reconciled with *Koehler*, and that an "outmoded" separate entity rule now frustrated collection of judgments, enabled judgment debtors to evade enforcement, and allowed international banks to shirk responsibility. Against the backdrop of global "banks being held more accountable than ever for their actions vis-à-vis their customers," the dissent described the majority opinion as a "step in the wrong direction."

Although the precise scope of the separate entity rule in the context of assets held in domestic branches (as well as assets other than deposit accounts, as in *Koehler*) has yet to be determined, judgment creditors can no longer view

New York as a haven for collecting assets located worldwide. Creditors' best course of action may be to utilize the judgment enforcement tools provided by the foreign venues in which the assets are held.

Lawyer Contacts

For further information, please contact your principal Firm representative or one of the lawyers listed below. General email messages may be sent using our "Contact Us" form, which can be found at www.jonesday.com.

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Endnotes

1 *Motorola Credit Corp. v. Standard Chartered Bank,* ___ N.Y.3d ___, 2014 WL 5368774 (N.Y. Oct. 23, 2014).
2 The authors of this *Commentary* submitted *amicus curiae* briefs in *Motorola*, on behalf of the Central Bank of Jordan, urging the Court of Appeals to uphold the separate entity rule.
3 *Koehler v. Bank of Bermuda Ltd*., 12 N.Y.3d 533 (N.Y. 2009). *See also* Sevan Ogulluk and Alan Schwartzald, "New York's High Court Beckons Foreign Judgment Creditors to New York—but does *Koehler* Loosen Cornerstone of New York's Economy?," *Bloomberg Law Reports*, New York Law, Vol. 1, No 14 (October 26, 2009); Lee A. Armstrong, William J. Hine, and Sevan Ogulluk, "New York Taps the Brakes on Foreign Judgment Collection," Jones Day *Commentary* (June 2013).
4 Motorola never attempted to domesticate its U.S. judgment in the UAE's courts.