Bankruptcies in Financial Services and Bank Holding Company Defaults

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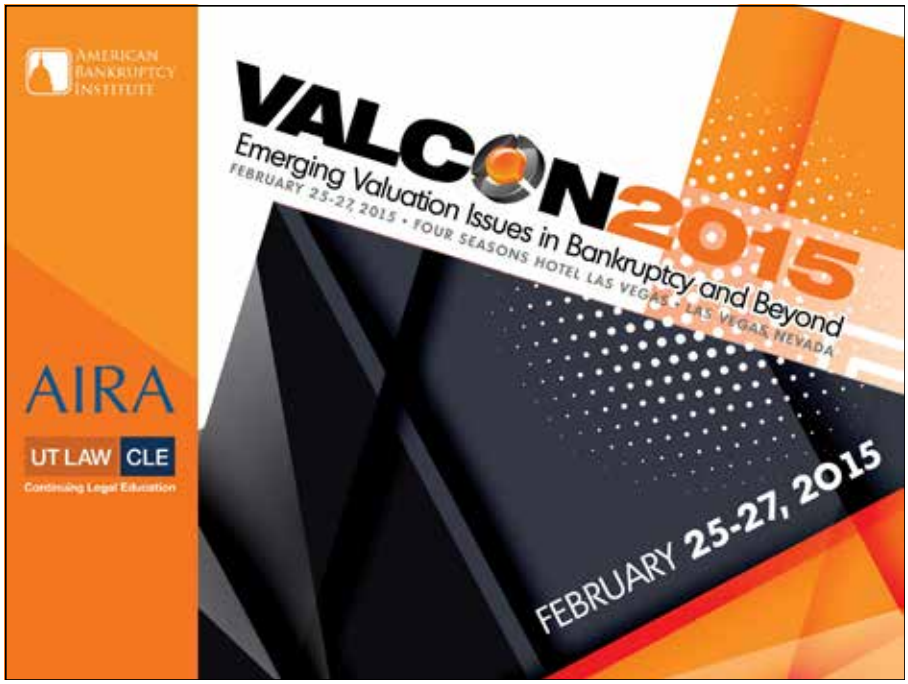

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Recent Case Law Developments in Tax Disputes Between the FDIC and Bank Holding Companies

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Background

- Since 2008, there have been over 500 bank failures resulting in the appointment of the FDIC as a receiver.
- The parent company of the failed bank is often left with worthless stock or claims against an essentially defunct entity.
- The parent company, however, has its own creditors and, usually, insufficient assets to satisfy the creditors' claims.
- One available asset is often the tax refund generated by the carry-back of net operating losses ("NOLs").

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NOLs and Consolidated Tax Group

- NOLs usually result from operating losses generated by the failed bank, such that if the bank filed its own tax returns, the bank would be entitled to direct payment of the refund.
- Generally, the parent holding company ("HoldCo") and the failed bank are parties to tax sharing agreements ("TSA") and file consolidated tax returns.
- Under the tax sharing agreements, the parent company files the tax returns and any tax refunds are paid to the parent company.

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What is the Issue?

- Since the tax refunds generated by NOLs can be significant, disputes often arise over who owns the tax refunds – the parent company or the FDIC, as receiver for the bank in receivership.
- This presentation addresses the recent case law addressing this issue where a tax sharing agreement exists.

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What are the Arguments?

- Arguments that support the tax refunds belong to the bank in receivership (and not to the parent company):
  - The parent company only holds the tax refunds in "trust" for the bank since the failed back generated the losses giving rise to the refund.
  - Support is provided by *W. Dealer Mgmt., Inc. v. England (In re Bob Richards Chrysler-Plymouth Corp.)*, 473 F.2d 262, 265 (9th Cir. 1973).
  - *Bob Richards* held that a parent company received a tax refund as an agent/ trustee for the subsidiary, and allowing the parent to keep the refund would unjustly enrich the parent.
- Parent companies and their bankruptcy estates often contend, for the reasons discussed in this presentation, that the tax refunds are paid to the parent company and that the FDIC/bank has only a contractual unsecured claim to the funds.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Background**
  - This case concerns the allocation of tax refunds pursuant to a TSA between the bank and HoldCo.
  - The TSA provided for mechanisms by which a tax group, including the bank and HoldCo, would pay taxes, receive and distribute refunds, and order tax-related affairs.
  - The bank failed and HoldCo filed for bankruptcy. Each requested refunds from IRS for year 2005.
  - Refunds were received by HoldCo and then held in escrow pending resolution of dispute.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Bankruptcy Court Opinion**
  - The bankruptcy court granted summary judgment in favor of the Liquidating Supervisor on the basis that the tax refunds were property of HoldCo's bankruptcy estate, and the FDIC had only an unsecured pre-petition claim.
  - The court also held that the Internal Revenue Code did not address relative rights to tax refunds and the TSA controlled.
  - The court rejected application of a federal common law rule stemming from the Ninth Circuit's *Bob Richards* opinion that the parent of a consolidated group receives a tax refund as trustee of a specific trust in the absence of an implied or express agreement to the contrary, since the parties had in fact entered into an agreement (the TSA).

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Bankruptcy Court Opinion (cont.)**
  - The court further held, applying Georgia law, that the TSA created a debtor-creditor relationship, and not a trust or agency one, since the TSA did not restrict HoldCo's use of tax refunds received and HoldCo was not subject to the direction or control of the bank or any group member.
    - The court placed particular significance on these facts and the fact that HoldCo was not required to escrow the refund.
  - The court also held that the economic reality of the TSA was to create a debtor-creditor relationship.
  - The court dismissed the significance of the Interagency Policy Statement on Income Tax Allocation (the "Interagency Statement") on the tax refund dispute between the bank and HoldCo.
  - The FDIC appealed.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Eleventh Circuit Opinion**
  - The Eleventh Circuit concluded the bankruptcy court erred.
  - This opinion was decided after a similar appeal in the *BankUnited* case, discussed below.
  - Consistent with the opinion from the *BankUnited* case, the court held that the determination of whether a tax refund was property of the parent or the subsidiary was a matter of contract interpretation.
  - The court concluded, as in *BankUnited*, that the parties intended to create an agency relationship, not a debtor-creditor relationship, with regard to tax refunds, and that the refund was not property of HoldCo's bankruptcy estate.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Eleventh Circuit Opinion (cont.)**
  - The Eleventh Circuit noted the following key provisions of the TSA:
    - § 4(d)-(e) – Requiring HoldCo to pay refunds to the bank within 30 days of receipt.
    - § 9 – Granting authority to HoldCo to claim refunds for the group and, according to the court, providing that HoldCo acts as "agent" for its subsidiaries.
    - § 10(a) – Stating intent to allocate tax liability in accordance with the Interagency Statement and, according to the court, evincing an intent to comply with the Interagency Statement.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Eleventh Circuit Opinion (cont.)**
  - Primary basis for the decision:
    - Key provisions of the TSA were ambiguous as to whether they created an agency or debtor-creditor relationship.
    - Therefore, under Georgia law, it was necessary to determine the parties' intent in context.
    - Here, that context included the parties' expressed intent to comply with the Interagency Statement.
    - The Interagency Statement stated that HoldCo receives refunds from the taxing authority as agent for the group.

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Zucker v. Fed. Deposit Ins. Corp. (In re NetBank, Inc.), 729 F.3d 1344 (11th Cir. 2013)

- **Eleventh Circuit Opinion (cont.)**
  - Primary basis for the decision:
    - Further, section 10(a) of the TSA required no less favorable treatment to the group than if returns were filed separately. A debtor-creditor relationship would violate this provision.
    - Accordingly, and resolving ambiguity in the TSA by reference to the Interagency Statement, the parties intended to create an agency relationship.
    - The Eleventh Circuit conceded certain "contraindications within the four corners" of the TSA – namely, those identified by the bankruptcy court – but stated that these are merely what create ambiguity in the TSA.

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Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Background**
  - This case concerned allocation of tax refunds pursuant to a TSA between the bank and HoldCo.
  - The TSA provided for mechanisms by which the tax group, including the bank and HoldCo, would pay taxes, receive and distribute refunds and order tax-related affairs.
  - The bank failed and HoldCo filed for bankruptcy. Each requested refunds from IRS for the years 2007 and 2008.
  - The refunds were received by HoldCo and held in escrow pending resolution of dispute.

Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Bankruptcy Court Opinion**
  - The court granted summary judgment in favor of the Plan Administrator because the tax refunds were property of HoldCo's bankruptcy estate and thus the FDIC had only an unsecured, prepetition claim.
  - In so holding, the court rejected application of the federal common law rule stemming from the Ninth Circuit's *Bob Richards* opinion that the parent of a consolidated group receives a tax refund as trustee of a specific trust in the absence of an implied or express agreement to the contrary.

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Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Bankruptcy Court Opinion (cont.)**
  - The court also held, recognizing that tax allocation arrangements are permissible under Delaware law, that the TSA created a debtor-creditor relationship, not a trust or agency relationship.
    - Although the TSA clearly contemplated that HoldCo would deliver any tax refunds to the bank at some stage, nothing suggested that this was a requirement or that HoldCo held such funds in a trust capacity.
  - The court found no basis for finding that an implied trust existed.
  - The FDIC appealed.

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Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Eleventh Circuit Opinion**
  - The Eleventh Circuit ruled that the bankruptcy court erred.
  - The key determination was that the TSA did not create a debtor-creditor relationship between the bank and HoldCo.
  - Primary basis for decision:
    - Key provisions of the TSA were ambiguous.
    - Therefore, under Delaware law, it was necessary to determine the parties' intent.
    - A "common-sense" reading of the TSA and context was required to determine intent, rather than a close analysis (minimal citations to authority).

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Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Eleventh Circuit Opinion (cont.)**
  - Primary basis for the decision:
    - There were no indications from the TSA that a debtor-creditor relationship was intended.
    - The bankruptcy court's reading frustrated the bank's ability to discharge its obligations to members of the tax group.
    - Key language from opinion:
      - "Although the TSA does not contain a provision expressly requiring the Holding Company to forward the tax refunds to the Bank on receipt, it is obvious to us that this is what the parties intended. That is, they did not intend that the Holding Company keep the refunds and incorporate them into its own portfolio, as if the Bank had loaned the refunds to the Holding Company unencumbered." …

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Zucker v. Fed. Deposit Ins. Corp. (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir. 2013)

- **Eleventh Circuit Opinion (cont.)**
  - Primary basis for the decision:
    - Key language:
      - "When the Holding Company received the tax refunds, it held the funds intact — as if in escrow — for the benefit of the Bank and thus the remaining members of the Consolidated Group. The parties intended that the Holding Company would promptly forward the refunds to the Bank so that the Bank could, in turn, forward them on to the Group's members. In the Bank's hands, the tax refunds occupied the same status as they did in the Holding Company's hands — they were tax refunds for distribution in accordance with the TSA."

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Siegel v. FDIC (*In re IndyMac Bancorp Inc.*), 2012 WL 1951474 (C.D. Cal. May 30, 2012)

- **Background**
  - Similar facts to *BankUnited* and *NetBank*.
  - HoldCo and the bank were parties to an Amended and Restated TSA setting forth the rights and obligations of all members of the tax group, including the bank and HoldCo.
  - The TSA provided a mechanism by which the tax group, including HoldCo and the bank, would pay taxes, receive and distribute refunds and resolve tax-related issues.
  - The FDIC seized the bank and Holdco filed a Chapter 7 bankruptcy case.
  - The FDIC filed a proof of claim in the Chapter 7 case and asserted various claims, including claims for ownership of tax refunds.
  - Siegel, the Chapter 7 Trustee, filed a complaint objecting to the FDIC's claim and seeking declaratory relief that the bankruptcy estate was entitled to receive all tax refunds resulting from the consolidated tax returns for the years 2000-2008.

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Siegel v. FDIC (*In re IndyMac Bancorp Inc.*), 2012 WL 1951474 (C.D. Cal. May 30, 2012)

- **Bankruptcy Court Findings**
  - The bankruptcy court issued proposed findings of fact and conclusions of law that were adopted by the district court.
  - The court relied on decisions such as *BankUnited* in reaching its conclusions.
  - The court examined and interpreted the TSA to determine the type of relationship that existed between HoldCo and the bank relating to the tax refunds, *i.e.*, a creditor/debtor or trustee/beneficiary relationship.

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Siegel v. FDIC (*In re IndyMac Bancorp Inc.*), 2012 WL 1951474 (C.D. Cal. May 30, 2012)

- **Bankruptcy Court Findings (cont.):**
  - The court applied three key factors to determine the kind of relationship (debtor/creditor or trustee/beneficiary) that existed:
    - The use of terms such as "reimbursement" or "payment" in the TSA evidenced fungible payment obligations;
    - The TSA lack provisions requiring HoldCo to segregate or escrow the tax refund and did not restrict HoldCo's use of the tax refunds while in its possession; and
    - The TSA contained provisions that gave HoldCo discretion to prepare and file the tax refunds and elect whether or not to receive the refunds.
  - The court concluded the FDIC was only a general unsecured creditor and the Chapter 7 Trustee was entitled to possession of the tax refunds.
  - The FDIC appealed.

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In re Indymac Bancorp, Inc., 554 F. App'x 668 (9th Cir. 2014)

- **Ninth Circuit Opinion**
  - The Ninth Circuit affirmed the bankruptcy court.
  - Applying California law, the court found the TSA did not establish a principal-agent relationship because the bank did not exercise control over Holdco's activities under the TSA.
  - Under California law, the absence of trust language evidenced a debtor-creditor relationship.
  - The court distinguished *NetBank* as involving a TSA that explicitly incorporated the Interagency Statement and involving Georgia, not California law.

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F.D.I.C. v. AmFin Fin. Corp., 757 F.3d 530 (6th Cir. 2014)

- **District Court Opinion**
  - Similar facts: parent company AFC filed consolidated tax returns on behalf of its subsidiaries, including the bank.
  - The parties disputed whether, under the TSA, a $170 million NOL refund belonged to AFC's bankruptcy estate or the bank.
  - The district court held that the TSA allocated the refund to AFC, and the bank was merely a creditor of the estate.
    - The court relied largely upon the *Indymac* decision pursuant to which the TSA provided for "payment" or "reimbursement" to affiliate bank under certain conditions.

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F.D.I.C. v. AmFin Fin. Corp., 757 F.3d 530 (6th Cir. 2014)

- **Sixth Circuit Opinion**
  - The Sixth Circuit reversed and remanded to the district court.
  - The court found, contrary to the district court's view, that the TSA was ambiguous; terms such as "reimbursement" or "payment" did not show an unambiguous debtor-creditor relationship.
  - The court distinguished the TSA in *Indymac* as expressly stating circumstances under which the parent would disburse refunds, unlike the TSA here.
  - The court relied upon *BankUnited* in finding that the TSA language was silent on tax refunds, did not unambiguously show "ownership" and thus failed to demonstrate a debtor-creditor relationship.
  - The court remanded the matter to the district court to consider extrinsic evidence offered by the FDIC relating to the parties' intent with respect to the TSA under Ohio law.

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In re Imperial Capital Bancorp, Inc., 492 B.R. 25 (S.D. Cal. 2013)

- **Background**
  - Similar facts – HoldCo and the bank in receivership had entered into a Tax Allocation Agreement (the "TAA").
  - HoldCo commenced an adversary proceeding to determine the ownership of the refunds.

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In re Imperial Capital Bancorp, Inc., 492 B.R. 25 (S.D. Cal. 2013)

- **District Court Opinion**
  - On summary judgment, the court held that the TAA created a debtor-creditor relationship and the tax refunds were property of the estate.
  - The court found no presumptive agency relationship because the TAA fully defined the rights and obligations of the parties.

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In re Imperial Capital Bancorp, Inc., 492 B.R. 25 (S.D. Cal. 2013)

- **District Court Opinion (cont.)**
  - Citing *AmFin*, *IndyMac*, *BankUnited*, and *NetBank*, the court held that the TAA unambiguously created a debtor-creditor relationship by use of terms such as "pay" and "repayment," and the requirement that Imperial remit an amount calculated under TAA rather than holding refunds in trust.
  - Citing *IndyMac*, the court held that the Interagency Statement was not incorporated in the TAA, was non-binding, and in any event was not inconsistent with finding a debtor-creditor relationship.

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In re Vineyard Nat. Bancorp, 508 B.R. 437 (Bankr. C.D. Cal. 2014)

- **Bankruptcy Court Opinion**
  - Debtor HoldCo and the FDIC again disputed ownership of tax refunds under a TSA.
  - The court held that the TSA created debtor-creditor relationship:
    - Looking to the four corners of the TSA, it was not vague and clearly established the obligation of the parent to pay bank an amount set by the TSA – namely, the amount of the refund the bank would have received if it had filed its own tax returns, through a "true up."
    - No trust relationship and no *res* existed where the parent had an obligation regardless of whether it received a refund, and the TSA did not contain express trust language or require segregation of funds.
    - The TSA terms "receivable" and "payable" evidenced an intent to create an obligation to the bank as a form of reimbursement consistent with a debtor-creditor relationship.

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In re Vineyard Nat. Bancorp, 508 B.R. 437 (Bankr. C.D. Cal. 2014)

- **Bankruptcy Court Opinion (cont.)**
  - The court distinguished the 11th Circuit's decisions in *NetBank* and *BankUnited*.
    - In *NetBank*, the TSA used express trust language irrevocably appointing the parent as agent for the bank and stating an intent to allocate tax liability in accordance with the Interagency Statement, but the TSA was found ambiguous because it also included language consistent with a debtor-creditor relationship; here, the TSA was not ambiguous.
    - In *BankUnited*, the TSA required the bank to distribute tax refunds and collect tax liabilities on behalf of the consolidated group but was also found ambiguous; here, the parties had a "true up" every quarter to settle intercompany taxes and there was no inconsistent language restricting the use or commingling of funds showing a debtor-creditor relationship.
  - Like *IndyMac*, the TSA here referred to "intercompany tax receivable/ payable."

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In re Temecula Valley Bancorp, Inc., No. 5:14-cv-02244-CAS, 2014 WL 7150731 (C.D. Cal. Dec. 8, 2014).

- **District Court Opinion**
  - Similar facts: under the TSA, HoldCo was required to file consolidated tax returns on behalf of HoldCo and the bank.
  - The FDIC-Receiver filed a motion to withdraw the reference, arguing that the district court was required to apply federal banking statutes.
  - The court denied the motion because, among other things, *IndyMac* and other precedent clearly established the finding that a debtor-creditor relationship would not violate federal banking statutes.
    - This was a question of contract interpretation under state law and did not require application of the federal statutes argued by the FDIC.
  - The court istinguished *NetBank* as explicitly incorporating the Interagency Statement, unlike here.

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