Corporate Law
I. **In Re Landmark Land Co.: A Landmark Roadblock for Bankruptcy Courts v. Federal Regulators?**

In *Landmark Land Co. v. Resolution Trust Corp.* (In re Landmark Land Co.), the Fourth Circuit Court of Appeals held that the lower federal district court lacked subject-matter jurisdiction to enjoin the Resolution Trust Corporation ("RTC"), acting as conservator of a failed thrift, from exercising its ownership rights over the thrift's bankrupt subsidiaries. The decision essentially precludes any interference with the RTC's responsibility of resolving failed thrifts, including control over a failed thrift's principal assets (its bankrupt subsidiaries), and reveals the court's view on whether companies owned by thrifts may seek protection in bankruptcy not only from private creditors, but also from government regulators.

In *Landmark*, Oak Tree Savings Bank, S.S.B. ("Oak Tree") was the sole shareholder of Clock Tower Place Investments, Ltd., ("Clock Tower") which owned all of the stock in five Landmark Land companies. On October 11, 1991, Clock Tower and its asset-rich subsidiaries (collectively with Clock Tower, the "subsidiaries") filed petitions for relief under Chapter 11 of the Bankruptcy Code. On that same day the United States Bankruptcy Court for the District of South Carolina issued, *ex parte*, a temporary restraining order against Oak Tree prohibiting Oak Tree from exercising its right to call a shareholders' meeting to elect new members to the subsidiaries' boards of directors. Thus, the order prevented the Office of Thrift Supervision ("OTS") from managing the thrift's principal assets—the subsidiaries.

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1. 973 F.2d 283 (4th Cir. 1992).
2. The five subsidiary companies included: Landmark Land Co. of California, Inc.; Landmark Land Co. of Carolina, Inc.; Landmark Land Co. of Florida, Inc.; Landmark Land Co. of Louisiana, Inc.; and Landmark Land Co. of Oklahoma, Inc. *Id.* at 286 n.1. These subsidiaries developed, owned, and managed resort residential communities using the savings bank's lower cost funds to finance their real estate investments. Early in 1991, these subsidiaries held approximately $1 billion in real estate assets and millions more in "goodwill," once an accepted asset. Sherry R. Sontag, *Laws Are Colliding Over Litigation Involving Thrift*, Nat'l L.J., Dec. 16, 1991, at 15. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA") nearly eliminated the capital value of goodwill and required that savings and loans no longer tie up capital in real estate. *Id.* Forced to recapitalize, Oaktree suddenly found its financial solvency deteriorating, and attempts to sell the subsidiaries did not meet regulatory approval. Anticipating that regulators would seize the institution, Oaktree placed its asset-rich subsidiaries under the protection of the bankruptcy court. *Id.*
4. *In re Landmark Land Co.*, 973 F.2d at 287.
On October 13, 1991, the OTS appointed the RTC to act as receiver for Oak Tree pursuant to 12 U.S.C. § 1464(d)(2)(E). The RTC organized, and the OTS chartered, Oak Tree Federal Savings Bank ("Oak Tree Federal"). Pursuant to a purchase agreement, Oak Tree Federal purchased all of the RTC's interest in Oak Tree's assets, including the wholly-owned subsidiaries. After the OTS appointed the RTC as conservator for Oak Tree Federal, the RTC immediately asked the district court to lift the temporary restraining order to allow it to call a shareholders' meeting and exercise its ownership rights over the subsidiaries. Concluding that the receivership powers of the RTC do not divest a court of the power to protect the reorganization of corporate entities under the Bankruptcy Code, the district court denied the RTC's motion and converted the TRO into a preliminary injunction. The RTC appealed the preliminary injunction, and the Fourth Circuit reversed and remanded with instructions to dissolve the preliminary injunction.

The Fourth Circuit framed the issue as "whether the district court has jurisdiction to enjoin the RTC, acting as conservator of a failed thrift, from assuming control of the thrift's subsidiaries that are under Chapter 11 protection of the bankruptcy court." The court held that the district court lacked subject-matter jurisdiction to enjoin the RTC from exercising its ownership rights over Oak Tree Federal's wholly-owned subsidiaries.

The court opined that Congress established within the Financial Institution Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") a comprehensive statutory scheme granting the RTC broad powers to reorganize and collect assets for the benefit of depositors and taxpayers. The court stated

6. Landmark Land Co. v. Resolution Trust Corp. (In re Landmark Land Co.), 134 B.R. 557, 559 (Bankr. D.S.C. 1991), rev'd, 973 F.2d 283 (4th Cir. 1992). The district court anticipated that the RTC intended to eventually sell the subsidiaries' assets to the detriment of other creditors. Id. The RTC, as conservator for Oak Tree Federal, owed 91% of the debtors' consolidated debt. The district court believed it had jurisdiction to avert "abuse of shareholder rights and to prevent interference with the debtors' rights to reorganize." Id. at 559-60. Essentially the court believed that allowing the RTC to control the reorganization would adversely affect the interests of other creditors. Id. at 559. For instance, the court believed that retaining experienced management would best protect the interests of the subsidiaries' other creditors because irreparable injury would result if the court permitted the RTC to replace management. Id. at 560.
8. Id. at 287.
9. Id. at 290.
11. Upon its appointment as conservator or receiver, the RTC succeeds to "all rights, titles, powers, and privileges of the insured depository institution, . . . and the assets of the institution." 12 U.S.C. § 1821(d)(2)(A)(i) (Supp. IV 1992). The RTC's power to control an institution's assets includes, but is not limited to, the power to "conduct all business of the institution," "perform all functions of the institution . . . consistent with the appointment as conservator or receiver," and "preserve and conserve the assets and property of such institution." Id.
that "Congress made no provision for protecting some assets, such as subsidiary corporations, from being controlled and/or disposed of as the RTC deems necessary to maximize the return for depositors."12 The court concluded that FIRREA clearly empowered the RTC to take any action "necessary to put the insured depository institution in a sound and solvent condition."13

Proper resolution of this issue requires a careful reconciliation of Title 11 (the Bankruptcy Code) and Title 12 (the United States Code on Banks and Banking, as recently amended by FIRREA). Section 105 of Title 11 clearly states that a district court "may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."14 Therefore, it would appear that this section gives the district court the authority to protect the reorganization process through injunctive relief in the bankruptcy context.

Title 11 and Title 12 evidence two separate statutory schemes to govern insolvent corporate entities and financial institutions. The Bankruptcy Code reserves to the district courts the jurisdiction to administer the reorganization of corporations such as the bankrupt subsidiaries, yet excludes financial institutions.15 In contrast, Title 12, grants the RTC extensive authority to manage the liquidation of insolvent savings and loan associations such as Oak Tree.16 Further, the two statutory schemes serve different purposes. Chapter 11 allows the debtor the opportunity to reorganize its debt in order to continue to operate. In contrast, Title 12 focuses on the RTC’s responsibility not only to manage insolvent thrifts, but also to operate them in a manner that "maximizes the net present value return from the sale or other disposition of institutions . . . or the assets of such institutions."17

Congress made no express provision that Title 12 supersedes the district court’s jurisdiction over corporate debtors granted by Titles 11 and 28. Further, Title 12 does not grant the RTC authority to act as conservator or receiver for business corporations which, conceivably, include corporate debtor subsidiaries of insolvent financial institutions.18 FIRREA repeatedly refers to the “principal assets” of the failed institutions—language the RTC emphasized encompasses any wholly-owned subsidiary.19 Curiously, the Fourth Circuit did not distinguish these two schemes, but instead appears to

§ 1821(d)(2)(B).
15. Id. § 109(b).
17. Id. § 1441a(b)(3)(C)(i).
18. Brief of Appellees at 27.
have taken a policy-driven approach. The court seemed convinced that both the Congressional mandate and the national concern over the savings and loan crisis warranted its decision. 20

In *Landmark*, the Fourth Circuit declined to follow the reconciliation offered in *In re American Continental Corp.*, 21 concluding instead “the *American Continental* court interfered with legitimate statutory functions of the RTC.” 22 However, the factual similarities between *American Continental* and *Landmark* would appear to suggest a result different than that ultimately reached by the Fourth Circuit. 23 In *American Continental* the RTC, as conservator of a failed thrift, moved for dismissal of the subsidiaries’ bankruptcy cases because of “pervasive conflicts” between Title 11 and Title 12. 24 Initially, the *American Continental* court regarded two points as significant. First, it noted that the subsidiaries were not financial institutions, but rather were separate corporations eligible for protection under the Bankruptcy Code. Second, the court noted that RTC was the conservator for the failed thrift, but not for the subsidiaries. 25 The RTC was entitled to direct the operations of the subsidiaries solely as a result of the thrift’s status as a shareholder. The court considered it pivotal that FIRREA neither deprives a district court of jurisdiction over the RTC nor nullifies any provision of the Bankruptcy Code. The court further noted that “Congress could have specifically preempted application of Chapter 11 as to subsidiaries of depository institutions regulated by Title 12, but it did not do so.” 26 Finally, the court recognized that subsidiaries of financial institutions do not

22. *In re Landmark* Land Co., 973 F.2d at 289.
23. In *American Continental* eleven wholly-owned subsidiaries of Lincoln Savings and Loan Association (“Lincoln”) filed bankruptcy petitions under Chapter 11 on April 10, 1989. Four days later the Federal Home Loan Bank Board (“FHLBB”) placed Lincoln into conservatorship and appointed the Federal Savings and Loan Insurance Corporation (“FSLIC”) as conservator. Three days later, FSLIC voted its 100% stock ownership in each subsidiary to establish new boards of directors which in turn installed new management teams. Within a few months the RTC succeeded FSLIC as receiver of the failed thrift and as conservator of the new federally-chartered savings and loan association pursuant to FIRREA. *In re American Continental Corp.*, slip op. at 1-2.
24. Similar to its position in *Landmark*, the RTC argued that the bankruptcy proceedings would conflict irreconcilably with the statutory mandate of FIRREA that the RTC manage the business of the institution and preserve and conserve its assets and property. *Id.* slip op. at 2.
25. *Id.* slip op. at 3.
fall among the entities that 11 U.S.C. § 109 precludes from protection under the Bankruptcy Code. 27

The Arizona District Court rejected the RTC's argument that FIRREA authorized the RTC to take over the "assets" of failed thrifts. 28 The court believed any expansive construction of the term "assets" was strained in the absence of a Congressional intent. The court disfavored repealing by implication one of two conflicting statutes and believed that Congress must manifest a clear legislative intent to repeal a statute. Therefore, the court attempted to reconcile the two conflicting titles. 29 The court found that the RTC's basic functions as conservator or receiver went unaffected by Chapter 11 supervision of the subsidiaries. The court reasoned that the RTC does not act as the designated conservator of the subsidiaries, but instead merely exercises powers of a shareholder pursuant to state law. The court believed that Chapter 11 administration would ensure a more orderly resolution and provide a measure of protection for the interests of subsidiary debtor estates and their creditors—interests that the court believed FIRREA did not intend to disregard. Therefore, the court denied the motion to dismiss, holding that a district court could resolve conflicts between Title 11 and Title 12. The court acknowledged a possible future avenue for the RTC to pursue under 11 U.S.C. § 305(a)(1) if the "interests of creditors and the debtor would be better served by such dismissal." 30

The American Continental decision seemed favorable for the Landmark debtor subsidiaries. However, the Fourth Circuit did not clearly distinguish its decision from American Continental. Although Landmark seems to mirror American Continental, the issues, when framed narrowly, distinguish the two cases. In American Continental, the court solely addressed the issue of whether the "pervasive conflicts" between Title 11 and Title 12 required the district court to dismiss the bankruptcy proceedings. 31 The FSLIC had already voted the stock of the bankrupt subsidiaries, replaced the management, and taken control of the subsidiaries subsequent to the bankruptcy filing. The American Continental court suggested that a district court may dismiss bankruptcy proceedings when a fact-intensive analysis of statutory requirements warrant such action. 32 On the other hand, in Landmark the district court enjoined the RTC from assuming control of the subsidiaries, 33 and the issue of the propriety of a bankruptcy dismissal was not presented. However,

27. Id.
28. Id. slip op. at 5.
29. Id.
30. Id. slip op. at 6 (quoting 11 U.S.C. § 305 (a)(1)(1988)).
32. Id. slip op. at 5.
33. In re Landmark Land Co., 973 F.2d at 287.
the Fourth Circuit implied that if RTC moved to dismiss the bankruptcy proceedings, a court could properly grant such a motion, stating that: "The RTC is well within its statutory authority to take control of [a] subsidiary in which it holds a 100% ownership interest, without interference by the bankruptcy or district court."  

Unfortunately the Fourth Circuit did not consider a more in-depth analysis of this statutory conflict necessary. The opinion provides little guidance for analyzing similar parent/subsidiary arrangements. A fair question would be: Does the RTC, as a federal agency, effectively accomplish indirectly, as the 100 percent owner of the debtor subsidiaries, what it is prohibited from doing directly, as a creditor of the debtor subsidiaries? For example, assume a failed savings and loan association owns less than 100 percent of a bankrupt thrift corporation. *Landmark* suggests the same result, but its policy-based tone does not provide a strong argument.

The Fourth Circuit interpreted FIRREA's anti-injunction provision, 12 U.S.C. § 1821(j), as precluding any injunctive action when the RTC acts within the scope of its authority as receiver or conservator. The debtor subsidiaries maintained that this provision did not negate a district court's power to enjoin RTC interference with Chapter 11 reorganizations of thrift subsidiaries of a failed savings and loan administered by the RTC. The RTC contended that § 1821(j) deprives a district court of jurisdiction to enjoin the RTC from undertaking its express obligation to takeover, and operate a wholly-owned asset of the failed institution. Specifically, § 1821(j) states: "Except as provided in this section, no court may take any action, except at the request of the Board of Directors by regulation or order, to restrain or affect the exercise of powers or functions of the Corporation as a conservator or a receiver."  

In *Landmark*, the Fourth Circuit based its decision heavily on other courts' interpretation of § 1821(j) and similar anti-injunction provisions. These decisions support the proposition that Congress designed the specific anti-injunction provisions of other titles of the United States Code to protect the integrity of administrative actions until they are final and judicial review becomes available for aggrieved parties. As a result, the prevailing view is that these statutes supersede the general language of the Bankruptcy Code. Accordingly, the Fourth Circuit concluded that "[b]ecause the anti-injunction

34. *Id.* at 290.
35. *Id.*
36. See Brief of Appellees at 1.
37. See Brief of Appellant at 2.
40. See id.
provision specifically precludes equitable interference, the district court may not prevent the RTC from exercising its lawful ownership rights." The following discussion examines these interpretations and notes the potential roadblocks these provisions create for debtors.

In *Rosa v. Resolution Trust Corp.* the RTC, as conservator of a failed institution, determined that it would continue the institution's Minimum Retirement Benefit Plan in which the plaintiffs were beneficiaries. The plan was subject to the Employee Retirement Income Security Act of 1974 ("ERISA"). The institution, through the RTC, made two contribution payments to the trustee as they became due. Subsequently, the RTC considered terminating the plan. No party made any further contributions. The district court enjoined the RTC from taking any further action to terminate the plan or any adverse or prejudicial action. Further, the court ordered the RTC to pay all contributions on a timely basis as required by the plan.

The RTC contended that FIRREA's anti-injunction provision, 12 U.S.C. § 1821(j), prohibited the district court's injunction except as to the RTC in its corporate capacity. In other words, § 1821(j) prohibited interference with the RTC in its capacity as receiver or conservator. The Third Circuit noted that "to the extent of a conflict between [§ 1821(j)] and provisions of ERISA authorizing relief, § 1821(j) controls." The *Rosa* court addressed the issue of whether the terms of the preliminary injunction requiring payments to the plan would "restrain or affect the exercise" of those powers granted to the RTC in § 1821(d)(2). The court found that the timely contribution requirements impinged on the RTC's statutory powers "to 'preserve and conserve the assets and property of such institution.'" Finally, the court concluded that the injunction's nonmonetary provisions "encroached on the exercise of statutory power residing in RTC as receiver and conservator."

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41. *Id.* at 290.
44. *Rosa*, 938 F.2d at 388-90.
45. *Id.* at 397.
46. *Id.* at 398 (quoting 12 U.S.C. § 1821(j))
47. *Id.* (quoting 12 U.S.C. § 1821(d)(2)(B)(iv) (Supp. I 1989)). The court reasoned that the provisions clearly required distribution of the institution's assets which encroached on the RTC's power to preserve and dispose of the assets it controlled. Further, such liquidation would accord the plan's trustee and beneficiaries a preference over other creditors. *Id.*
48. *Id.* at 399. The court found that the institution's board of directors reserved the right to amend, suspend, or terminate the plan. *Id.* at 398-99. The court concluded that under 12 U.S.C. § 1821(d)(2)(A)(i), the RTC "succeeded to the termination rights contained in the original plan." *Id.* at 399. It emphasized that § 1821(j) serves to prevent a particular remedy in the interest of allowing the RTC, as receiver or conservator, promptly to carry out its mandate to resolve the thrift industry crisis. *Id.*
The Fifth Circuit reached a similar conclusion under its interpretation of § 1821(j) in 281-300 Joint Venture v. Onion.\textsuperscript{49} In Onion the plaintiff sought to enjoin the RTC, as conservator of a new federally-chartered institution, from conducting a foreclosure sale. The court concluded that courts lack the ability to enjoin nonjudicial foreclosures that fall within the RTC’s statutory powers as conservator or receiver.\textsuperscript{50}

The Fourth Circuit reached a similar result in an order entitled \textit{Automated Business Systems \& Services, Inc. v. FDIC}.\textsuperscript{51} Automated Business Systems and Services, Inc. sought a preliminary injunction to enjoin the Federal Insurance Deposit Corporation “‘from impounding or freezing the cash flows generated or being held by’ the FDIC.”\textsuperscript{52} The Fourth Circuit denied the motion on the ground that § 1821(j) expressly prohibited restraining the liquidation of assets.\textsuperscript{53}

In \textit{Telematics International, Inc. v. NEMLC Leasing Corp.},\textsuperscript{54} the First Circuit held that under § 1821(j) a federal court lacks jurisdiction to enjoin the FDIC, as receiver for a banking institution, “from attaching a certificate of deposit in which the banking institution holds a security interest.”\textsuperscript{55} The First Circuit stated that Congress enacted § 1821(j) to provide a broad limit on the power of courts to interfere with the FDIC’s efforts to preserve the assets of a failed financial institution quickly and without undue interruption.\textsuperscript{56} The court stated that “the elaborate structure created by FIRREA, and the evident intent of Congress that the structure should be permitted to stand with minimal court interference [require the conclusion] that section 1821(j) deprived the district court of jurisdiction to enter the injunction. . . . Such

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\item \textsuperscript{49} 938 F.2d 35 (5th Cir. 1991), \textit{cert. denied}, 112 S. Ct. 933 (1992).
\item \textsuperscript{50} \textit{Id.} at 39 (citing FSLIC v. Hall Whispertree Assocs., 653 F. Supp. 148, 150 (N.D. Tex. 1986)). The court reasoned that the ability of the RTC to foreclose on the debtor’s property existed under FIRREA. \textit{Id.} This rationale stemmed from the RTC’s “broad authority to dispose of assets and to ‘collect all obligations and money due the [failed] institution.’” \textit{Id.} (alteration in original) (quoting 12 U.S.C. § 1821(d)(2)(B)(ii) (Supp. I 1989)).
\item \textsuperscript{51} No. 90-1513 (4th Cir. Aug. 27, 1990).
\item \textsuperscript{52} \textit{Id.} slip op. at 1 (quoting appellant’s request).
\item \textsuperscript{53} \textit{Id.} slip op. at 2.
\item \textsuperscript{54} 967 F.2d 703 (1st Cir. 1992).
\item \textsuperscript{55} \textit{Id.} at 704. Lessor NEMLC Leasing Corp. assigned its assets, including the lease underlying the action, to the New Bank of New England (“NBNE”). Telematics International, Inc. (“Telematics”) and Digital Radio Networks (“Digital”) were the lessees. The FDIC was appointed as receiver for NBNE, and succeeded to NBNE’s rights under the lease. Telematics originally granted NEMLC a security interest in a certificate of deposit to secure Digital’s performance. Digital subsequently defaulted under the terms of the lease, and the FDIC sought to foreclose upon the pledged certificate of deposit. \textit{Id.}
\item \textsuperscript{56} \textit{Id.} at 705.
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judicial interference would dramatically limit the FDIC’s ability to exercise its statutory powers efficiently and effectively.\(^57\)

Additionally, courts conclude that anti-injunctive language found in other titles of the United States Code supersedes the general language of the Bankruptcy Code. For example, in *Board of Governors of the Federal Reserve System of the United States v. MCorp Financial, Inc.*,\(^58\) the Supreme Court held that the general provisions that govern bankruptcy proceedings do not supersede the specific preclusive language in 12 U.S.C. § 1818(i)(1).\(^59\) MCorp, a bank holding company, filed voluntary bankruptcy petitions and then initiated an adversary proceeding against the Board of Governors of the Federal Reserve System ("Board") to enjoin the prosecution of two administrative proceedings. The Supreme Court held that the district court lacked jurisdiction to enjoin either regulatory proceeding.\(^60\) Nevertheless, MCorp argued that either the automatic stay provision in the Bankruptcy Code\(^61\) or 28 U.S.C. § 1334(b)\(^62\) authorized the injunction.\(^63\) The Court rejected the argument that the automatic stay provisions apply to ongoing, nonfinal administrative proceedings.\(^64\) Further, the Court rejected the second argument that 28 U.S.C. § 1334(b) authorized a district court to exercise concurrent jurisdiction over certain bankruptcy-related civil proceedings.\(^65\) The Court found MCorp’s reliance on § 1334(b) to be misplaced in that an

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57. *Id.* at 705-06 (citations omitted).


59. *Id.* at 465. Section 1818(i)(1) provides: "[E]xcept as otherwise provided in this section . . . no court shall have jurisdiction to affect by injunction or otherwise the issuance or enforcement of any notice or order under any such section, or to review, modify, suspend, terminate, or set aside any such notice or order." 12 U.S.C. § 1818(i)(1) (Supp. IV 1992).

60. *MCorp Fin., Inc.*, 112 S. Ct. at 466.


62. 28 U.S.C. § 1334(b) (1988) authorizes district courts in bankruptcy proceedings to exercise concurrent jurisdiction over certain civil proceedings that would otherwise be subject to the exclusive jurisdiction of another court.

63. *MCorp Fin., Inc.*, 112 S. Ct. at 463.

64. *Id.* at 464. The Court stated that these proceedings enforced a "'governmental unit's police or regulatory power,'" and therefore, were expressly exempted by the automatic stay exception in § 362(b)(4). *Id.* (quoting 11 U.S.C. § 362(b)(4) (1988)). This section is qualified by the legislative statements that § 362(b)(4) is "to be given a narrow construction in order to permit governmental units to pursue actions to protect the public health and safety and not to apply to actions by a governmental unit to protect a pecuniary interest in property of the debtor or property of the estate." 11 U.S.C. § 362 legislative statements (1988).

The automatic stay may have met the same fate in *Landmark* had the Fourth Circuit addressed § 362(a)'s application. The *Landmark* court apparently took the position that the case did not specifically present the question of whether the RTC is subject to the automatic stay of Title 11, but rather Title 12 precludes a court from enjoining the RTC from exercising control over the bankrupt subsidiaries of a failed thrift. *See In re Landmark Land Co.*, 973 F.2d at 287.

administrative agency such as the board was not a "court" for purposes of that section.\textsuperscript{66} Realistically, MCorp resolved little of the conflicting issues in Landmark, but rather decided only one of many tangles emerging between the banking and bankruptcy laws.\textsuperscript{67}

Similarly, pursuant to 26 U.S.C. § 7421(a), the Fourth Circuit held that the bankruptcy court lacked authority to issue a preliminary injunction restraining the revocation by the IRS of a nonprofit organization's tax-exempt status.\textsuperscript{68} This provision, the Anti-Injunction Act, provides that "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed."\textsuperscript{69} In Clark the court stated: "There is no express provision in the Bankruptcy Code indicating congressional intent that the Code supersede the Anti-Injunction Act."\textsuperscript{70} In recognizing the clear mandate of the Anti-Injunction Act to prohibit such injunctions, the court continued: "Although revocation may potentially obstruct the orderly administration in bankruptcy, we decline to create an exception to the Act in the absence of express congressional intent."\textsuperscript{71}

In Carlton v. Firstcorp, Inc.\textsuperscript{72} the Fourth Circuit affirmed a district court's ruling that a provision of the Financial Institutions Supervisory Act of 1966 ("FISA")\textsuperscript{73} superseded the Bankruptcy Code's automatic stay.\textsuperscript{74}

\textsuperscript{66} Id. "[T]he prosecution of the Board proceedings, prior to the entry of a final order and prior to the commencement of any enforcement action, seems unlikely to impair the Bankruptcy Court's exclusive jurisdiction over the property of the estate . . . ." Id. The Court suggested that if the proceedings culminated in a final order, and judicial proceedings commenced to enforce the order, the Bankruptcy Court might properly exercise its concurrent jurisdiction under § 1334(b). \textit{See id.}

\textsuperscript{67} However, Landmark did not involve an administrative proceeding. It involved a district court's preliminary injunction preventing the RTC, as receiver, from voting stock owned by the failed thrift. Still, as apparent from the Fourth Circuit's decision, any precedent favoring regulators presents a danger to debtor entities. Prior to the Landmark decision, John L. Douglas of Atlanta's Alston & Bird, who represented Landmark against the RTC, commented: "MCorp is clearly a gorilla here because the courts have sided with the government, but it's not clear how big a gorilla it is." Sontag, \textit{supra} note 2, at 15. Apparently, MCorp was a larger gorilla than Mr. Douglas preferred in that the Landmark decision suggests that this pack of gorillas favoring regulators may continue to grow.

\textsuperscript{68} Clark v. United States (\textit{In re} Heritage Village Church & Missionary Fellowship, Inc.), 851 F.2d 104, 105 (4th Cir. 1988) (per curiam).

\textsuperscript{69} 26 U.S.C. § 7421(a) (1988).

\textsuperscript{70} Clark, 851 F.2d at 105 (citing LaSalle Rolling Mills, Inc. v. United States (\textit{In re} LaSalle Rolling Mills, Inc.), 832 F.2d 390, 394 (7th Cir. 1987)).

\textsuperscript{71} Id. at 106.

\textsuperscript{72} 67 F.2d 942 (4th Cir. 1992).

\textsuperscript{73} FISA is codified at 12 U.S.C. § 1818(i)(1) (Supp. IV 1992); \textit{see also supra} note 59 and accompanying text.

\textsuperscript{74} Carlton, 967 F.2d at 943. In Carlton the Office of Thrift Supervision, pursuant to its
Recognizing that the Supreme Court's decision in *MCorp* controlled a major part of Firstcorp's appeal, the Fourth Circuit ruled that § 1818(i)(1) precludes application of the automatic stay provision to an administrative proceeding. The court held that the Supreme Court's reasoning in *MCorp* applied equally to temporary cease and desist orders of regulatory agencies. Finally, the court concluded that § 1818(i)(1) is part of "a unified regulatory scheme which under *MCorp* is free from the intrusion of bankruptcy's automatic stay."

Post-Landmark decisions have relied on the Fourth Circuit's Landmark opinion to reach similar results in other contexts. In *Furgatch v. Resolution Trust Corp.* a district court cited Landmark for the proposition that "the only relevant question when applying [§] 1821(j) is whether the conservator or receiver is carrying out a statutory function or power." If so, the court may not issue an injunction. Accordingly, the court held that an RTC real estate foreclosure sale is within its statutory powers and consequently "[§] 1821(j)'s clear and unambiguous prescription prevent[ed the court] from enjoining the RTC in conducting a nonjudicial foreclosure sale." However, the Second Circuit distinguished Landmark, holding that § 1821(j) does not inhibit the operation of the automatic stay imposed by 11 U.S.C. § 362(a). The court reasoned that Congressional mandate, not court order, imposed the automatic stay which does not require court action to take effect. Injunctive relief is appropriate where that remedy is imposed by statute automatically and by operation of law without any action by a court. The weight of authority suggests that most circuits interpret anti-injunction provisions in favor of the federal regulatory agency which the particular authority under FISA, ordered Firstcorp, Inc., a savings and loan holding company, to decrease a Firstcorp-operated savings institution's insolvency and issued a temporary cease and desist order. Additionally, the OTS initiated an administrative proceeding designed to result in a final cease-and-desist order. Following this action, Firstcorp filed for protection under Chapter 11 and sought an order confirming that the automatic stay provisions of § 362 suspended the actions of the OTS. Subsequently, the OTS declared the savings institution insolvent, appointed the RTC as receiver, and chartered a new federal savings association that purchased the assets and assumed the liabilities of the insolvent thrift. *Id.* at 943-44.

75. *Id.* at 945-46.
76. *Id.*
77. *Id.* at 946. While the Carlton decision precludes applying the automatic stay to a temporary cease and desist order, a party may still apply for an injunction under § 1818(c)(2).
79. *Id.* at *2.
80. *Id.*
81. *Id.*
82. FDIC v. Hirsch (*In re Colonial Realty Co.*), 980 F.2d 125 (2d Cir. 1992).
83. *Id.* at 137 (citing Gross v. Bell Sav. Bank, 974 F.2d 403, 407 (3d Cir. 1992)).
84. *Id.* (citing 11 U.S.C. § 362(a) (1988)).
provision was designed to benefit. The rationale most often noted is Congress’s apparent intent to allow these regulatory agencies full rein to exercise their statutory authority without injunctive restraints. The general consensus is that a district court retains general jurisdiction over bankruptcy cases commenced by debtors and, generally, over the debtor’s estates. However, FIRREA limited a court’s power to act in particular matters. The “comprehensive statutory scheme” referred to in Landmark, while not divesting a court’s jurisdiction over the debtor’s assets, limits the court’s powers to act in certain proceedings that focus on the disposition of the assets. In other words, the court retains adequate jurisdiction under the Bankruptcy Code; however, Landmark suggests that the court must respect and honor other statutory mandates that limit the court’s bankruptcy powers.

Evidently, § 1821(j) does not create a complete roadblock to injunctive actions. For instance, the Code provides opportunities for injunctive relief where appropriate.\(^8\) Additionally, a few courts permit injunctions when the plaintiff alleges the regulatory agency acted beyond the scope of its statutory authority.\(^7\)

Still, some commentators express concern about the potential liberal effect from Landmark and other decisions that limit the RTC’s receivership powers in handling the affairs of a failed savings and loan when those powers conflict with the Bankruptcy Code’s provisions. For example, one commentator states: “The court of appeals is rapidly creating a monster called the RTC that is above litigation.”\(^8\) Patrick M. Duffy of the Charleston office of McNair & Sanford, P.A., who represented the Landmark debtor subsidiaries, characterized the decision as “a very broad opinion, and one that I expect the RTC to rely on very heavily in subsequent proceedings—which I do not think is a happy prospect for those outside of government.”\(^9\) Further, John L.


89. Donovan, supra note 88, at 21.
Douglas of Atlanta's Alston & Bird, lead counsel for the debtor subsidiaries, surmised that "[t]here is a real danger that, when all these decisions are added up, that this is an agency that is beyond judicial scrutiny or judicial review." The broad language of Landmark probably raises more questions than it answers. Given the large number of financial institution failures, the court will likely be forced to re-address the interplay of the FIRREA receivership provisions with the Bankruptcy Code in the future.

On balance the Landmark opinion illustrates a proper statutory interpretation, and its ruling should aid the government in resolving the monumental savings and loan crisis. One hopes, the RTC, in using this decision as a springboard for resolving the thrift crisis, will direct any adverse impact to those responsible for the thrift disaster and attempt to minimize any detrimental impact on innocent creditors and other contracting parties. In dealing with corporate subsidiaries, these third parties expect that commercial remedies available in the event of insolvency include recourse to Bankruptcy Code provisions. The Landmark decision arguably suggests that when the parent financial institution becomes insolvent as well, only the RTC retains the power to decide what rights and remedies are available to these third parties.

Richard F. Hewitt Jr.

II. COURT IMPLIEDLY EXPANDS A LENDER'S PERMISSIBLE INVOLVEMENT IN REAL ESTATE DEVELOPMENTS TO WHICH IT HAS LOANED MONEY

In Peoples Federal Savings & Loan Ass'n v. Myrtle Beach Golf & Yacht Club the South Carolina Court of Appeals held that a lender was not individually liable for the debt secured by a mortgage in a real estate development project that the lender initially financed. The court rejected several theories of lender liability, but did not significantly modify this area of law. However, the court's application of existing law may have impliedly expanded the degree that a lender may participate in the operation and management of a real estate development project to which it has loaned funds without incurring individual liability to the project's third party creditors.

The case involved an action for a mortgage foreclosure initiated by Peoples Federal Savings & Loan Association ("Peoples"). In 1984, Justice, Inc. ("Justice"), through its president, R. L. Propps, approached Peoples about financing the purchase and development of property in Myrtle Beach, South Carolina. The proposal involved the construction, lease, and sale of

90. Id. (alteration in original).

single and multi-family dwellings and an amenities tract featuring a golf course, club house, tennis courts, and swimming pool. In return for providing funding, Peoples would share in the profits from the development through a wholly owned subsidiary corporation.2

To accomplish this plan, Peoples incorporated a subsidiary, Peoples Joint Venture Group, Inc. (“Peoples Venture”), and Justice incorporated its own subsidiary, Myrtle Beach Golf and Yacht Club, Inc. (“MBGYC”). These two subsidiary corporations then formed a partnership known as Myrtle Beach Golf and Yacht Club (“the Partnership”) on February 28, 1984. Peoples Venture and MBGYC owned 25% and 75% of the Partnership, respectively. The partners agreed to share the project’s profits and losses in proportion to their ownership percentages. The partnership agreement stated that the Partnership would borrow money from “an affiliate of Peoples [Joint Venture].”3 Further, it provided that MBGYC would be the managing general partner, “but gave Peoples Venture veto authority over major management decisions.”4

From February 29 to September 20, 1984, Peoples loaned a total of $6,650,000 to the Partnership for acquisition, construction, and development costs. The Partnership acquired the property and commenced construction.5 In June 1985, a predecessor corporation to one of the appellants, American Community Development Group, Inc. (“ACDG”), proposed to buy Propps’s interest in the development. On August 9, 1985, Peoples sold all of its stock in Peoples Venture to Propps for $403,000, and accepted a promissory note and mortgage on the development for the amount of the stock purchase price. ACDG claimed that the parties based the purchase price on the estimated profits Peoples would have received if it had stayed in the project.6

On August 13, 1985, Loyola Federal Savings and Loan became the principal lender for the project by committing $13,000,000 to the Partnership for development of the housing tract. Peoples focused on developing the amenities tract. On October 9, 1985, Peoples loaned the Partnership $5,100,000 from which it refinanced the $3,000,000 amenities loan from 1984.7

To purchase Propps’s interest in the development, ACDG transferred $750,000 to MBGYC and $150,000 to Justice between September 30 and October 30, 1985. However, in January 1986, Propps and his partner disagreed about ACDG’s purchase of Propps’s interest in the Partnership, causing ACDG to cancel the purchase of the project. Subsequently, Justice,

2. Id. at ___, 425 S.E.2d at 767.
3. Id. at ___, 425 S.E.2d at 767 (alteration in original).
4. Id. at ___, 425 S.E.2d at 769-70.
5. Id. at ___, 425 S.E.2d at 768.
7. Id. at ___, 425 S.E.2d at 768-69.
MBGYC's parent corporation, signed a promissory note to repay ACDG the $750,000 it had advanced to MBGYC, and the Partnership also signed a promissory note to repay ACDG for its $150,000 advancement. Justice and the Partnership eventually defaulted on these notes.\(^8\)

In June 1986, Propps and Justice sold their interests in the Partnership to the Myrtle Beach Holding Corporation. ACDG then filed for involuntary bankruptcy.\(^9\) In March 1987, ACDG sued Propps, Justice, and the Partnership to recover on the two notes. A court-approved settlement required the Partnership to sign a new note and give ACDG a mortgage lien on all of the Partnership's property. However, the new note was subordinate to the mortgage lien that Peoples had on the property.\(^10\) In September 1988, Peoples commenced a foreclosure action against the Partnership, MBGYC, ACDG, and numerous other defendants. ACDG answered and counterclaimed that Peoples was liable for the Partnership's note secured by the mortgage on the development. The master in equity ruled that the mortgage held by Peoples had priority over ACDG's mortgage and ordered it foreclosed as a first lien. ACDG appealed,\(^11\) advancing several theories of lender liability all of which the court of appeals rejected.

First, the court of appeals applied the two-prong test of \textit{Sturkie v. Sifty}\(^12\) and refused to pierce Peoples Venture's corporate veil so as to make Peoples liable for Peoples Venture's debt to the Partnership. The first prong of the \textit{Sturkie} analysis includes an application of the eight factors listed in \textit{DeWitt Truck Brokers, Inc. v. W. Ray Flemming Fruit Co.}\(^13\) to determine if the dominant shareholders sufficiently observed corporate formalities.\(^14\) ACDG satisfied the first prong of \textit{Sturkie} by showing that Peoples Venture was undercapitalized, failed to observe corporate formalities, shared corporate offices and directors with Peoples, and was a front for the business of Peoples.\(^15\) However, \textit{DeWitt} also requires a showing of injustice or fundamental unfairness before the court will pierce the corporate veil.\(^16\) To

\begin{itemize}
  \item 8. \textit{Id.} at \underline{\hspace{1cm}}, 425 S.E.2d at 769.
  \item 9. \textit{Id.} at \underline{\hspace{1cm}}, 425 S.E.2d at 769.
  \item 10. \textit{Id.} at \underline{\hspace{1cm}}, 425 S.E.2d at 769.
  \item 11. \textit{Peoples Fed. Sav. & Loan Ass'n, ___ S.C.} at \underline{\hspace{1cm}}, 425 S.E.2d at 767.
  \item 12. 280 S.C. 453, 313 S.E.2d 316 (Ct. App. 1984).
  \item 13. 540 F.2d 681 (4th Cir. 1976). The eight \textit{DeWitt} factors are: (1) failure to provide adequate capital; (2) failure to observe corporate formalities; (3) nonpayment of dividends; (4) the insolvency of the debtor corporation; (5) siphoning of funds of the corporation by the dominant stockholder(s); (6) nonfunctioning of other officers or directors; (7) absence of corporate records; and (8) whether the corporation is merely a facade for the operations of the dominant stockholder(s). \textit{Id.} at 686-87.
  \item 15. \textit{Peoples Fed. Sav. & Loan Ass'n, ___ S.C.} at \underline{\hspace{1cm}}, 425 S.E.2d at 770.
  \item 16. \textit{DeWitt Truck Brokers, Inc.}, 540 F.2d at 687.
\end{itemize}
establish fundamental unfairness, the second prong of Sturkie requires the plaintiff to establish "(1) that the defendant was aware of the plaintiff’s claim against the corporation, and (2) thereafter, the defendant acted in a self-serving manner with regard to the property of the corporation and in disregard of the plaintiff’s claim in the property."17 However, the court of appeals concluded that ACDG had not established injustice or fundamental unfairness because Peoples was unaware of any claim by ACDG against the Partnership when Peoples sold its Peoples Venture stock to Propps.18

Although the court of appeals refused to pierce Peoples Venture’s corporate veil and hold Peoples liable as its sole shareholder, the court indicated that Peoples could be liable for Peoples Venture’s share of the Partnership debt under one or more of ACDG’s overlapping theories.19

The court of appeals stated that Peoples could be held liable under the participation/involvement theory of Kennedy v. Columbia Lumber & Manufacturing Co.20 and Roundtree Villas Ass’n v. 4701 Kings Corp.21 if, as a lender, Peoples “was an active participant . . . in the construction, management, and marketing of the development.”22 However, the court noted that under Roundtree a lender will not be liable for construction defects occurring prior to the lender’s involvement in the construction, repair, and management of the project.23 The court of appeals inferred from Roundtree that “a lender also will not be held liable for defects or injury occurring after it in good faith removes itself from the project, unless the defects or injury may be traced to its prior involvement.”24

To support another theory of liability based on the participation/involvement of Peoples, ACDG identified the following activity by Peoples with the Partnership after the August 9, 1985 stock sale: Peoples advanced money to the Partnership after the project’s construction stopped and guaranteed payments and issued checks directly to subcontractors, undercapitalized the Partnership, retained an interest in the profits from the development, and communicated with the homeowners association regarding homeowner concerns. Further, Peoples advanced money to the Partnership’s

19. Id. at ___, 425 S.E.2d at 769-75. ACDG asserted five theories to hold Peoples liable for Peoples Venture’s partnership debt: (1) participation/involvement liability, (2) principal/agent liability, (3) joint venture liability, (4) instrumentality or alter ego liability, and (5) the doctrine of equitable subordination. Id.
23. Id. at ___, 425 S.E.2d at 770; see also Roundtree Villas Ass’n, 282 S.C. at 423, 321 S.E.2d at 50-51.
payroll, participated in efforts to sell the project, and sent letters to government agencies requesting approval of the project.\textsuperscript{25} ACDG’s experts testified that Peoples’ involvement in the project constituted abnormal commercial practices for a lender.\textsuperscript{26}

In spite of this involvement, the court of appeals rejected this theory of liability by holding that Peoples’ involvement with the project fell below the level required for liability under \textit{Roundtree}.\textsuperscript{27} The court stated that such involvement was not “unusual under the circumstances” because Peoples wanted the project to succeed and had abandoned the project only after it determined that the project’s necessary capital would overwhelm its funding capabilities.\textsuperscript{28} Accordingly, the court of appeals held that Peoples effectively removed itself from the project by selling the stock of its subsidiary and was therefore not liable for the debt incurred by the Partnership after the sale.\textsuperscript{29}

The court of appeals also refused to hold Peoples individually liable for the Partnership debt under the principal/agent theory of liability. Under this theory, a lender becomes liable for the obligations of a business if it takes \textit{de facto} control over the business either in person or through an agent.\textsuperscript{30} Reiterating Peoples’ involvement in the project, ACDG argued that Peoples had total control of the Partnership both before and after the August 9th sale. The court of appeals noted that ACDG failed to offer evidence that Peoples made any construction or development recommendations to the Partnership after the sale and that Peoples acted primarily to protect its collateral in the project. Consequently, the court held that Peoples’ actions taken after August 9, 1985 did not demonstrate the \textit{de facto} control over the Partnership necessary to impose individual liability on Peoples as a lender.\textsuperscript{31}

The court of appeals also summarily rejected ACDG’s attempt to impose liability on Peoples under a joint venture liability theory. Joint venture liability arises when two or more persons united in a common enterprise possess equal authority, express or implied, to act for all in the control and execution of the enterprise and to direct the conduct of each other with respect to the enterprise.\textsuperscript{32} ACDG cited \textit{Central Bank, N.A. v. Baldwin},\textsuperscript{33} a Nevada

\begin{itemize}
\item 25. Id. at __, 425 S.E.2d at 770-71.
\item 26. Id. at __, 425 S.E.2d at 770-71.
\item 27. Id. at __, 425 S.E.2d at 772-73.
\item 28. Id. at __, 425 S.E.2d at 772.
\item 29. People's Fed. Sav. & Loan Ass'n, ___ S.C. at ___, 425 S.E.2d at 772-73.
\item 30. Id. at __, 425 S.E.2d at 773 (citing RESTATEMENT (SECOND) OF AGENCY § 14(O) cmt. a (1958)).
\item 31. Id. at __, 425 S.E.2d at 773-74 (citing A. Gay Jenson Farms Co. v. Cargill, Inc., 309 N.W.2d 285 (Minn. 1981)).
\item 32. Id. at __, 425 S.E.2d at 774 (citing Spradley v. Houser, 247 S.C. 208, 146 S.E.2d 621 (1966) and Long v. Carolina Baking Co., 190 S.C. 367, 3 S.E.2d 46 (1939)).
\item 33. 583 P.2d 1087 (Nev. 1978).
\end{itemize}
case, which held a lender liable as a joint venturer in a construction project. In *Baldwin* the lender loaned money for the project, approached the building contractor to "joint venture" the construction project, and owned half of the construction company's stock through its wholly owned subsidiary.\(^{34}\) Based on much of its previous analysis of other liability theories, the court of appeals concluded that the joint venture theory was also inapplicable to Peoples.\(^{35}\)

ACDG also sought to hold Peoples liable under the instrumentality or alter ego theory in which liability results when the lender controls the business decisions and actions of its borrower such that the borrower, in effect, becomes the lender's instrument or alter ego.\(^{36}\) Further, under this theory, the lender must achieve "total domination" over the borrower so that the borrower exists solely to effectuate the lender's purpose, and then the lender must misuse that control.\(^{37}\) The court of appeals rejected this theory because it found that Peoples neither exercised the requisite total control over the Partnership after August 9, 1985, nor misused its influence to benefit itself.\(^ {38}\)

A final liability theory that ACDG argued was that Peoples should be individually liable for the Partnership's debt under the doctrine of equitable subordination.\(^ {39}\) Bankruptcy courts use this doctrine to subordinate a shareholder's claim as creditor of a bankrupt corporation to the claims of outside creditors when the shareholder's claim is actually an equitable investment rather than a bona fide debt.\(^ {40}\) After discussing the grounds for applying the doctrine as articulated in *Pepper v. Litton*\(^ {41}\) and in *Machinery Rental Inc. v. Herpel (In re Multiponics, Inc.)*,\(^ {42}\) the court stated that "[t]he linchpin in the decisions applying the doctrine of equitable subordination is the conviction that insider misconduct caused injury to the creditors of a bankrupt corporation."\(^ {43}\) The court of appeals held the doctrine of equitable subordination inapplicable because the evidence failed to show that Peoples was an

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34. *Id.* at 1089.
36. *Id.* at ___, 425 S.E.2d at 774 (citing 10 S.C. JUR. *Banks and Banking* § 170 (1992)).
37. *Id.* at ___, 425 S.E.2d at 774 (citing *Krivo Indus. Supply Co. v. Nat'l Distillers & Chem. Corp.*, 483 F.2d 1098 (5th Cir. 1973)).
38. *Id.* at ___, 425 S.E.2d at 774.
39. *Id.* at ___, 425 S.E.2d at 774-75.
41. 308 U.S. 295 (1939).
42. 622 F.2d 709 (5th Cir. 1980).
insider after the stock sale or that it at any time engaged in inequitable conduct that injured ACDG or any other creditors.44

Equity also defeated any of ACDG’s claim of priority over Peoples’ mortgage because ACDG’s mortgage emanated solely from the investment of funds to purchase Propps’s partnership interest, while Peoples’ mortgage arose from its loans to the Partnership used for development of the project. The court noted that the express language of ACDG’s mortgage (subordinating itself to Peoples’ mortgage) estopped ACDG from asserting priority.45

In summary, the court of appeals concluded that Peoples was not involved in a joint venture with the Partnership after the August 9, 1985 stock sale, that Peoples did not control the finances or management of the Partnership after that date, and that “[t]he actions of Peoples were either in keeping with usual lender practices or were done with the consent of the Partnership or the court and with the intent of protecting its collateral and ensuring the viability of the project.”46

The court of appeals decision in this case, holding that Peoples’ mortgage was superior to ACDG’s mortgage, was indeed appropriate considering the following: (1) the express terms of ACDG’s mortgage subordinating it to Peoples’ mortgage; (2) the financing arrangements upon which the respective mortgages arose; and (3) ACDG’s knowledge of the stock sale prior to both its investment and acceptance of the Partnership’s note and mortgage. However, the court of appeals’ application of existing law raises two potential concerns.

First, as discussed above,47 the first prong of the Sturkie v. Sifly48 veil-piercing test includes an examination of the eight factors listed in DeWitt Truck Brokers, Inc. v. W. Ray Flemming Fruit Co.49 to determine if the dominant shareholder sufficiently observed the corporate formalities. The second prong of the test requires the plaintiff to show some element of injustice or fundamental unfairness before the court will attribute the acts of the corporation to the dominant shareholder.50

Stringent application of the second prong of the Sturkie test could apparently produce inequitable results. For example, consider a situation in which a group of corporate officers ignore corporate formalities, totally dominate and control the corporation for their personal advantage, act in a self-serving manner, and as a result place the corporation in imminent financial

44. Id. at ___, 425 S.E.2d at 775-76.
45. Id. at ___, 425 S.E.2d at 776.
46. Id. at ___, 425 S.E.2d at 776.
47. See supra text accompanying notes 12-17.
49. 540 F.2d 681 (4th Cir. 1976); see supra note 13 for a list of the eight factors.
50. Sturkie, 280 S.C. at 459, 313 S.E.2d at 319; see supra text accompanying notes 17-18.
failure. Suppose further that an unwary or unsophisticated creditor or investor loans to or invests money in the corporation, and the corporation subsequently fails because of the corporate officers' previous improprieties. Under the second prong of *Sturkie*, the officers could escape liability to the creditor or investor unless they acted in a self-serving manner after the creditor or investor committed funds to the corporation, regardless of their previous culpability. However, in *DeWitt* the Fourth Circuit stated:

"[T]his concept of separate entity is merely a legal theory, "introduced for purposes of convenience and to subserve the ends of justice," and the courts "decline to recognize [it] whenever recognition of the corporate form would extend the principle of incorporation "beyond its legitimate purposes and [would] produce injustices or inequitable consequences."" Accordingly, "in an appropriate case and in furtherance of the ends of justice," the corporate veil will be pierced and the corporation and its stockholders "will be treated as identical.""51

Although courts are hesitant to disregard the corporate entity,52 strict application of the second prong of the *Sturkie* test may lead to inequitable results in certain cases, and thus undermine the policy articulated in *Dewitt* for piercing the corporate veil.

A second important concern raised by *Peoples Federal* is that the decision impliedly allows a lender to actively participate in the operation and management of a real estate development project without incurring individual liability to the project's third party creditors. However, the South Carolina Supreme Court stated in *Kennedy v. Columbia Lumber & Manufacturing Co.*53 that sound policy considerations underlie the reluctance to extend liability to lenders in construction cases. It stated:

The public policy reasons for refusing to impose warranty liability on a mere lender are myriad. To require every lender to foreclose in order to shield itself from liability instead of taking a deed in lieu would be unduly burdensome on the state's judicial and administrative machinery. The imposition of warranty liability on all lenders/sellers would discourage lending, and thus, economic growth. Further, it is unduly punitive to impose potential warranty liability on a lender that is searching for some way to recover the losses it has suffered due to the default of the debtor.54

51. *DeWitt Truck Brokers, Inc.*, 540 F.2d at 683 (citations omitted).
52. See id.; *Sturkie*, 280 S.C. at 459, 313 S.E.2d at 319.
54. Id. at 340, 384 S.E.2d at 734.
Similarly, in Roundtree Villas Ass'n v. 4701 Kings Corp. the South Carolina Supreme Court stated that “[b]oth the lender and the borrower have a common interest in seeing that the construction company builds a building free of defects but absent a contract the builder has no common law duty to protect the lender and the lender has no common law [duty] to protect the builder.”

However, in Kennedy the court also stated that a lender may be held liable when: (1) the lender is also a developer; (2) “when the lender becomes highly involved with construction in a manner that is not normal commercial practice for a lender”; (3) when the lender is “so amalgamated with the developer or builder so as to blur its legal distinction”; and (4) when the lender “forecloses on a developer in the midst of construction, takes title, has substantial involvement in completing the construction and sells homes.” Likewise, in Roundtree the South Carolina Supreme Court imposed liability on a lender for construction defects “when the Lender, in effect, took over the project and undertook to market the units through a corporation it had created and when it undertook to repair defects which existed to promote sales.”

In Peoples Federal the court of appeals held that the involvement of Peoples in the affairs of the project, after it had sold the stock on August 9, 1985, failed to reach the level of involvement required for liability under Roundtree. The facts indicate that Peoples remained active in the project nonetheless. Dissenting, Judge Gardner noted that Peoples: (1) disbursed large sums of money to itself; (2) paid itself for various sales of property belonging to the project; (3) paid $150,000 on a debt of Propps for his corporations; (4) advanced money to the Partnership after construction on the project stopped in 1986; (5) communicated with the homeowners association regarding homeowner concerns about the project; (6) wrote letters to state and federal officials concerning road construction and paving in the project and seeking FHA guarantees of loans; (7) made large advances to Justice (a parent corporation of MBGYC); (8) actively participated in attempting to sell the project in 1987; (9) throughout 1987, guaranteed payment to subcontractors employed by the Partnership, and directly paid approximately $1,000,000 to subcontractors for the Partnership's debts; (10) solicited and received bids to perform road work, patching, and road extensions on the project through November 1988; (11) in August 1988, obtained permission from the bankruptcy court to operate the golf course; (12) in December 1988, formed

56. Id. at 422, 321 S.E.2d at 50 (citing Butts v. Atlanta Fed. Sav. & Loan Ass'n, 262 S.E.2d 230 (Ga. Ct. App. 1979)).
58. Roundtree Villas Ass'n, 282 S.C. at 423, 321 S.E.2d at 51 (citing RESTATEMENT (SECOND) OF TORTS § 323 (1965)).
a corporation to control and manage the golf course and obtained a liquor license for the club; and (13) received income, entered into service contracts, employed personnel, and actively participated in the maintenance and operation of the golf club until an employee of Peoples was appointed by the bankruptcy court as receiver for the project in February 1989.  

The majority opinion dismissed many of these involvements as unpersuasive because they "occurred pursuant to [a bankruptcy] court order or after default and under the default provisions of the mortgage in foreclosure." However, Peoples' total involvement in the project both before and after the August 9, 1985 stock sale seems to reach the level necessary to subject Peoples to lender liability under the Kennedy and Roundtree tests. In a detailed analysis, Justice Gardner's dissenting opinion in Peoples concludes that ACDG established by a preponderance of the evidence that Peoples engaged in a joint venture with the Partnership and enjoyed control of the project after August 9, 1985.

The South Carolina Court of Appeals in Peoples Federal properly concluded that the lender was not individually liable for debt secured by a mortgage lien on a real estate development project that the lender initially financed. The court's application of the existing law, however, may have impliedly expanded the degree to which a lender may participate in the operation and management of such a project without subjecting itself to individual liability.

David J. Parrish

60. Id. at __, 425 S.E.2d at 781-82 (Gardner, J., dissenting).
61. Id. at __, 425 S.E.2d at 771.
62. Id. at __, 425 S.E.2d at 784 (Gardner, J., dissenting).