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Preserving N.Y. Property Law And Dividing A District

Law360, New York (February 08, 2012, 1:01 PM ET) -- A recent decision in the Southern District of New York holds that blocked proceeds of electronic fund transfers (EFTs) held by banks are not subject to attachment in satisfaction of judgments on claims premised on acts of terrorism. This decision creates a split of authority within the Southern District.

In Calderon-Cardona, et al. v. JPMorgan Chase Bank NA (11 Civ. 3283), Judge Denise Cote determined that the Terrorism Risk Insurance Act (TRIA) does not preempt state property law, which determines whether an EFT is actually owned by the terrorist-party/judgment-debtor.

Under New York law, neither an originator nor a beneficiary owns a midstream EFT. Thus, pursuant to this decision, judgment creditors of those parties cannot execute on blocked EFTs under TRIA.

In this case, the petitioners — families and victims of a terrorist attack for which the North Korean government had been found liable — sought to execute on accounts at nine banks that held the proceeds of EFTs that had been blocked pursuant to sanctions against North Korea.

The petitioners relied on Section 201 of TRIA, which provides, in relevant part, that:

> "in every case in which a person has obtained a judgment against a terrorist party on a claim based upon an act of terrorism … the blocked assets of that terrorist party … shall be subject to the execution or attachment in aid of execution in order to satisfy such judgment[.]"

In addition to finding that North Korea was no longer a terrorist party, the court held that the petitioners could not attach the blocked EFTs because the accounts did not consist of "blocked assets of [North Korea]."

Applying a recent U.S. Supreme Court decision that "the use of the word 'of' denotes ownership" (Bd. of Trustees of the Leland Stanford Junior Univ. v. Roche Molecular Sys. Inc., 131 S.Ct. 2188, 2196 (2011)), the court reasoned that the EFTs are not subject to execution unless they are owned by North Korea under New York property law.

The court's decision to apply New York law to assess North Korea's ownership of the blocked EFTs diverged from two other recent decisions of the Southern District: Hausler v. JP Morgan Chase Bank, 740 F.Supp.2d 525 (S.D.N.Y. 2010), and Levin v. Bank of New York, 09 Civ. 5900 (S.D.N.Y. March 4, 2011).[1]

In those decisions, Judges Victor Marrero and Robert Patterson reasoned that the statutory provision that "blocked assets … shall be subject to the execution or attachment" overrode state law governing the ownership of those assets. They relied on the definition of "blocked assets" in U.S. Department of the Treasury regulations, which require blocking assets with relationships to terrorist parties that fall short of ownership.

The court in Calderon-Cardona, however, concluded that incorporating the regulatory definition into TRIA would lead to absurd results, permitting attachment of interests with "only the most tangential relationship to North Korea."

Moreover, while the regulations defined "property" and "property interest" to designating the types of property and interests which could be blocked, the regulations did not define property ownership, and this provided "ample room" for state law to supplement federal law.

The court also cited a statement of interest filed by the United States in another case concerning a similar regulation: "the mere fact that assets have been blocked pursuant to the [sanctions regime] … does not show that the assets at issue are owned by the [defendant government.]"

Having concluded that federal law did not preempt state property law, the court then applied New York law — specifically, the rule that the interest of an originator or a beneficiary in a midstream EFT falls short of ownership — and held that the blocked EFTs were not subject to attachment pursuant to TRIA.

Large money-center banks, especially those with international operations, are experiencing a wave of enforcement litigation brought by judgment creditors of various nations and organizations that have been designated terrorist parties, such as Cuba, Sudan and Iran.

The reasoning in Calderon-Cardona, if adopted by other courts, may have the effect of limiting the number of assets that are potentially subject to enforcement. It remains to be seen whether courts will follow Judge Cote.

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[1] Mayer Brown represents one of the defendant banks in Levin.