Court Denies Foreclosure to Bank for Breach of Fiduciary Duties

The Wisconsin Court of Appeals has affirmed a trial court's decision denying a foreclosure judgment to a bank because its loan officer breached his fiduciary duty to the borrower. There was no dispute that the borrower had a valid note and mortgage with the bank, had not made scheduled payments on the note, and was liable to the bank on the note and other loans. Nevertheless, **the court determined that "equity" would not permit the bank to benefit from the wrongful actions of its loan officer**. Although the mortgage would remain a lien on the property, the bank was prohibited from enforcing its mortgage through foreclosure.

Todd and Carolyn Bork had a long-standing and close relationship with their loan officer, David Larson. They owned and operated a tree farm in Minnesota. They also owned property in Wisconsin. While an employee of MidCountry Bank, Larson put together a refinancing transaction that tied together the Borks' business and personal debt and that was secured in part by a mortgage on the Borks' Wisconsin property.

When the Borks missed loan payments, they preemptively initiated a lawsuit against MidCountry and Larson in Minnesota, alleging breach of fiduciary duty, fraud, and promissory estoppel. They claimed that Larson took advantage of them by "inducing" them to buy the Wisconsin property and by **improperly structuring and securing their loans**. In response, MidCountry counterclaimed in the Minnesota action and also brought a separate action in Wisconsin to foreclose the Wisconsin property. The Borks asserted the affirmative defense of "unclean hands" and brought a counterclaim for breach of fiduciary duty in the Wisconsin action.

The Wisconsin court granted summary judgment to MidCountry on the issue of default but declined to enter a judgment of foreclosure pending the outcome of the Minnesota case. The Borks ultimately prevailed on their breach of fiduciary duty claim in the Minnesota action and were awarded $636,000 in damages. MidCountry also prevailed in the Minnesota action and was awarded over $4 million on the outstanding loans.

MidCountry again moved for summary judgment in the Wisconsin action, requesting entry of a foreclosure judgment. It contended that the Borks were made whole for MidCountry's and Larson's breach of fiduciary duty by the $636,000 damage award in Minnesota. The Borks filed their own summary judgment motion, arguing that the Wisconsin court must recognize that Larson breached his fiduciary duty when the court was "balancing the equities" in the foreclosure action.

The trial court sided with the Borks and found that it "would be inequitable to allow MidCountry to foreclose on the Borks' Wisconsin property given its breach of fiduciary duty." The Wisconsin Court of Appeals agreed with the trial court's holding. The appellate court pointed out that the Borks still owed the amount outstanding on the note, that any unpaid amount would continue to accrue interest under the note's terms, and that MidCountry retained a security interest in the Wisconsin property. However, MidCountry could not enforce its security interest through foreclosure.

The *MidCountry Bank v. Bork* case illustrates two important points. First, loan officers are in the business of building relationships with borrowers. It is important that the relationship does not become so close that the loan officer has heightened fiduciary responsibilities to the borrower. Likewise, it is important that loan officers do not take unfair advantage of that relationship. The Court of Appeals' decision does not explain how Larson became the Borks' fiduciary or exactly what he did to abuse that position; but, a Minnesota jury decided to assess significant damages against the bank for Larson's actions.

The second take-away from the *MidCountry Bank v. Bork* case is the reminder that **"[f]oreclosure proceedings are equitable in nature, and the circuit court has the equitable authority to exercise discretion throughout the proceedings," even after confirmation.** If a trial court's sensibilities are offended by the actions of the bank or its employees or if the outcome sought by the bank seems unjust (even if the bank is acting within its rights), the court has a great degree of flexibility to craft appropriate remedies. In this case, the rather dramatic result was that the court deprived the bank of its right to foreclose.