The Consumer Finance Podcast — Deposit Account Litigation: Highlights From 2024 and What to Expect in 2025
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Chris Willis:

Welcome to *The Consumer Finance Podcast*. I'm Chris Willis, the co-leader of the Troutman Pepper Locke's Consumer Financial Services Regulatory Practice. Today's episode is another in our series about the Year in Review and A Look Ahead to accompany our Year in Review and Look Ahead publication, which you can find in the Consumer Financial Services page of troutman.com.

But before we jump into that topic, let me remind you to visit and subscribe to our blogs, TroutmanFinancialServices.com and ConsumerFinancialServicesLawMonitor.com. And don't forget to check out our other podcasts. The *FCRA Focus*, all about credit reporting. *The Crypto Exchange*, about everything crypto. *Unauthorized Access*, which is our privacy and data security podcast. *Payments Pros*, all about the payments industry. And *Moving the Metal*, which is our auto finance industry. All of those are available on all popular podcast platforms. Speaking of those platforms, if you like this podcast, let us know. Leave us a review on your podcast platform of choice and let us know how we're doing.

Now, as I said today, we're going to be doing another of our series of the Year in Review and Look Ahead. This time, we're going to be talking about something that really is very important to our depository institution clients, and that is deposit account-related litigation, which seems to be an ongoing theme that our bank and credit union clients have to deal with.

Joining me to talk about that are the two authors of that section of our Year in Review and Look Ahead publication, Mary Zinsner and Heryka Knoespel. Mary, Heryka, thanks for being on the show with me today.

Mary Zinsner:

Thanks, Chris. Glad to be here.

Heryka Knoespel:

Thanks, Chris. Excited to be here with you.

Chris Willis:

We're talking about essentially deposit account litigation, and let's just jump right into it with you, Mary, if you don't mind. Just give the audience first a little bit of an overview of what kind of

litigation are we talking about, and then, maybe talk about some of the trends that you saw in 2024 in this important area of litigation.

Mary Zinsner:

Thanks, Chris. I'm glad to do that. Deposit litigation is just a range of litigation that depository banks see that arise out of their daily operations. We see everything. We see elder fraud cases, we see check cases, we see Ponzi scheme cases. Just every type of imaginable claim that could be brought against a bank, merely because the fact that banks book commercial and individual deposit customers.

2024 was a really busy year for deposit litigation. One of the bigger trends we saw in terms of dollar value was really kind of an upsurge in Ponzi scheme type cases brought against banks. While Ponzi scheme cases are not new, we're starting to see some novel twists with respect to the allegations and the attempts to hold the banks responsible for the conduct of the bad actors who orchestrated the schemes. Plaintiffs really have always tried to loop the banks in. They see the banks and the financial institutions as the deep pocket from whom they can extract and sometimes extort a settlement. The typical claims we see are civil conspiracy, aiding and abetting fraud, aiding and abetting breach of fiduciary duty, et cetera.

The plaintiffs assert that the bank's servicing or banking the bad actors were complicit and knowingly participated in the scheme, even though they really have little evidence of either an agreement between the bank and the bad actors to the fraud, or any cognizable or discernible act of a knowing participation in the fraud. But what we're seeing is a new trend, and that's to couple the aiding and abetting claims with assertions that the banks were obligated under know-your-customer obligations and bank secrecy act laws to detect and deter the fraud. The red flag should have triggered warning, et cetera.

As bank regulators get more and more vocal about AML and BSA compliance in the part of the institutions they oversee, class action plaintiffs are listening, and looking at these statutes, and attempting to craft claims to put some more meat on the bones of their claims. So, what we see is, plaintiffs asserting that the banks were aware of the alleged Bank Secrecy Act red flags and should have taken additional action to protect the investors or the persons defrauded. But as we all well know, the Bank Secrecy Act, Anti-Money Laundering laws, and know-your-customer obligations do not confer private rights of action and we regularly move to dismiss these claims. We really kind of take a front at the effort to masquerade ordinary tort claims where what plaintiffs are really trying to assert is a BSA type claim masquerading as a common law tort claim, which they lack standing to assert.

Chris Willis:

Yes, unless they've suddenly become FinCEN all of a sudden. That make sense to me, Mary. I mean, that was actually the first thing I thought of when you started saying like, sort of a negligence per se based on a BSA violation. So, you've talked about the plaintiff's tactic and our response, so how are those claims ending up getting resolved when they're being litigated?

Mary Zinsner:

Yes. We saw some good victories for banks this year, and we're having some success for our clients in these cases. There's some good written opinions that we're able to rely on, really stemming from some two 2024 cases, which are discussed in our year-in-review blog. They were pretty high-profile federal court cases, one in New York and one in Florida. Raising Ponzi-type scheme claims against banks and really encourage you to have them in your arsenal if you're facing one of these claims.

The first one we talked about in the blog was the O'Dell versus Berkshire Bank case, which had been pending in New York. In that case, the federal judge granted a motion to dismiss the Berkshire Bank from a class case alleging that it had aided and abetting a $90 million Ponzi scheme for roughly a decade. What the court said was that, the investors simply had not pleaded facts showing that the bank had actual knowledge of the fraud. They had just pleaded their claims in general terms, the fact that the bank had numerous internal controls, legal obligations, oversight mechanisms, et cetera, to detect and impede the fraudulent activity

But then, what they failed to do was plead actual non-conclusory facts showing that the defendant possessed actual knowledge of the fraudulent intent, and that just wasn't enough. The court found it was just speculation, and the fact that the bank should have known that the bad actor was conducting a Ponzi scheme wasn't sufficient to state a claim and allege the substantial assistant that was required under the law to sustain the claim.

Then, there was another more recent case decided in November of 2024 out of the Southern District of Florida, the FW Distributors case. It wasn't a Ponzi scheme case, but it was a similar fraud type scheme. But the plaintiff had fallen victim to a fraud scheme, and thereafter brought claims against the banks who banked the fraudsters, alleging that they engaged in aiding and abetting fraud, by allowing hundreds and thousands of dollars to flow through their accounts. And it couldn’t have escaped the notice of bank personnel they alleged. The court granted the bank's motion to dismiss in that case as well, holding that that type of allegation, the mere routine banking services provided to the fraudsters was insufficient to show the actual knowledge necessary to sustain an aiding and abetting claim. And that the mere ministerial services of banking bad actors is not the type of substantial assistance that the law requires.

Really, the headline here is that courts are finding that allegations of providing routine banking services are insufficient to show actual knowledge, and that these claims looping in Bank Secrecy Act and know-your-customer allegations don't get them over that hurdle either.

Chris Willis:

Yes, that's interesting, Mary. From the two cases that you described, it seems like the courts are drawing a bright line between the legal requirement of actual knowledge of fraud, which the court seemed to be putting out on the plaintiffs, and rejecting the idea that the banks have some duty of supervision, or duty of inquiry, or duty to monitor what their depositors do to make sure they're not committing fraud. That seems like a very important line for the courts to have drawn.

Mary Zinsner:

It is, Chris, you're absolutely right. It also points out that the courts aren't allowing constructive knowledge to be enough either. They're not saying, "Well, your systems knew that there was some fraud going on, so you must have known as well." So, courts fortunately are kind of seeing through some of these strategies that plaintiffs' lawyers are embarking on.

Chris Willis:

Well, that's good news. Heryka, I'm going to turn to you now, and see what kind of good news you have to share with the audience. What are the kinds of trends you're seeing in the litigation matters you're handling?

Heryka Knoespel:

Well, I don't know if it's good news, but it's definitely a trend that we're seeing here, with check washing, and elder exploitation scams. In the check washing space, this is when the fraudster is completely removing or erasing the ink from a legitimate check and then creating a new instrument. That in many ways is very difficult for a bank to see that it's not a legitimate check. So, these check washing cases are really interesting, because under the UCC, there is a different liability structure here.

The account may see a denial for the check claim, and then, an insurance company pays out the claim, and then the insurance company is usually coming after the bank under Subpart E rights. So, it's very interesting to see the insurance companies starting to get involved in these cases, and really explaining to plaintiff's counsel about these differences in how a check washing case versus an altered check are different under how the UCC treats those types of cases.

Then, of course, the elder exploitation scams unfortunately continue to be on the rise. This is a topic of deep concerns. The FBI and regulators, including the CFPB, FinCEN, and OCC have been writing about these issues. We're seeing a lot of marketing campaigns to make senior citizens more aware of these types of scams. But unfortunately, they continue to occur. The real remedy for the victim of plaintiffs is not to sue the banks, but to lobby the state legislatures for increased protections for seniors. Those are two trends that are coming across my desk a lot and have been keeping me quite busy these days.

Chris Willis:

Okay. Well, I'm definitely sorry to hear about that. What kind of scams were most prevalent in your practice over the past year?

Heryka Knoespel:

We're still seeing individuals posing as big tech, or big bank employees, and urging elderly senior citizens to take some type of specific action. With the rise of AI, that's easier to do through spoofing telephone numbers, using certain voices. So, these unfortunate victims are

then doing those actions believing that it was a big tech or a big bank employee who is legitimately asking them to do those things to secure their funds. So, sometimes, that could be buying gift cards and then giving the fraudsters the gift card numbers, converting their funds into crypto, which then is very hard to track down, or sending very large wire transfers out to the fraudsters. It's a lot of different types of things, Chris, but those are the main patterns

that we see over and over that we're seeing that folks fall victim to.

Mary Zinsner:

Chris, I just want to add some color on these elder scheme cases as well, because it's something I – in my deposit litigation practice, I touch an elder fraud case just every day, and they're very, very sad and troubling cases. But the banks typically do not have liability, and we've had a lot of success defending these cases. But want to just touch on just kind of from a personal note, I had the privilege of speaking at the Georgia Women in Banking Conference this fall and the topic was conversations that count caring for elders. The purpose of the conversation was to engage women bankers on what we could do both as banking professionals to protect the elderly from the onslaught of scams they're facing and what we can do as persons caring for our own elderly parents. So, this personal side is important to me as somebody with an 83-year-old mother who get scam calls every day.

I think people think that their parents are managing fine, but the reality is that the increasing sophistication of these scams are catching our seniors off guard, and our aging parents are among those seniors, and tend to ignore the spam-detected warning signs that pop up on their cell phones, or can't read the print, or they actually answer their landlines, and talk to the spammers, click on links, et cetera.

It's just very easy for the elderly to be tricked, and we all need to be just taking steps to educate our parents, get added on any joint account, so the joint owner can monitor, and actively monitor accounts. Every single deposition I've taken in an elder-fraud case, the person I'm deposing says, "I thought my mom had it under control" or "I never would have thought she would fall for the scam, but they still do." We as individuals with aging parents are the responsible ones for detecting these scams and not the financial institutions who bank our elderly parents.

Chris Willis:

Mary, I've definitely seen a lot of news about wire transfer scams and I feel like I get tons of disclosures from my own depository institution about it every time I want to make a wire transfer. But when those scams happen and people lose money as a result of them, and sue the banks involved, how do those lawsuits come out? Did the plaintiffs succeed in those cases, Mary?

Mary Zinsner:

It's honestly rare for the plaintiffs to succeed. In large part, it's because of Article 4A. The way it was drafted when the drafters of the Uniform Commercial Code, drafted Article 4A, they wanted to create just a uniform scheme outlining the risks and liabilities of the parties. They were very,

very cognizant of making the person who's closest to the fraudster be the one who's responsible for the fraud. So, that is typically the depositor, not the bank. It's usually the depositor who's been duped by fraud.

We rely on the UCC and also principles of privity and preemption. Preemption is a really big defense. Article 4A sets forth a liability scheme and allocates the risk of losses between the parties, and the statute explicitly states that resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties, or liabilities inconsistent with this article.

What that means in ordinary terms is, is that parties who sue the banks have a difficult time recovering by asserting common law claims such as negligence or breach of fiduciary duty, because those claims are encompassed by the UCC itself. Then, the other area where we've had a lot of success in is just the cool concept of privity. The UCC is grounded in concepts of privity and the premise that the party closer to the fraudsters has the duty to detect the fraud and is the party who bears responsibility. So, no mistake about it, the drafters of the UCC intended to create and crack procedures to facilitate really high-volume seamless fund transfers on a daily basis and insulate the banks from liability.

As a result, what you're seeing is more and more courts are enforcing privity requirements and making plaintiffs who are victims have privity with the bank against if the claim is asserted. We wrote about privity in our recent blog article on the Year in Review. The case called Approved Mortgage Corporation out of the Seventh Circuit. In that case, what the court held was that the sender of a wire could not seek a refund from the beneficiary bank. Remember, the beneficiary bank is the bank that actually receives the funds in the wire transfer. So. the person who was defrauded didn't have a direct cause of action against that beneficiary bank under the UCC because it lacked privity. Its relationship was with the bank that sent the wire, not the bank that received the funds.

In many cases, unbeknownst to the beneficiary bank, they're banking the fraudster, and once the funds hit the account, they're gone. So, the sender tries to sue the beneficiary bank directly, but courts are imposing this privity requirement, and that's what happened in the Approved Mortgage, the Seven Circuit held that because the sender of the wire had a relationship with the banks that originated the wire transfer and not the beneficiary bank. It couldn't assert a UCC claim. The court just went on to talk about the whole purpose of the UCC is to provide certainty and finality between the various parties. Privity is one of those ways of enforcing that uniformity.

The takeaway is, Chris, is really that the parties have an uphill battle suing the banks and really should focus on the non-bank parties and the parties closer to the fraudster. So, if it's a scam arising between a vendor and somebody who was expecting payment, those are the parties you should be fighting it out and not bringing in the banks.

Chris Willis:

Okay, got it. Well, Heryka, if you don't mind, let me go back to you. We talk about this being a year in review and look ahead. We've reviewed what's happened in 2024 with both of your practices and this important area of litigation. But what do you see in terms of potential changes or developments, things you're going to be looking out for in 2025?

Heryka Knoespel:

Sure. I'm a very optimistic person, Chris. So, I'm hopeful that we see a decrease in scams, but the reality of the landscape that we're seeing is that we probably will see the same in 2025 with these continued types of scams. Maybe even getting a little bit more sophisticated with the rise of AI. One thing that Mary and I are continuing to monitor as Mary discussed earlier. We are making some great wins on behalf of our clients through the preemption and privity arguments, but we are monitoring a pushback and a change in arguments that are being raised in our court cases where plaintiffs are trying to shift what law applies to these claims.

That is improper, but given the vulnerability of the plaintiffs, sometimes we might see and we've seen some blows in other cases that are not ours, where the court adopts a different type of law in the cases. So, we are continuing to monitor what we're seeing with whether or not the Electronic Fund Transfer Act applies to wire transfers. We do not think that applies. We think the UCC 4A governs, but we are monitoring that as we've seen some cases that have seemed to indicate that it depends on where the wire is in the process. So, whether it's a movement of funds within the wire network or it's the bank-to-bank portion.

This type of parsing out makes it very, very difficult to show where the liability should fall and goes against what the UCC instructs to make a clear division of liability in these cases, so that all the parties have finality. We're continuing to monitor emerging case law and the regulator's statements on this issue. It's something to continue watching in 2025. We're happy to chat with folks and be a sounding board on these types of cases that we've discussed today.

Chris Willis:

Okay. Well, thank you very much. This is a really important topic. It's important to our depository institution clients, as I mentioned before, and important just from a societal standpoint as well. It's part of the overall entire suite of services that we offer to our financial institution clients to help them with litigation matters like this. So, Mary, Heryka, thank you very much for being on the podcast today. Of course, thanks to our audience for listening as well. Don't forget to visit and subscribe to our blogs, TroutmanFinancialServices.com and ConsumerFinancialServicesLawMonitor.com. While you're at it, why not visit us on the web at troutman.com and add yourself to our Consumer Financial Services email list. That way, we can send you copies of the alerts and advisories that we release from time to time, as well as invitations to our industry-only webinars that we also put on. Of course, stay tuned for a great new episode of this podcast every Thursday afternoon. Thank you all for listening.