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NEW YORK HIGH COURT DECISION, ALLOWING JUDGMENT CREDITORS TO GARNISH OVERSEAS OR OUT-OF-STATE PROPERTY, SIGNIFICANTLY IMPACTS INTERNATIONAL BANKS AND THEIR CLIENTS

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The New York Court of Appeals, New York's highest court, earlier this year rendered a decision, captioned *Koehler v. Bank of Bermuda Ltd.*,[1] that is in the course of becoming a landmark case for judgment collection worldwide. Based on the split opinion in *Koehler*, a New York court may order a bank, brokerage house or other financial institution with a presence in New York to deliver to a judgment creditor any assets it holds for a judgment debtor, regardless of whether the judgment debtor or creditor have any contacts with New York, or whether the bank is holding the assets outside of New York. The judgment creditor may use a special "turnover" proceeding to force the bank that is in possession of the judgment debtor's assets to bring those assets to New York and turn them over to the judgment creditor. Because there is no need for the judgment debtor or creditor, or the debtor's assets, to have any ties to New York, the ruling allows judgment creditors around the globe to reach the assets of a judgment debtor anywhere in the world that are held by a bank wherever located, so long as the bank also happens to do sufficient business in New York – and most of the major banks do, if only through a branch office or agent – so as to subject the bank to personal jurisdiction here.

The ramifications of *Koehler* are potentially staggering. As expressed in the amicus brief filed on behalf of the banks by The Clearing House Association, the nation's oldest banking association, the case sets "a precedent that could profoundly affect the business of financial institutions and the role of New York as a leading financial center." Indeed, in the few months since the ruling was issued, several international banks operating in New York have received subpoenas seeking information and documents, accompanied by restraining notices, in connection with efforts by judgment creditors to collect on judgments obtained in legal actions outside of New York that were registered for collection here.

Background of the Case

In 1993, Lee Koehler, a citizen of Pennsylvania, obtained a default judgment for roughly $2 million against David Dodwell, a citizen of Bermuda, in the U.S. District Court for the District of Maryland.[2] At that time, Dodwell owned shares in a Bermuda

[1] 12 N.Y.3d 533 (2009); 911 N.E.2d 825 (N.Y. 2009).
[2] *See* 12 N.Y.3d at 536.

corporation, which were held in that country by the Bank of Bermuda Ltd. ("BBL") as collateral for a loan made to him by BBL.[3]

Koehler registered the judgment for collection with the U.S. District Court for the Southern District of New York and initiated a garnishment proceeding against BBL for delivery of the shares pursuant to New York Civil Practice Law and Rules ("CPLR") § 5225(b).[4] This special proceeding authorizes a New York court to order a third party in possession of assets of a judgment debtor (the third party often called the "garnishee") to turn over to a judgment creditor any of the judgment debtor's assets in which the garnishee does not itself have a superior interest.

BBL initially argued that it did not do business "regularly and systematically" in New York so as to be subject to personal jurisdiction in New York, even though its affiliate, Bank of Bermuda (New York) Ltd., maintained offices in New York.[5] After a decade of litigation, BBL eventually consented to personal jurisdiction in New York.[6] But the district court nevertheless dismissed Koehler's application on several grounds, including that it did not have *in rem* jurisdiction (*i.e.*, power over the "thing") as regards the assets in question – Dodwell's shares – because these assets were not present within New York, but were still in Bermuda.[7]

Koehler appealed to the U.S. Court of Appeals for the Second Circuit, which "certified" the following question to the New York Court of Appeals: does a turnover proceeding pursuant to CPLR § 5225(b) reach assets located outside New York?[8]

In a 4-3 split opinion, the New York Court of Appeals answered the question in the affirmative.

The Court's Reasoning

Writing for the majority, Judge Pigott, joined by Chief Judge Lippman and Judges Ciparick and Graffeo, held that CPLR § 5225(b) permits a New York court to order a garnishee over which it has personal jurisdiction to deliver property over which it has no *in rem* jurisdiction.[9] According to the majority, the requirement that there be *in rem* jurisdiction prior to granting a pre-judgment order of attachment under CPLR Article 62 (*e.g.*, where the defendant is seeking to hide or remove assets from the state) was not dispositive of the question of whether *in rem* jurisdiction was also required for a post-judgment garnishment under CPLR § 5225(b) such as here. Although pre-judgment attachment requires *in rem* jurisdiction because CPLR Article 62 allows a creditor to proceed against property by requesting a New York sheriff to take custody of it, post-judgment enforcement requires only personal jurisdiction because CPLR § 5225(b) provides for a "turnover order" where the judgment debtor's property is in a third party's possession. CPLR § 5225(b) thus offers a vehicle by which to proceed against a person, not only a piece of property.[10]

The majority also observed that CPLR § 5225 "contains no express territorial limitation [although i]t would have been an easy matter for the Legislature to have added such a restriction," citing as further support a recent amendment to a parallel provision of the CPLR.[11]

Judge Smith's dissent, joined by Judges Read and Jones, noted that the majority's conclusion could turn New York into a "forum-shopping opportunity for any judgment creditor trying to reach an asset of any judgment debtor held by a bank (or other garnishee) anywhere in the world [as long as] the bank has a New York branch – either one that is not separately incorporated, or a subsidiary with which the parent's relationship is close enough to subject the parent to New York jurisdiction."[12] New York courts could thus be called upon to adjudicate the ownership of assets around the world, despite the fact that the jurisdiction in which the asset is actually held would

3 *See id.*
4 *See id.*
5 *See id.*
6 *See id.*
7 *See id.* at 537.
8 *See id.*
9 *See id.* at 537-41.
10 *See id.* at 537-38.
11 *Id.* at 539.
12 *Id.* at 542.

be the logical venue to adjudicate competing ownership claims.[13] According to the dissent, the majority's holding could also subject banks operating in New York to "significant administrative burdens," and subject them to the risk of conflicting adjudications by different courts that may decide over the ownership of the assets at issue.[14]

The dissent argued further that the majority's disposition of the case may violate the limits placed on the jurisdiction of New York courts by the Due Process Clause of the U.S. Constitution, such as that any assertion of state court jurisdiction must satisfy "traditional notions of fair play and substantial justice."[15] Because none of the parties or assets at issue in *Koehler*, aside from the bank garnishee, had any connection to New York, the enforcement of the judgment by a New York court may well violate this standard, the dissent opined.[16]

Conclusion

The constitutional and policy issues raised in the dissent suggest that *Koehler*, upon remand to the Second Circuit or in its progeny in other cases, will be subject to vigorous challenge. If undisturbed, *Koehler* makes the assets of foreign and out-of-state judgment debtors vulnerable to garnishment in New York, even where the judgment debtor has no connection to New York other than that her bank does business there.

Although the full impact of *Koehler* has yet to be seen, judgment debtors and banks in any jurisdiction should be concerned about this ruling because it may provide legal precedent for judgment creditors to collect on debts that may previously have been considered beyond reach. Judgment debtors should be aware that their banks, if they do business in New York, may be forced by New York courts to ship the debtors' assets to New York to turn them over to judgment creditors. As a result, judgment debtors anywhere in the world may be called to defend their interests before New York courts and should consider how best to protect their assets.

International banks and other financial institutions should advise their clients of these risks. They should also determine whether their business in New York makes them subject to jurisdiction there and, if so, whether that business is worth the legal and administrative burdens possibly resulting from the simple fact that in their home office some client may have an account, which client may also be a judgment debtor elsewhere. In particular, a financial institution should attempt to gauge the risk that its refusal to comply with a New York turnover order results in the complex, extensive and costly litigation that it often does; and, conversely, the risk that compliance with such an order, or with a subpoena seeking documents and information in connection therewith, could expose it to damages claims by its clients and violate bank secrecy laws in force in other jurisdictions in which it may operate.

Finally, judgment creditors will increasingly choose New York as their forum of choice to bring turnover proceedings against financial institutions with operations here that hold assets for foreign or out-of state judgment debtors. To judgment creditors, New York may offer new hope that they may be able to enforce judgments that, like in *Koehler*, have gone unsatisfied for years elsewhere.[17] Further, CPLR § 5225(b) allows judgment creditors who have difficulties locating their debtors to initiate a turnover proceeding in New York without personal service, by serving the judgment debtor by registered or certified mail, return receipt requested. Nevertheless, although judgment creditors clearly get all the upside of *Koehler*, they – together with any other creditors of the judgment debtor – may feel the downside of being forced to come to New York to defend their interests in a debtor's assets against attempts by a competing judgment creditor that seeks to seize those assets through a turnover proceeding in that state.[18]

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13 *See id.*
14 *See id.*
15 *Id.* at 544 (*quoting Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945)).
16 *See id.* at 544-45.
17 The New York statute of limitations for judgments is twenty years.
18 Although no other party made a competing claim to the shares at issue in *Koehler*, CPLR § 5225(b) allows any party with a competing claim to the judgment debtor's assets to intervene in a turnover proceeding commenced by the judgment creditor in New York.

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