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I. INTRODUCTION

This Comment seeks to examine the procedural issue presented by a conflict between the federal circuit courts. At issue in the split between on the one hand, the D.C. and Eighth Circuits, and on the other, the Eleventh Circuit, is the effect on existing federal common law when Congress enacts a statute covering the same substantive area of law. The question of the interaction between statutory and common law is a difficult one because all judicial power is, by necessity, limited. As Benjamin Cardozo described the judicial power:

courts . . . are free in marking the limits of the individual’s immunities to shape their judgments in accordance with reason and justice. That does not mean that . . . they are free to substitute their own ideas of reason and justice for those of the men and women whom they serve. Their standard must be an objective one.1

Federal courts, as courts of limited jurisdiction, are particularly restricted in the exercise of their judicial power. Within their federal question jurisdiction, however, they, like all courts, have the power to create common law. This power might best be described as the ability to create a rule of decision to resolve a dispute before the court when that dispute is not resolved by statute or administrative rule. Though federal courts have the ability to create common law, this power is only exercised in rare cases.2 These cases are made even rarer by the deference that courts must show to the legislative branch; outside of constitutional law, the judiciary regularly defers to the legislative branch’s disposition of federal law. This deference is at its height when Congress enacts comprehensive legislation.3 The question of deference becomes more complicated, however, when Congress legislates in an area where the courts have already created federal common law rules of decision.

By comparing the specific conflict between, on the one hand, the D.C. Circuit’s decision in Murphy v. Federal Deposit Insurance Corp.4 and the Eighth Circuit’s decision in DiVall Insured Income Fund Ltd. Partnership v. Boatmen’s First National Bank,5 and, on the other, the Eleventh Circuit’s decision in Motorcity of Jacksonville, Ltd. v. Southeast Bank,6 the issue of the deference of the judiciary to the legislature comes into focus. The three cases examine the common law D’Oench

2. See Wheeldin v. Wheeler, 373 U.S. 647, 651 (1963) (describing the instances when a federal court may create common law as “few and restricted”).
4. 61 F.3d 34 (D.C. Cir 1995).
5. 69 F.3d 1398 (8th Cir. 1995).
6. 83 F.3d 1317 (11th Cir. 1996) (en banc).
rule of decision. This rule was created by the United States Supreme Court in 1942 to protect the Federal Deposit Insurance Corporation (FDIC) from secret agreements when it must step in to resolve a failing depository institution.\(^7\) Under the *D'Oench* rule, secret agreements between a maker of an instrument and a depository institution cannot be asserted against the FDIC.\(^8\) In 1950, Congress codified a part of the common law rule.\(^9\) This codification was amended in 1989 by the passage of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA).\(^10\) Both *Murphy* and *DiVall* held that the latter amendment displaced the *D'Oench* rule of decision.\(^11\) As a result, any secret agreement that fell outside the statute could be asserted against the FDIC, even if it would have been barred by the common law rule. *Motorcity* rejected this result, arguing that there was no indication within the statute that Congress intended it.\(^12\)

A comparison of these cases reveals for consideration the issue of the proper standard to be applied to determine whether a statute has displaced the common law. The *Murphy/DiVall* decisions relied upon the standard set forth in *O'Melveny & Myers v. Federal Deposit Insurance Corp.*,\(^13\) which held that FIRREA was a comprehensive statute that barred the federal courts from creating new common law.\(^14\) In relying upon a decision explaining a refusal to create new common law to invalidate the well-developed *D'Oench* rule, *Murphy* essentially created a new standard for determining congressional displacement of established common law. The *Motorcity* court refused to go along with the new standard and distinguished *O'Melveny & Myers* as inapplicable; *D'Oench* was not new common law, but an established rule of decision.\(^15\) The Eleventh Circuit held that the standard used to determine displacement should instead be that of *United States v. Texas*,\(^16\) which required a finding of congressional intent to displace before abrogating established common law.\(^17\) The *Motorcity* court was unable to find the requisite congressional intent and found no displacement of *D'Oench* and its progeny.\(^18\)

Although this conflict centers around a narrow area of commercial law, the decisions have ramifications beyond the substantive issue of which secret agreements may be asserted against the FDIC. These cases add uncertainty to the interplay between statutory and common law. This Comment examines this area of

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8. See id. at 460.
11. See *Murphy v. Federal Deposit Ins. Corp.*, 61 F.3d at 39; DiVall Insured Income Fund Ltd. Partnership v. Boatmen's First Nat'l Bank, 69 F.3d at 1404. Although, strictly speaking, *DiVall* concerned the federal holder in due course doctrine, that doctrine has its genesis in *D'Oench*. See infra note 112. *DiVall* relied upon *Murphy* in reaching its decision that FIRREA also displaced the federal holder in due course doctrine. See DiVall Insured Income Fund Ltd. Partnership v. Boatmen's First Nat'l Bank, 69 F.3d at 1402.
14. See id. at 86-87.
15. See *Motorcity of Jacksonville, Ltd. v. Southeast Bank*, 83 F.3d at 1331.
17. See *Motorcity of Jacksonville, Ltd. v. Southeast Bank*, 83 F.3d at 1333; *United States v. Texas*, 507 U.S. at 539.
interaction and argues that the *Murphy/DiValle* decisions were based upon a misperception of the correct relationship between statute and common law and were therefore wrongly decided. Part I introduces the federal common law and the traditional approach taken by the United States Supreme Court in resolving the common law with federal statutes. Part II provides context to the Circuit Court split with an explanation of the substantive *D'Oench* common law rule of decision and its statutory enactments. Part III discusses the split between the circuits, while Part IV suggests a resolution.

This Comment argues that the same policies underlying the reluctance of federal courts to create new common law also underlie the analysis of whether a statute has displaced the established common law even though the common law has a much greater vitality in the latter case than in the former. When Congress has created a comprehensive statutory scheme, the creation of new common law has the potential to upset that scheme. When Congress legislates against the background of established common law, on the other hand, it should be presumed that there was no intent to displace that law. Absent an explicit contrary congressional intent, the established common law should be seen as a complement to the congressional scheme. Otherwise, Congress might rely upon a background of established rules of decision when it creates its legislative scheme, only to find the plan upset when a federal court uses the legislation to eliminate those established rules.

The question of the interaction between statutory and common law will arise again in the future. Other circuits should follow the Eleventh Circuit's example in *Motorcity* when faced with the question of the continued vitality of *D'Oench* and should reject any attempt to expand the *Murphy/DiValle* presumption about federal common law into other substantive areas. When courts retain the traditional presumption of the survival of common law, they ensure that an important part of our system remains vital. The common law is an inherently flexible approach to rule-making that exists in balance with legislative authority. *Murphy/DiValle* upset this balance; for these reasons, the conflict between the circuits should be resolved to continue the practice of refusing to find displacement of established common law by a newly enacted statute unless there is explicit indication of a contrary congressional intent.

II. A BRIEF OVERVIEW OF FEDERAL COMMON LAW

Federal courts are courts of limited jurisdiction. They can exercise that jurisdiction in only two areas: where there is a complete diversity of citizenship in the parties or where the action "aris[es] under this Constitution, the Laws of the

20. Even under the traditional rules allowing for the survival of established common law following passage of a comprehensive statute, the common law is inherently limited. Unlike constitutional precedent, Congress may change judicially created rules it finds inimicable. This Comment argues, however, that Congress must act affirmatively and explicitly in order to exercise this power.
United States, and Treaties made, or which shall be made, under their Author-
ity." 22 Within their areas of jurisdiction, federal courts have the power to create
common law. The common law tradition has evolved to give courts the power to
"fashion law for the litigants before" them. 23 "In fashioning it for them, [the court]
will be fashioning it for others." 24 In this respect, common law moves beyond an
interpretation of statute or administrative rule to the creation of new rules of deci-
sion. 25 In federal courts, this power was initially quite broad. In *Swift v. Tyson*,
the Supreme Court construed § 34 of the 1789 Judiciary Act, requiring federal
courts to regard "as rules of decision in trials at common law in the Courts of the
United States" the "laws of the several states." 27 The Court held that "[i]n the
ordinary use of language it will hardly be contended that the decisions of Courts
constitute laws." 28 Consequently, federal courts were free both to construe the
statutes of the states independently of the construction given them by state courts
and, when there was no statute covering the facts before the court, to create inde-
pendently the common law rule of decision.

In 1938, these broad powers were curtailed when the Supreme Court decided
*Erie Railroad Co. v. Tompkins*. 29 Tompkins had instituted a diversity suit against
the railroad, alleging that the negligence of the railroad caused the injury he sus-
tained when he was struck by a freight train while walking on the railroad's right
of way. 30 The railroad contended that under Pennsylvania common law, its duty to
Tompkins was that owed to a trespasser, and consequently, Tompkins could not
prove facts sufficient to allow recovery. 31 Tompkins argued that because there
was no Pennsylvania statute covering the duty owed to one walking on a railroad's
right of way "the railroad's duty and liability is to be determined in federal courts
as a matter of general law." 32 The court rejected this argument and declared that

have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of
the United States."). Although the language in this section is similar to that in the Constitution,
courts have recognized important differences in the meaning of the two. The constitutional
language has been read expansively so that any case or controversy that might call for the appli-
cation of federal law could confer jurisdiction. See *Osborn v. Bank of the United States*, 22 U.S.
326, 334-36, 9 Wheat. 737, 758-60 (1824). The actual statutory grant, however, is much more
limited, requiring "that the federal question must appear on the face of a well-pleaded complaint
and may not enter in anticipation of a defense." See *Verlinden v. Cent. Bank of Nigeria*, 461


24. Id.

one might call 'federal common law' in the strictest sense, i.e., a rule of decision that amounts,
not simply to an interpretation of a federal statute or a properly promulgated administrative rule,
but, rather, to the judicial 'creation' of a special federal rule of decision").


27. Id. at 18 (quoting § 34 of the 1789 Judiciary Act). Until 1875 there was no federal
question subject matter jurisdiction; prior to that date, diversity of citizenship was the only way
for a federal court to take jurisdiction.

28. Id.

29. 304 U.S. 64 (1938).

30. See id. at 69.

31. See id. at 70.

32. Id.

33. Id. at 78.
"[t]here is no federal general common law." The Court noted that "[t]he federal courts [had improperly] assumed, in the broad field of 'general law,' the power to declare rules of decision which Congress was confessedly without power to enact as statutes." With this decision, the broad power of the federal courts to create common law was severely restricted.

_Erie_, however, did not mean the end of all federal common law. _Erie_ stands for the proposition that

law in the sense in which courts speak of it today does not exist without some definite authority behind it. The common law so far as it is enforced in a State, whether called common law or not, is not the common law generally but the law of that State existing by the authority of that State without regard to what it may have been in England or anywhere else.

Even without the broad idea of a universally applicable "general common law," federal courts could continue to exercise their "common law" powers so long as they were promulgating rules of decision under the authority of the United States. As _Erie_ itself stated, "[e]xcept in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State." When faced with a federal question not answered by a statute, _Erie_ left open the possibility that the federal courts could fashion their own rule of decision.

This power, however, has never been broadly construed and has instead been limited to certain specific instances:

The Court has recognized the need and authority in some limited areas to formulate what has come to be known as "federal common law." These instances are "few and restricted," and fall into essentially two categories: those in which a federal rule of decision is "necessary to protect uniquely federal interests," and those in which Congress has given the courts the power to develop substantive law.

Absent a congressional directive to the courts to make common law, a federal court, before creating common law, must decide whether it is faced with one of the "few areas, involving 'uniquely federal interests,'…so committed by the Constitu-

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34. _Id._ at 72.
35. _Id._ at 79 (quoting Black & White Taxicab Co. v. Brown & Yellow Taxicab Co., 276 U.S. 518, 533-34 (Holmes, J., dissenting)).
36. _Erie R.R. Co._ v. _Tompkins_, 304 U.S. at 78.
37. As Justice Jackson stated in his famous concurrence to _D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp._, discussed _infra_ at notes 82-103 and accompanying text:

I do not understand Justice Brandeis's statement in _Erie R.R. Co._ v. _Tompkins_, 304 U.S. 64 at 78, that "There is no federal general common law," to deny that the common law may in proper cases be an aid to, or the basis of, decision of federal questions. In its context it means to me only that federal courts may not apply their own notions of the common law at variance with applicable state decisions except "where the constitution, treaties, or statutes of the United States [so] require or provide."

tion and laws of the United States to federal control that state law is pre-empted and replaced, where necessary, by federal law of a content prescribed (absent explicit statutory directive) by the courts-so-called "federal common law." In cases where there is an explicit statutory scheme, however, this power to create new federal common law is curtailed. In *Northwest Airlines, Inc. v. Transportation Workers* and *Texas Industries, Inc. v. Radcliff Materials, Inc.*, the Court dealt with the question of whether a statutory enactment allows for the creation of new federal common law to supplement existing statutory remedies. In both cases, the Court declined to allow the creation of such a remedy.

In *Northwest Airlines*, the Court was asked to create a right of contribution in favor of Northwest. Northwest had lost a class action suit instituted by a Mary Laffey, who argued that the wage differentials between the male cabin attendants, classified as pursers, and the female cabin attendants, classified as stewardesses, were in violation of the Equal Pay Act and Title VII of the Civil Rights Act of 1964. Northwest was ordered to pay "in excess of $20 million in back pay, damages, and interest to the members of the Laffey plaintiff class." After this loss, Northwest brought the present action against the two unions representing the airline workers, Transport Workers Union of America and the Air Line Pilots Association, International, reasoning that they bore "at least partial responsibility for the statutory violations" and that Northwest had either "a federal statutory or common-law right to contribution" from the two unions. In *Texas Industries*, both parties "manufactured and sold ready-mix concrete in the New Orleans, La., area." Texas Industries, however, had been sued in 1975 by one of its customers who had alleged a conspiracy to raise concrete prices in violation of the Sherman Act. The complaint sought treble damages and attorney's fees.

39. Boyle v. United Techs. Corp., 487 U.S. 500, 504 (1988)(citations omitted). The issue in Boyle was whether a federal contractor should be shielded as a matter of federal common law against state tort claims allegedly arising from design defects in equipment produced for the military. See id. at 503. The Court reasoned that the protection of contractors who created their designs under the close supervision of the military was an area of "uniquely federal" interest as it directly affected the government's ability to get work done and procure at a reasonable cost necessary equipment for the military. See id. at 504-07. The Court then concluded that state law was displaced, at least in part, and designed an immunity from state law actions for design defects in cases where the contractor had acted according to specifications given them by the government and had warned the government of any risks connected with the equipment that the contractor was aware of. See id. at 512. Unique federal interests have also been found in cases where there was a controversy between two states regarding streamwater, see Hinderlider v. La Plata River & Cherry Creek Ditch Co., 304 U.S. 92 (1938), where the controversy concerned the relationship between the United States and members of its armed forces, see United States v. Standard Oil Co. of Cal., 332 U.S. 301, 305 (1947), where the controversy implicated the liability of federal officers for official conduct, see Howard v. Lyons, 360 U.S. 593, 597 (1959), and where the controversy has concerned official relationships with other countries, see Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 425 (1964).

42. See *Northwest Airlines, Inc. v. Transp. Workers*, 451 U.S. at 80-81.
43. Id. at 82.
44. Id. at 79-80.
46. See id. at 632.
47. See id.
tries also brought a third party complaint asking for contribution from respondents, the "other concrete producers that had participated in the alleged price-fixing scheme," in the event that it was held liable against its customer.48

The Court followed the same analysis in both Texas Industries and Northwest Airlines. It noted that the right of contribution in both cases could be created in one of two ways: either it was created by statute or by "the exercise of judicial power to fashion appropriate remedies for unlawful conduct."49 In neither case, however, could the Court discover a right of contribution under the statutory language.50 The Court then went on to consider whether it might fashion a remedy outside of the statutory language and began its analysis with the premise that the power of federal courts to fashion common law was limited.51 Such a step, the Court determined, could be undertaken where there were "‘uniquely federal interests’ of the kind that oblige courts to formulate federal common law."52 Even in areas where the "federal judiciary’s lawmaking power [was] at its strongest," common law powers were subordinate to Congress’s power to legislate.53 The federal judiciary’s capacity to make common law had to coexist with Congress’s inherent power to legislate for the nation. When Congress had already legislated on an issue, courts had to be circumspect in the decision to create a common law rule of decision, lest they create a remedy that Congress had deliberately decided not to include. In the absence of direct congressional intent, courts had to rely upon a presumption about whether a remedy was deliberately excluded; "[t]he presumption that a remedy was deliberately omitted from a statute is strongest when Congress has enacted a comprehensive legislative scheme including an integrated system of procedures for enforcement."54 Where there was such a scheme, only direct evidence to the contrary would overcome the presumption and allow courts to create new common law rules.55 Otherwise, a court might "fashion new remedies that might upset carefully considered legislative programs."56 The Court found a

48. Id. at 633.
comprehensive scheme in both cases and refused to create a federal common law right of contribution.\textsuperscript{57}

In both \textit{Northwest} and \textit{Texas Industries}, the Court was asked to create new common law rules of decision following the passage of a comprehensive statute. Congress does not always have the first word on an issue. In \textit{Northwest} and \textit{Texas Industries}, the Court was concerned that the creation of new common law would upset the statutory scheme. The Court has expressed a similar concern, though with different results, when Congress legislates in an area where a common law rule of decision is already in existence. Congress legislates against the background of common law. "The Court has admonished that statutes will not be construed in derogation of the common law unless such an intent is clear."\textsuperscript{58} In order for this principle to apply, however, the existing common law must be established prior to the passage of the statute.

In \textit{Milwaukee v. Illinois},\textsuperscript{59} the Court established guidelines for determining when common law could be considered created and thus when the presumption regarding the interaction between statute and common law would change. The state of Illinois had sued the city of Milwaukee, claiming that discharges from the city’s sewer system, in combination with inadequate treatment of sewage, was allowing various pathogens to be released into Lake Michigan where they were transported by lake currents to Illinois.\textsuperscript{60} Illinois had first sought, in \textit{Illinois v. Milwaukee},\textsuperscript{61} to invoke the Supreme Court's original jurisdiction.\textsuperscript{62} While the Court rejected any exercise of original jurisdiction, it nonetheless observed that the dispute between Milwaukee and Illinois concerned interstate waters, and, therefore, federal law should apply.\textsuperscript{63} The statutes that had been passed by Congress at that point did not appear to address the situation, but the Court said that such laws were "not necessarily the only federal remedies available" and that "Illinois could appeal to federal common law to abate a public nuisance in interstate or navigable waters."\textsuperscript{64} Following that decision, "Illinois filed a complaint in United States District Court for the Northern District of Illinois, seeking abatement, under federal common law, of the public nuisance [Milwaukee was] allegedly creating.... Five months later Congress . . . passed the Federal Water Pollution Control Act

\textsuperscript{58} Milwaukee v. Illinois, 451 U.S. 304, 339 n.8 (1981) (Blackmun, J. dissenting) (citing Isbrandtsen Co. v. Johnson, 343 U.S. 779, 783 (1952) (holding that "[s]tatutes which invade the common law...are to be read with a presumption favoring the retention of long-established and familiar principles, except when a statutory purpose to the contrary is evident")). \textit{See also} Graham v. John Deere Co., 383 U.S. 1, 16-19 (1966) (holding that § 103 of the Patent Act was a "codification of judicial precedents embracing" the prior federal common law and rejecting, for that reason, an argument urging the Court to "find in § 103 a relaxed standard, supposedly a congressional reaction to the 'increased standard' applied by this Court in its decisions over the last 20 or 30 years;" instead the statute created "no change in the general strictness with which the overall test is to be applied"); Cannon v. Univ. of Chicago, 441 U.S. 677, 698-99 (1979) (holding that "Congress was thoroughly familiar with...precedents from this and other federal courts and that it expected [Title IX of the Education Amendments of 1972] to be interpreted in conformity with them").

\textsuperscript{59} 451 U.S. 304 (1981).
\textsuperscript{60} \textit{See id.} at 309.
\textsuperscript{61} 406 U.S. 91 (1972).
\textsuperscript{62} \textit{See id.} at 93.
\textsuperscript{63} \textit{See Milwaukee v. Illinois}, 451 U.S. at 309.
\textsuperscript{64} \textit{Id.} at 309-10 (quoting Illinois v. Milwaukee, 406 U.S. at 103).
\textsuperscript{65} \textit{Id.} at 310 (citations omitted).
Amendments of 1972.65 After the lower courts found, in part, for Illinois on the basis of a federal common law of nuisance, Milwaukee appealed, thus bringing before the Court the question of whether the statutory enactment had displaced federal common law.66 Concluding that Congress had “occupied the field through the establishment of a comprehensive regulatory program supervised by an expert administrative agency,” the Court decided that there was no room for the federal judiciary to use “often vague and indeterminate nuisance concepts and maxims of equity jurisprudence” to decide the issues presented by this case.67 The Court reached its decision through a close analysis of the statute in relation to Illinois’s claims. It noted that “the Court has been called upon to pronounce common law that will fill the interstices of a pervasively federal framework, or avoid subjecting relevant federal interests to the inconsistencies in the laws of several States,”68 but finally concluded that “[t]here is no ‘interstice’ here to be filled by federal common law: overflows are covered by the Act and have been addressed by the regulatory regime established by the Act.”69 The statute was comprehensive, thus preventing the lower courts from using the federal common law of nuisance to resolve the problem as suggested by the Court in Illinois v. Milwaukee.70

On the other hand, where there was an established common law rule of decision, the Court has refused to find statutory displacement absent an explicit indication of such a congressional intention. In United States v. Texas,71 the Court was asked by Texas to find that the passage of the Debt Collection Act eliminated the common law rule that imposed prejudgment interest on states for amounts they contractually owed the federal government.72 Texas had distributed food stamps through the mail as part of its participation in the Federal Food Stamp Program.73 The federal regulations required that a state reimburse the federal government for all losses above a minimum level that were incurred as a result of using the mails.74 Texas was contractually obligated to follow all applicable federal regulations; it became liable for a debt of $412,385 under these regulations when a substantial

66. See id. at 311-12.
67. Id. at 317.
68. Id. at 336.
69. Id. at 323.
70. Although the Court described its opinion as one determining the standards for when Congress has acted to “supplant[] the federal common law...” id. at 319, and that “[o]ur ‘commitment to the separation of powers is too fundamental’ to continue to rely on federal common law “by judicially decreeing what accords with “common sense and the public weal”’ when Congress has addressed the problem,” id. at 315, the decision is concerned with the creation of new law. Illinois had only learned in 1972, nine years before the Court’s decision, that the federal common law of nuisance might offer it some relief. Furthermore, the Court noted that “legislative activity resulting in the 1972 Amendments largely occurred prior to this Court’s decision in Illinois v. Milwaukee. . . . It is therefore difficult to argue that particular provisions were designed to preserve a federal common-law remedy not yet recognized by this Court.” Id. at 327 n.19. No specific federal common law rule of decision was in existence at the time of the passage of the 1972 statute and the Court was therefore preventing the creation of a new rule that might upset the statutory scheme.
72. See id. at 537.
73. See id. at 530-31.
74. See id. at 531. The mail program was less expensive to operate, but less secure and resulted in replacement costs for lost or stolen food stamps. See id.
number of mail-issued food stamps required replacement, in part because "United States Postal employees stole food stamps that had been mailed by the Texas Department of Human Services to qualified households." In challenging the vitality of the common law rule, Texas sought to avoid paying prejudgment interest on the award.

In its analysis of the Debt Collection Act, the Court concluded that the Act was "intended to enhance the Government's debt collection efforts..." Moreover, the language of the Act demonstrated that "the Act was intended to reach only one subset of potential debtors—persons—and to leave the other subset alone." The common law for applying prejudgment interest to the states required the courts to weigh the state and federal interests involved in the award of prejudgment interest in each case. The common law was therefore more flexible than the standard expressed in the Act. The Court concluded that the Act was meant "to apply more stringent requirements to debts owed by private persons and to keep the more flexible common law in place for debts owed by state and local governments." Without an indication in the statute of an intent to displace, the common law survived the passage of the Act. Texas was obliged to pay prejudgment interest on its debt owed to the federal government.

It is within this federal common law context that any examination of the interaction between the D'Oench common law rule of decision and FIRREA must be examined. These common law principles indicate that the underlying policy consideration is a concern that federal courts not upset a carefully crafted legislative enactment. As the Supreme Court as indicated, however, this policy does not always mandate the abrogation of the judiciary's common law rule-making power. When the common law precedes the statutory enactment, Congress is required to take affirmative action to eliminate the common law rule. Any analysis of the potential displacement of established federal common law thus requires an understanding both of the genesis of the common law rule and the congressional intention underlying the recent enactment.

III. THE INTERACTIONS BETWEEN THE D'OENCH COMMON LAW RULE AND ITS STATUTORY CODIFICATION.

Both the D'Oench common law rule and its statutory codification offer protection to the Federal Deposit Insurance Corporation (FDIC) when it acts after the failure of a lending institution. These two rules have developed side by side since the first codification of the D'Oench rule in 1950. It has only been relatively recently, following the passage of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) in 1989, that an argument has been made for preemption of the common law rule. To understand this argument, it is first necessary to examine the history and development of the D'Oench substantive rule.

75. Id. at 531-32.
77. Id. at 536.
78. See id. at 533.
79. Id. at 536.
80. See id. at 539.
81. See id.
The common law rule was first developed by the United States Supreme Court in *D’Oench, Duhme & Co., Inc. v. Federal Deposit Insurance Corp.*83 *D’Oench* concerned an action on a demand note for $5000 given to the Belleville Bank & Trust Co. (Belleville) in 1933 by D’Oench, Duhme & Co., Inc. (D’Oench, Duhme & Co.) in renewal of notes originally executed in 1926.84 The FDIC had acquired the note in 1938 as collateral for a $1,000,000.00 loan made to Belleville, which was “made in connection with the assumption of the latter’s deposit liabilities by another bank.”85 D’Oench, Duhme & Co. was in the securities business and had sold Belleville a number of bonds that had later defaulted. The note was given and interest payments were made to keep the notes as “live paper” so that the past due bonds would never appear as assets on Belleville’s books.86 Belleville had given D’Oench, Duhme & Co. a receipt for the bonds that stated that “[t]his note is given with the understanding it will not be called for payment. All interest payments to be repaid.”87 Although Belleville’s president knew of the agreement not to sue on the notes, this information was never communicated to the FDIC.88

After Belleville defaulted on the loan made to it by the FDIC, the corporation sought to recoup its loss by demanding payment from D’Oench, Duhme & Co. In response to this demand, D’Oench, Duhme & Co. raised the defense that the note was given without consideration and that the secret agreement between it and Belleville barred the FDIC from any recovery.89 D’Oench, Duhme & Co. alleged that Belleville’s agreement not to call the note for payment should also bind the

83. 315 U.S. 447 (1942).
84. See *id.* at 454.
85. *Id.* Under the terms of the loan transaction, the FDIC was authorized to try to attempt collection in its own name on any collateral should there be a default on the payment of the principal. Belleville Bank defaulted and the FDIC instituted this action after demanding payment of the note. *See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 117 F.2d 491, 492 (8th Cir. 1941).
86. *D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. at 454. The bonds were drainage district bonds, and when they went into default, the bank requested D’Oench, Duhme & Co. to execute two demand notes in an amount equal to the face of the bonds. The bonds were to be carried as “purported collateral” for the notes. *See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 117 F.2d at 492. The notes were originally executed in St. Louis and “contained a recital that they were negotiable and payable at the office of [D’Oench, Duhme & Co.] in that city. The contents of the intermediate renewal notes are not shown. The [present note] consolidated the amounts of the original notes and... was dated Belleville, Illinois, and was made payable at the office of the Belleville Bank & Trust Co. in that city.” *Id.*
88. *See id.* The notes had been among the charged off assets of the bank since 1935. *See id.* D’Oench, Duhme & Co. attempted to raise the issue that this status of the note provided notice of an infirmity and therefore should have defeated any claim by the FDIC that it was an holder in due course. The lower courts rejected this argument, noting that “[t]he charging off of commercial paper by a bank does not necessarily imply an infirmity in the instrument or a defect in the bank’s title, and without other circumstances, is not knowledge of such facts that the transferee’s action in taking the instrument amounts to bad faith under the Negotiable Instruments Law.” *D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 117 F.2d at 494. The Supreme Court, though affirming on different grounds, essentially agreed that a charged off note did not cease to become an asset that the FDIC would have relied upon when insuring the Belleville Bank. *See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. at 461.
FDIC. In addition, the FDIC was, according to D’Oench, Duhme & Co., not a holder in due course and therefore took the note subject to the maker’s defenses. Arguing that the Missouri law applied to this contract, D’Oench, Duhme & Co. contended that the application of this law would bar any recovery by the FDIC. The district court rejected D’Oench, Duhme & Co.’s choice of law argument, deciding instead that the law of Illinois should provide the rule of decision. Under Illinois law, the district court held that the FDIC “had the status of a holder in due course.” D’Oench, Duhme & Co. was therefore liable on the note and judgment was entered accordingly. On appeal, the Eighth Circuit again rejected the choice of law argument, noting that “an accommodation note, like any written instrument, is subject to competent modification. And where, on a renewal of accommodation paper, its terms and recitations are so changed as to make applicable other or different principles of law, their effect cannot be escaped by mere inferences from the original paper.” Determining that the renewal note had been executed in Illinois and that there were no other controlling provisions in it, the court held that Illinois law controlled the contract.

The Eighth Circuit then turned to the issue of whether the FDIC stood as a holder in due course in reference to this note. Referring to the Uniform Negotiable Instruments Law as it was then in force in Illinois, the court noted that a holder cannot be a holder in due course when the note is taken after an “unreasonable length of time after its issue....” Illinois courts, however, had not applied this standard to accommodation notes. A holder of such notes could become a holder in due course if the note was negotiated in due course and the holder had no reason to believe that the note was fraudulent or altered.

90. See id. A holder in due course takes an instrument free of all except the “real” defenses the maker of the instrument may have against enforcement. See U.C.C. § 3-302 (1990). In order to become a holder in due course, the holder must take an instrument without apparent evidence of forgery or alteration and “(i) for value, (ii) in good faith, (iii) without notice that the instrument is overdue or has been dishonored or that there is an uncured default..., (iv) without notice that the instrument contains an unauthorized signature or has been altered, (v) without notice of any claim to the instrument..., and (vi) without notice that any party has a defense or claim in recoupment....” U.C.C. § 3-302 (a) (1990). For a further explanation of the holder in due course concept and its specific relation to the FDIC, see infra note 112.

91. See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. at 455. D’Oench, Duhme & Co. argued that the original notes were executed in Missouri and that as such, they and all that followed from them were contracts falling under Missouri law. See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 117 F.2d at 492. Missouri law would bar recovery because “[t]he note showed on its face that it was nonnegotiable, and at the time the Bank closed was in default...as to principal. This, under Missouri law, charged [the FDIC] with notice of defenses.” D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. at 450. If the FDIC had notice of the defenses, then, contrary to the Circuit Court of Appeals ruling, the FDIC was not the equivalent of a holder in due course entitled to recover. See id. at 455.


93. See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 117 F.2d at 492.

94. See id.

95. Id.

96. See id. at 493. The Supreme Court characterized this decision as one of applying general law to determine which law should apply. See D’Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. at 455.

97. The Uniform Negotiable Instruments law is the precursor to Article 3 of the U.C.C. See U.C.C. Art. 3, Prefatory Note (1990).

in due course even if the notes had been taken after maturity. The court dismissed D'Oench, Duhme & Co.'s contention that five years was an unreasonable length of time. Instead the court held that the FDIC was a holder in due course under Illinois law and therefore took free and clear from the defenses asserted in this case.

D'Oench, Duhme & Co. appealed to the Supreme Court, which affirmed on different grounds. Since "[t]he jurisdiction of the District Court in this case...is not based on diversity of citizenship" but was instead taken under the authority of an "Act of Congress," the Supreme Court held that federal common law rather than the law of Illinois or Missouri should supply the rule of decision for this case. The Court found in the Federal Reserve Act a "federal policy to protect [the FDIC], and the public funds which it administers, against misrepresentations as to the securities or other assets in the portfolios of the banks which [the FDIC] insures or to which it makes loans." Basing its decision upon that policy, the Court held that D'Oench, Duhme & Co. was estopped from pleading the secret agreement between it and the bank as a defense to its obligation on the note. Secret agreements between a bank and a third party hindered the FDIC in its efforts to safeguard the banking system. If it could not depend upon a bank's books, the FDIC could not quickly and efficiently make decisions about insurance or loans. In order to further the federal policy of protecting the FDIC, secret agreements could not be pled as a defense to the obligation on an asset of the bank that was acquired by the FDIC through a purchase and assumption transaction. Moreover, it was not necessary that the parties specifically intend to deceive the FDIC. "The test is whether the note was designed to deceive the creditors or the public authority, or would tend to have that effect. It would be sufficient in this type of case that the maker lent himself to a scheme or arrangement whereby the banking authority

99. See id.
100. Id. at 493.
101. The Court cited 12 U.S.C. § 2640 which stated that "[a]ll suits of a civil nature at common law or in equity to which the Corporation shall be a party shall be deemed to arise under the laws of the United States...." D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. at 455 n.2. Justice Jackson argued that this section of the statute not only conferred jurisdiction upon federal courts, but also allowed those courts to make law in areas where the statute was silent. See id. at 467-68, see also Santoni v. Federal Deposit Ins. Corp., 677 F.2d 174, 178 (1st Cir. 1982) (looking to Jackson's concurrence for guidance in shaping the content of federal common law). In the specific case at hand, Jackson noted that

no federal statute purports to define the Corporation's rights as holder of the note in suit or the liability of the maker thereof. There arises, therefore, the question whether in deciding the case we are bound to apply the law of some particular state or whether, to put it bluntly, we may make our own law from materials found in common-law sources.

D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. at 468. For Justice Jackson, the choice was a simple one:

Federal law is no juridical chameleon, changing complexion to match that of each state wherein lawsuits happen to be commenced because of the accidents of service of process and of the application of the venue statutes. It is found in the federal Constitution, statutes, or common law. Federal common law implements the federal Constitution and statutes, and is conditioned by them.

Id. at 471-72 (footnote omitted).
103. Id. at 457.
on which respondent relied in insuring the bank was or was likely to be misled." 104

B. Statutory Enactments and Judicial Gloss

In 1950 Congress amended the FDIC act. 105 In this amendment of the original 1933 act, Congress added 12 U.S.C. § 1823(e). 106 This section was roughly consistent with D'Oench, though there were important differences when the statute was compared to the judicial expansion of the D'Oench rule. As enacted in 1950, 12 U.S.C. § 1823(e) did not apply to the FDIC when it acts as receiver of a bank, nor did it apply to the Federal Savings & Loan Insurance Corporation (FSLIC). The legislative history of 12 U.S.C. § 1823(e), however, does not mention D'Oench, prompting the courts interpreting the section to conclude that there was no displacement of the common law by the 1950 amendments. 107

104. Id. at 460. The creation of the D'Oench rule is consistent with the rules regarding the creation of federal common law outlined in the text, supra, accompanying notes 14-19. D'Oench was decided four years after Erie and the Court clearly had that decision in mind when reaching its decision. See id. at 455. The Court first examined the federal interest in protecting the FDIC, and only created a common law rule of decision after determining that the interest was significant. See id. at 456-57.


106. The text of old § 1823(e) was:

No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

12 U.S.C.A. § 1823(e) (West 1989). As enacted, this section imposed strict requirements upon any agreement that might be allowed to defeat the FDIC's interest in an asset of the bank. It is important to note, though, the use of the word "asset." This provides a much broader level of protection to the FDIC than that provided holders in due course under the Uniform Commercial Code. Unlike the federal holder in due course doctrine, the word "asset" does not require a finding of negotiability for the FDIC's interest to be protected. See Resolution Trust Corp. v. Kennelly, 57 F.3d 819, 821 (9th Cir. 1995) (rejecting defendant's argument that the variable interest rate on the note sued upon by the RTC removed negotiability of the note under Pennsylvania law; the court noted that whether or not this was a correct statement of the law, the issue was irrelevant in a D'Oench§ 1823 analysis); see also Randolph v. Resolution Trust Corp., 995 F.2d 611, 614-15 (5th Cir. 1993) (per curiam) (holding it "unnecessary to decide whether these notes are negotiable, as the D'Oench, Duhme doctrine may defeat Plaintiffs [sic] defenses to collection regardless of negotiability"), Adams v. Madison Realty & Dev., Inc., 937 F.2d 845, 855 (3d Cir. 1991) (holding that "section 1823(e) requires only that the RTC have an 'interest' which the alleged agreement could diminish or defeat"; the issue of the holder in due course status of the RTC was therefore irrelevant); Federal Deposit Ins. Corp. v. P.L.M. Intern., Inc., 834 F.2d 248, 255 (1st Cir. 1987) (holding that "section 1823(e) covers nonnegotiable as well as negotiable instruments").

107. See Federal Deposit Ins. Corp. v. McClanahan, 795 F.2d 512, 514 n.1 (5th Cir. 1986) (reasoning that with no mention of D'Oench in the legislative history, "there is no reason to suppose that Congress intended to forbid the rule of estoppel from being applied" in areas the statute did not reach).
After concluding there was no displacement by the 1950 amendment, most courts, until recently, applied 12 U.S.C. § 1823(e) and the common law as two overlapping tools available to the FDIC when it seeks to recover funds due upon notes it has acquired after a bank fails. There are two routes available to the FDIC when it steps in as receiver for a depositary institution after the Comptroller of the Currency has declared that particular institution insolvent.

As receiver, the FDIC manages the assets of the failed bank on behalf of the bank’s creditors and shareholders. In its corporate capacity, the FDIC is responsible for insuring the failed bank’s deposits. Although there are many options available to the FDIC when a bank fails, these options generally fall within the two categories of approaches, either liquidation or purchase and assumption. The liquidation option is the easiest method, but carries with it two major disadvantages. First, the closing of the bank weakens confidence in the banking system. Second, there is often substantial delay in returning funds to depositors.

The preferred option when a bank fails, therefore, is the purchase and assumption option. Under this arrangement, the FDIC, in its capacity as receiver, sells the bank’s healthy assets to the purchasing bank in exchange for the purchasing bank’s promise to pay the failed bank’s depositors. In addition, as receiver, the FDIC sells the ‘bad’ assets to itself acting in its corporate capacity. With the money it receives, the FDIC-receiver then pays the purchasing bank enough money to make up the difference between what it must pay out to the failed bank’s depositors, and what the purchasing bank was willing to pay for the good assets that it purchased. The FDIC acting in its corporate capacity then tries to collect on the bad assets to minimize the loss to the insurance fund. Generally, the purchase and assumption must be executed in great haste, often over-night.

As mentioned above, the original enactment of 12 U.S.C. § 1823(e) only applied when the FDIC executed a purchase and assumption. In this respect, it mirrored D’Oench which was decided after the FDIC had executed a purchase and assumption with Belleville Bank and thus was arguably limited to those situations. The federal courts, however, quickly expanded the common law rule to cover situations omitted by the original statutory language. The federal courts used D’Oench to protect the FDIC from secret agreements even when it was acting in its receivership capacity during a liquidation. The FSLIC has been given

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108. See Motorcity of Jacksonville, Ltd. v. Southeast Bank, 83 F.3d 1317, 1326 n.7 (11th Cir. 1996) (en banc) ("Courts that expanded the D’Oench doctrine often applied the common law and § 1823(e)(1) in tandem, reasoning that ‘the purposes of D’Oench and section 1823(e) were the same, and therefore...the same analysis [applies] regardless of whether the party involved in the case was the FDIC or another federal banking regulator.’ Cases interpreting either common law D’Oench or § 1823(e)(1) were both considered precedent.") (citations omitted) (quoting Baumann v. Savers Fed. Sav. & Loan Ass’n, 934 F.2d 1506, 1515 (11th Cir. 1991)). In the vast majority of cases cited in this comment, the court begins by analyzing 12 U.S.C. § 1823(e)(1) and then applied D’Oench to any remaining issues. See, e.g., Howell v. Continental Credit Corp., 655 F.2d 743 (7th Cir. 1981); Inn at Saratoga Assocs. v. Federal Deposit Ins. Corp., 60 F.3d 78 (2d Cir. 1995).

109. Timberland Design, Inc. v. First Service Bank For Sav., 932 F.2d 46, 48 (1st Cir. 1991) (citations omitted). See also Gunter v. Hutcheson, 674 F.2d 852, 856-66 (11th Cir. 1982) (describing the purchase and assumption transaction and noting that it must be “consummated with great speed”).

D'Oench protection, whether acting in its corporate or its receivership status.\textsuperscript{112} Defenses based upon an improper acknowledgement of a mortgage have been barred, even though under state law the mortgage would have been voidable.\textsuperscript{113} In perhaps the largest extension of the doctrine, some courts have used the policy justifications behind D'Oench to create the federal holder in due course doctrine, giving the FDIC holder in due course status when it takes instruments as part of a purchase and assumption.\textsuperscript{114}

\begin{itemize}
\item \textsuperscript{111} See, e.g., Federal Deposit Ins. Corp. v. Bernstein, 944 F.2d 101 (2d Cir. 1991).
\item \textsuperscript{112} See Federal Sav. and Loan Ins. Corp. v. Two Rivers Assocs, 880 F.2d 1267, 1274-75 (11th Cir. 1989).
\item \textsuperscript{113} See Federal Deposit Ins. Corp. v. McCullough, 911 F.2d 593, 602 (11th Cir. 1990), cert. denied, 500 U.S. 941 (1991). In McCullough, the mortgage was notarized by a notary who was not present at the time of signing. See id. The Eleventh Circuit noted that while "the error in acknowledgement might render the mortgage voidable were this suit involving two private parties litigating under state law," the D'Oench common law rule barred the defense. Id. The mortgage appeared valid on its face, thus preventing bank examiners from knowing of the possible infirmity and implicating D'Oench policy considerations. See id.
\item \textsuperscript{114} See Federal Deposit Ins. Corp. v. Wood, 758 F.2d 156, 161 (9th Cir.), cert. denied, 474 U.S. 944 (1985). Under state law, the FDIC would not normally be entitled to holder in due course status after a purchase and assumption. The Uniform Commercial Code, for instance, exempts from holder in due course status anyone who takes possession of an instrument "(i) by legal process or by purchase in an execution, bankruptcy, or creditor's sale or similar proceeding, (ii) by purchase as part of a bulk transaction not in ordinary course of business of the transferor, or (iii) as the successor in interest to an estate or other organization." U.C.C. § 3-302(c) (1990); see also § 3-302 cmt. 5 (1990) ("[S]ubsection (c) may be preempted by federal law if the Federal Deposit Insurance Corporation takes over an insolvent bank. Under the governing federal law, the FDIC and similar financial institution insurers are given holder in due course status and that status is also acquired by their assignees under the shelter doctrine.").
\end{itemize}

The genesis of the holder in due course doctrine has been traced back to Gunter v. Hutcheson, where the maker of a note sought to rescind it on the basis of fraud and securities law violations. See Gunter v. Hutcheson, 674 F.2d 862 (11th Cir.), cert. denied, 459 U.S. 826 (1982). See also In Re 604 Columbus Ave. Realty Trust, 968 F.2d 1332, 1350-53 (1st Cir. 1992). The Gunter court, noting the need for speed inherent in any purchase and assumption transaction, held that the FDIC should be treated like a holder in due course, thus cutting off the defenses sought to be asserted in this case. It justified its holding by noting that subjecting the FDIC to fraud claims of which it had no knowledge would only inhibit its ability to fulfill what the court saw as a statutory requirement in 12 U.S.C. § 1823(e) to execute a purchase and assumption, as opposed to a liquidation, whenever possible. See Gunter v. Hutcheson, 674 F.2d at 870. It further noted that such a holding, as it merely put the FDIC in the same position as a holder in due course, did not upset note makers' expectations since the holder of the note could always negotiate it to a holder in due course. See id. at 872.

There are important differences between this doctrine and D'Oench. In many respects D'Oench is the broader of the two, particularly as it has been interpreted by the courts and codified by Congress. See supra note 100. As it now stands, it applies to any asset of the bank, whether or not negotiable and whether or not the FDIC is acting in its corporate or its receiver status. See Federal Deposit Ins. Corp. v. P.L.M. Int'l, Inc., 834 F.2d 248, 254 (1st Cir. 1987) (holding that a letter of guaranty was an asset under 12 U.S.C. § 1823(e) and that defenses based on secret agreements were barred whether or not the asset was a negotiable instrument). The federal holder in due course doctrine, however, can only apply to instruments that are negotiable under state law. See Sunbelt Sav., FSB v. Montross, 923 F.2d 353, 356, modified on other grounds by Resolution Trust Corp. v. Montross, 944 F.2d 227 (5th Cir. 1991). Nor have many courts been willing to extend holder in due course protection to the FDIC when it acts as a receiver. See In Re 604 Columbus Ave. Realty Trust, 968 F.2d 1332, 1350-53 (1st Cir. 1992) (holding that, since the underlying rationale of the federal holder in due course doctrine is "to promote purchase and
Likewise, the courts usually adopted, in keeping with the policy concerns that had motivated the original *D’Oench* decision, a broad interpretation of 12 U.S.C. § 1823(e) to add further protection to the FDIC. The section has been applied to bar claims based upon fraud in the inducement, based upon agreements between obligors and third parties, and based upon a letter from a bank official indicating that a trust was irrevocable. Prior to 1987, these broad interpretations were not universally approved. For instance, in *Federal Deposit Insurance Corp. v. Meo*, the Ninth Circuit created an innocent maker exception, holding that the “bank borrower who was neither a party to any deceptive scheme involving, nor negligent with respect to, circumstances giving rise to the claimed defense to his note is not estopped from asserting such defense against the bank’s receiver.” Some courts also held that the term “agreement” in 12 U.S.C. § 1823(e) did not apply to agreements about whether one party was or was not a surety. Other courts held that the diminishment of the FDIC’s interests must be contained in a

assumption transactions,” the doctrine is inapplicable to the FDIC when it is acting as receiver; see also Federal Deposit Ins. Corp. v. Houde, 90 F.3d 600 (1st Cir. 1996); Federal Deposit Ins. Corp. v. Laguarta, 939 F.2d 1231, 1239 n.19 (3rd Cir. 1991). But see, Campbell Leasing, Inc. v. Federal Deposit Ins. Corp., 901 F.2d 1244, 1249 (5th Cir. 1990) (holding federal common law holder in due course rule applicable whether FDIC acting in its corporate or receiver capacity); Firstsouth, F.A. v. Aqua Constr., Inc., 858 F.2d 441, 443 (8th Cir. 1988).

115. See McGlothlin v. Resolution Trust Corp., 913 F. Supp. 15, 17 (D.D.C. 1996) (denying relief to plaintiffs who alleged that they had been fraudulently induced by an agent of the failed bank to sign a promissory note relating to a construction project undertaken by their son’s business; the signatures were gained through oral representations by the agents and those representations were barred under 12 U.S.C. § 1823(e)).


117. See Suzan Tantleff Trusts v. Federal Deposit Ins. Corp., 938 F. Supp. 14 (D.D.C. 1996). The issue in *Suzan Tantleff* concerned the amount of federal insurance available to the beneficiaries of three trusts that had been kept in deposit at the American Commerce National Bank. See id. at 15. When the bank failed, the FDIC examined the trusts to determine whether they were revocable or irrevocable. The decision had a material effect upon the amount of depositary insurance available. See id. at 16. After first determining the trusts were irrevocable and thus eligible for a higher level of insurance, the FDIC reversed itself, pointing to language in the trust that seemed to make the trust revocable. See id. Among other theories, plaintiffs argued that the FDIC should be estopped from determining the trusts were revocable by pointing to a letter sent by one of ACNB’s officers stating that the trusts were irrevocable. See id. at 19. The court held that such an argument was prevented by 12 U.S.C. § 1823(e). See id. at 20.

118. 505 F.2d 790 (9th Cir. 1974).

119. Federal Deposit Ins. Corp. v. Meo, 505 F.2d at 793. The *Meo* decision has been referred to as creating an “innocent borrower exception” to the *D’Oench* rule. See In Re 604 Columbus Ave. Realty Trust, 968 F.2d at 1347-48. A number of courts, referring back to *D’Oench*, have concluded that its plain import was to create a situation where “the borrower’s state of mind is irrelevant, because the ‘proper focus under *D’Oench* is whether the agreement, at the time it was entered into, would tend to mislead the public authority.” Id. at 1348. (quoting Timberland Design v. First Serv. Bank, 932 F.2d 46, 50 (1st Cir. 1991)); see also Baumann v. Savers Fed. Sav. & Loan Assoc., 934 F.2d 1506, 1516 (11th Cir. 1991); Young v. Federal Deposit Ins. Corp., 103 F.3d 1180, 1188 (4th Cir. 1997) (holding that the *Meo* “innocent borrower exception” “conflicts with the underlying rationale of the *D’Oench* doctrine” and was therefore unavailable). Many courts have concluded that the *Meo* analysis was “based on an outdated understanding of the *D’Oench* doctrine,” and did not survive the Supreme Court’s decision in *Langley v. Federal Deposit Ins. Corp.*, 484 U.S. 86 (1987). Federal Sav. & Loan Ins. Corp. v. Gordy, 928 F.2d 1558, 1567 n.14 (11th Cir. 1991).

120. See Federal Deposit Ins. Corp. v. Blue Rock Shopping Ctr., Inc., 766 F.2d 744 (CA 3 1985). The court held that the types of agreements covered by 12 U.S.C. § 1823(e) are those between obligor and bank “showing or attempting to show that the obligation was illusory or conditional.” Id. at 754.
separate agreement; where the defense arises from a bilateral agreement—the defense arising from the breach of that agreement by the FDIC, on its own or as successor in interest—some courts have found that 12 U.S.C. § 1823(e) is not implicated and cannot serve to bar that particular defense. These courts took a very narrow view of the term “agreement” and used it to exclude various situations from protection under the statute.

In 1987, however, the Supreme Court rejected this narrow view of the term “agreement” and brought statutory interpretation closer to the breadth already accorded the common law rule. In *Langley v. Federal Deposit Insurance Corp.*, the Court allowed the use of 12 U.S.C. § 1823(e) to prevent a defense based upon the alleged violation of certain warranties made by the underlying bank regarding a plot of land. The Langleys had purchased land in Louisiana and sought to finance the purchase with a loan from Planters Trust & Savings Bank (Planters). After the Langleys missed a payment on the note, Planters filed suit. This suit was removed to federal court and consolidated with a lawsuit brought by the Langleys against Planters. The Langleys argued that the note had been procured through misrepresentations about the land and the mineral acres present in the tract. Planters was declared insolvent shortly thereafter and the FDIC stepped in as receiver. A purchase and assumption transaction followed in which the FDIC became the possessor of the Langleys’ note. The FDIC was substituted for Planters as plaintiff in the action to recover on the note. After this substitution, the Langleys’ argued that the term “agreement” should be narrowly construed to “encompass[] only an express promise to perform an act in the future.”

In responding to the Langley’s argument, the Court held that the term “agreement” should be taken at its normal meaning, which went beyond simple promises, and that under such a definition, the term could “embrac[e] such a condition upon performance” as a warranty. Moreover, the “leading case in this area prior to enactment of § 1823(e) in 1950,” *D'Oench*, also had adopted a broad view

121. See Howell v. Continental Credit Corp., 655 F.2d 743 (7th Cir. 1981). In Howell the court dealt with a case where there was a bilateral agreement visible on the face of the lease that the bank, Continental Credit Corp., was to purchase certain equipment. When the FDIC sued to recover payments under the lease, Howell raised as a defense the failure of the bank to purchase the equipment. The court noted that the terms that tend to diminish the FDIC’s rights are in the very document which creates those rights, thus 12 U.S.C. § 1823(e) is not implicated because there is no secret agreement separate from the asset that is diminishing the FDIC’s rights in the asset. See id. at 747 (citing Riverside Park Realty Co. v. Federal Deposit Ins. Corp., 465 F. Supp. 305, 313 (M.D. Tenn. 1978)).


123. See id. at 88.

124. See id. at 89.

125. See id. The FDIC had notice of the lawsuit prior to its obtaining the note. See id. Reasoning that “[t]he harm to the FDIC caused by the failure to record occurs no later than the time at which it conducts its first bank examination that is unable to detect the unrecorded agreement and to prompt the invocation of available protective measures, including termination of the bank’s deposit insurance,” the Court denied the Langleys’ argument that the FDIC had knowledge of a defense and that such knowledge should allow the maker to assert that defense. Id. at 95. “An agreement that meets [the requirements of § 1823(e)] prevails even if the FDIC did not know of it; and an agreement that does not meet them fails even if the FDIC knew.” Id.

126. Id. at 90.

127. See id. at 91.
of what an agreement was.\textsuperscript{128} "We can safely assume that Congress did not mean ‘agreement’ in § 1823(e) to be interpreted so much more narrowly than its permissible meaning as to disserve the principle of the leading case applying that term to FDIC-acquired notes."\textsuperscript{129}

The Court also discerned in the statute the twin purposes of allowing the FDIC and other banking authorities to rely upon the written records of the bank and of "ensur[ing] mature consideration of unusual loan transactions by senior bank officials, and prevent[ing] fraudulent insertion of new terms, with the collusion of bank employees, when a bank appears headed for failure."\textsuperscript{130} Based upon these purposes and its broad reading of the word “agreement,” the Court held that 12 U.S.C. § 1823(e) barred almost all defenses based upon an underlying agreement where there was an asset, whether or not the FDIC had knowledge of the agreement.\textsuperscript{131} The Court, however, did leave open the possibility for the maker to assert fraud in the factum as a defense to the obligation on the instrument. In its analysis of this defense, the Court distinguished fraud in the inducement from fraud in the factum and based its distinction upon the question of whether there was an asset left to be diminished.\textsuperscript{132} If a defendant alleged fraud in the factum, that is, a fraud that caused the maker to sign without knowing what it was they were signing, then the instrument would be void, “thus leaving no ‘right, title or interest’ that could be ‘diminish[ed] or defeat[ed].’”\textsuperscript{133} On the other hand, fraud in the inducement merely made the instrument voidable, and a “bank therefore had and could transfer to the FDIC voidable title, which is enough to constitute ‘title or interest’ in the note.”\textsuperscript{134}

\textbf{C. THE 1989 AMENDMENTS}

In 1989 Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA). FIRREA was enacted during the savings and loan crisis and was specifically designed to shore up "public confidence in the savings and loan industry in order to ensure a safe, stable, and viable system of affordable housing finance."\textsuperscript{135} As of the end of 1988, the savings and loan industry had suffered numerous setbacks. Congress found that “[t]he nation’s thrift industry

\begin{itemize}
\item \textsuperscript{128} Id. at 92.
\item \textsuperscript{129} Id. at 92-93.
\item \textsuperscript{130} Id.
\item \textsuperscript{131} See id. at 93.
\item \textsuperscript{132} See id. at 93-94.
\item \textsuperscript{133} Id. Absent compliance with the four-fold requirements of 12 U.S.C. § 1823(e), this appears to be the only defense left after Langley that may be asserted on the basis of oral proof. Despite numerous attempts to use this argument, courts have rarely accepted it, finding in most cases only fraud in the inducement. \textit{See, e.g.,} Federal Deposit Ins. Corp. v. Giammettei, 34 F.3d 51, 59 (2d Cir. 1994) (holding the defendants’ allegations of fraud in the factum instead indicate only fraud in the inducement).
\end{itemize}
and its deposit insurance fund, the Federal Savings and Loan Insurance Corporation are currently in precarious financial condition and consumer confidence in the savings and loan industry is waning." 136 The industry’s "precarious financial condition" was widely known, with numerous newspapers reporting on the problem. In the last months of 1988, it was widely reported that over 500 federally insured thrifts were identified as insolvent. 137 Estimates of the eventual cost of resolving the problem ranged from $50 to $100 billion. 138 Most writers felt that a taxpayer bailout would be necessary, and at least one economist was viewing the crisis as having the potential to create a recession that "could snowball into something much more dangerous because of the big debt buildup and the growing savings and loan and banking crises." 139 Indeed, Congress believed that "[t]he Bank Board and the Reagan Administration continually understated the magnitude of the S&L crisis, effectively delaying its resolution and needlessly adding billions of dollars to the cost of resolving the problem." 140 Moreover, Congress felt that there had been a conflict of interest within the Bank Board which oversaw the FSLIC. "[T]he Bank Board's record of relaxing capital standards and a lack of enforcement actions against thrift operators" had led in part to an escalation of the thrift crisis. 141 There was a widespread belief that the escalating thrift crisis would soon cause the bankruptcy of the FSLIC. 142 FIRREA was meant to address the breakdown and potential collapse of both the Savings & Loan industry and its enforcement arm.

This collapse of the thrifts concerned Congress because it saw the thrift industry as a major way in which funds were made available to home buyers. The thrift industry's purpose had always been to "provide the American people with affordable mortgage credit." 143 Some commentators, concerned about the projected cost of taxpayer assistance to resolve the problem, were urging Congress to enact "sweeping reforms...to prevent a recurrence of the present disaster." 144 Numerous "witnesses, and other experts, [in testifying before Congress had] pointed out the major flaws in our thrift system." 145 There was a concern with the public costs

of the crisis, and an emphasis that “the theme of the Committee’s deliberations” was “Never Again.”

FIRREA was a broad reworking of the FDIC Act that, as noted by the Supreme Court, extensively regulated the FDIC’s rights. The Act was meant to deal with a crisis of national proportions. While it did change the language of 12 U.S.C. § 1823(e), it is not surprising that relatively little of the legislative history discusses that change. There is no affirmative indication that FIRREA was intended to displace the D’Oench common law rule. Instead, Congress “adopted provisions which expand, enhance and clarify enforcement powers of the financial institution regulatory agencies.” In changing the effect of 12 U.S.C. § 1823(e)(1), Congress, for the most part, brought it in line with the existing common law.

FIRREA eliminated the FSLIC and transferred its assets to “the newly-created

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147. See O’Melveny & Myers v. Federal Deposit Ins. Corp., 512 U.S. 79, 86 (1994) (rejecting the argument that FIRREA was a “nonexclusive grant of rights to the FDIC receiver which can be supplemented or modified by federal common law” by listing the several statutory rules of decision which cover the FDIC as receiver).
149. See In re NBW Commercial Paper Litigation, 826 F. Supp. 1448, 1459-60 (D.D.C. 1992) (discussing the lack of legislative history about FIRREA’s changes to 12 U.S.C. § 1823(e) and concluding that there was no intent to preempt D’Oench).
150. The same can be said of the federal holder in due course doctrine. Though Congress knew of the existence of this doctrine, it nowhere indicated an intent that the passage of FIRREA should displace this element of federal common law. Indeed, given the level of concern in Congress and the country about the costs of the crisis and the desire to prevent a recurrence, it would be counterintuitive to imply a congressional purpose to displace two common law rules that quite clearly decrease the amount of money that the FDIC may be able to recover upon the failure of an “insured depository institution.”
152. Amended 12 U.S.C. § 1823(e)(1) reads:
No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—
(A) is in writing,
(B) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,
(C) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and
(D) has been, continuously, from the time of its execution, an official record of the depository institution.
12 U.S.C. § 1823(e)(1) (1994). Subsection (2), which deals with agreements "provid[ing] for the lawful collateralization of deposits of a Federal, State, or local governmental entity or of any depositor referred to in section 1821(a)(2) of this title," was added by amendment in 1994. 12 U.S.C. § 1823(e)(2) (1994). Such agreements “shall not be deemed to be invalid pursuant to paragraph (1)(B) solely because such agreement was not executed contemporaneously with the acquisition of the collateral or with any changes in the collateral made in accordance with such agreement.” Id.
FSLIC Resolution Fund (FRF) to be administered by the FDIC."¹⁵³ Public law 101-73 changed the term "insured bank" to "insured depository institution" wherever it appeared in the Federal Deposit Insurance Act, which included 12 U.S.C. § 1823(e)(1).¹⁵⁴ This change resulted in the extension of the FDIC's powers to cover thrifts, with the exception of any thrifts placed in conservatorship or receivership between January 1, 1989 and December 31, 1995, which were to be resolved by the Resolution Trust Corporation (RTC).¹⁵⁵ FIRREA also extended the protection of this section to assets acquired by the FDIC when it was acting as receiver.¹⁵⁶ Finally, 12 U.S.C. § 1821(d)(9)(A) was added, which made 12 U.S.C. § 1823(e) the exclusive measure of an agreement that might be asserted as "a claim against the receiver or the Corporation."¹⁵⁷ Although the specific purpose behind the changes to § 1823(e)(1) is not clear, a desire to protect the FDIC and to minimize the losses to the corporations in order to resolve the crisis and prevent future problems does emerge.¹⁵⁸

D. The Supreme Court's First Interpretation of FIRREA:
A Refusal To Create New Federal Common Law.

Since the passage of FIRREA, the United States Supreme Court has had two opportunities to rule upon its effect on federal common law. In both cases, the Court was asked to decide the question of whether new federal common law could be created, a question that the Court answered in the negative. Significantly, in neither case was FIRREA's effect upon established federal common law before the court.

1. O'Melveny & Myers v. Federal Deposit Insurance Corp.:
The Supreme Court Rejects an Appeal for New Federal Common Law.

In 1994, O'Melveny & Myers v. Federal Deposit Ins. Corp.¹⁵⁹ reached the Supreme Court. In O'Melveny & Myers, the American Diversified Savings Bank


¹⁵⁷. Section 1821(d)(9)(A) states: "Except as provided in subparagraph (B), any agreement which does not meet the requirements set forth in section 1823(e) of this title shall not form the basis of, or substantially comprise, a claim against the receiver or the Corporation." 12 U.S.C. § 1821(d)(9)(A) (1994).

¹⁵⁸. The changes made to 12 U.S.C. § 1823(e) in combination with the addition of 12 U.S.C. § 1821(d)(9)(A) are consistent with a desire to protect the FDIC and to minimize future losses. When compared to the earlier statute, the two sections expand the protection given the FDIC when it acquires assets following a bank failure.

(ADSB), a federally insured savings and loan, had gone into receivership to the FDIC in February 1986. ADSB had been acquired in 1983 by two investors who had caused the thrift to "engage[] in many risky real estate transactions, principally through limited partnerships sponsored by ADSB and its subsidiaries." These transactions formed both the basis for this suit and the basis for the declaration of insolvency that resulted in ADSB going into receivership. The particular real estate transactions underlying the issue in this case had begun in September 1985, when O'Melveny & Myers, a "Los Angeles-based law firm, represented ADSB in connection with two real estate syndications." These transactions proved to be not quite what they seemed, and shortly after the FDIC stepped in as receiver, investors besieged the receiver with demands for refunds, claiming that they "had been deceived in connection with the two real estate syndications." The FDIC brought suit against O'Melveny & Myers, claiming professional negligence and breach of fiduciary duty. The law firm sought summary judgment, which was granted by the District Court but reversed by the Ninth Circuit.

The Supreme Court, in taking the case, first noted that the FDIC's causes of action were all created by California law. The issue before it, then, was whether (1) a federal common-law rule and not California law determines whether the knowledge of corporate officers acting against the corporation's interest will be imputed to the corporation; and (2) even if California law determines the former question, federal common law determines the more narrow question whether knowledge by officers so acting will be imputed to the FDIC when it sues as receiver of the corporation.

The Court declined to extend federal common law in either case. The first question, the Court reasoned, was "plainly wrong," because there was "no federal general common law," and "the remote possibility that corporations may go into federal receivership is no conceivable basis for adopting a special federal common-law rule divesting States of authority over the entire law of imputation." The second question took up the bulk of the Court's analysis.

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161. Id. at 81.
162. See id. at 81-82. The regulators concluded that ADSB had "incurred substantial losses because of violations of law and unsound business practices." Id.
163. Id. at 81.
164. Id. at 82.
165. See id.
166. The district court granted the motion for summary judgment after argument that the claims asserted by the FDIC would be barred by California law and that the FDIC, as receiver, stood in the shoes of the failed bank. See Federal Deposit Ins. Corp. v. O'Melveny & Meyers, 969 F.2d 744, 747 (9th Cir. 1992). The Ninth Circuit reversed, holding "[i]t is by now clear beyond doubt that federal, not state, law governs the applications of defenses against the FDIC." Id. at 751. The circuit court then "fashion[ed] a federal rule of decision" that prevented O'Melveny & Myers from making an estoppel argument. See id. Reasoning that a receiver does not voluntarily step into the shoes of the bank as a normal successor in interest would, the court ruled that federal common law required that "equitable defenses good against a bank do not carry over against the bank's receiver." Id.
168. Id.
169. Id.
The Court framed the second question in terms of whether the California law was displaced or could be displaced by federal law and, if it were displaced, then what governmental entity should order the displacement.

In answering the central question of displacement of California law, [the Court] of course would not contradict an explicit federal statutory provision. Nor would [the Court] adopt a court-made rule to supplement federal statutory regulation that is comprehensive and detailed; matters left unaddressed in such a scheme are presumably left subject to the disposition provided by state law.\(^{170}\)

The Court agreed that the passage of FIRREA demonstrated a high level of federal interest in this area, but noted that the statute explicitly stated in 12 U.S.C. § 1821(d)(2)(A)(i) that the FDIC, when acting as receiver, “shall...by operation of law, succeed to—all rights, titles, powers, and privileges of the insured depository institution...”\(^{171}\) When combined with several other provisions within the statute that explicitly allowed the FDIC to escape the action of state law, the Court concluded that the statute intended to place “the FDIC in the shoes of the insolvent S&L, to work out its claims under state law, except where some provision in the extensive framework of FIRREA provides otherwise.”\(^{172}\) Section 1821 (d)(2)(A)(i) was not such a provision and there was consequently no displacement of the California law of imputation.

The Court, however, did not end its analysis with the conclusion that FIRREA prevented the creation of new federal common law. Noting that the FDIC took over as receiver in 1986 and that FIRREA was not passed until 1989, the Court concluded that even absent FIRREA, this was not a situation in which new federal common law should be created.\(^{173}\) The FDIC was unable to identify to the Court’s satisfaction any “significant conflict with an identifiable federal policy or interest.”\(^{174}\) The FDIC had put forth two arguments for the displacement of California law: first, that “state rules regarding the imputation of knowledge might ‘deplet[e] the deposit insurance fund,’” and second, that “it would ‘disserve the federal program’ to permit California to insulate ‘the attorney’s or accountant’s malpractice,’ thereby imposing costs ‘on the nation’s taxpayers, rather than on the negligent wrongdoer.’”\(^{175}\) The Court rejected the first argument as overly broad because FIRREA did not state an anticipated level of the fund.\(^{176}\) The Court reasoned that without a set level for the fund, the only principle which would justify the FDIC’s logic must be that it was a federal policy to prevent any depletion of the fund.\(^{177}\) Characterizing this as a “federal policy that the fund should always win,” the Court refused to endorse it.\(^{178}\) The second argument was similarly rejected as a “demonstration of the runaway tendencies of ‘federal common law’ untethered to a genuinely identifiable (as opposed to a judicially constructed) federal policy.”\(^{179}\)


\(^{171}\) Id. at 86 (quoting 12 U.S.C. §1821(d)(2)(A)(i) (1994)).

\(^{172}\) Id. at 87.

\(^{173}\) See id.

\(^{174}\) Id. at 87.

\(^{175}\) Id. at 88-89 (quoting Brief for Respondent, 32).

\(^{176}\) See id. at 88.

\(^{177}\) See id.

\(^{178}\) Id.

\(^{179}\) Id. at 89.
The Court then reversed the judgment of the Ninth Circuit finding a federal common law rule of decision and remanded the case for a resolution of the imputation issues under California law. 180

2. Atherton v. Federal Deposit Ins. Corp.: Erie Employed

A similar issue surfaced in 1997 when the Supreme Court decided Atherton v. Federal Deposit Ins. Corp. 181 In Atherton, the Resolution Trust Corporation (RTC) had sued officers and directors of City Federal Savings Bank (City Federal), claiming that those officers and directors “had violated the legal standard of care they owed that federally chartered, federally insured institution.” 182 The RTC alleged that the actions of these officers and directors had led to a series of bad loans being underwritten by City Federal and that “these actions (or omissions) were unlawful because they amounted to gross negligence, simple negligence, and breaches of fiduciary duty.” 183 The District Court had dismissed the simple negligence and fiduciary duty claims in reliance upon 12 U.S.C. § 1821(k) which established, in its view, a gross negligence duty of care for officers and directors of a federally insured savings institution. 184 The Third Circuit agreed with the import of the statute, but reversed nonetheless, arguing that there was still a federal common law cause of action available outside of the statute which would allow the RTC to proceed on its simple negligence and breach of fiduciary duty claims. 185

Although the Supreme Court recognized that it had once created federal common law rules to govern the duty of officers and directors of federally insured banks, the Court held that these rules had not survived Erie. 186 Consequently, the question presented by this case, in the Court’s view, was whether this was one of the “few and restricted” cases where a court-created federal rule of decision would be justified to supplement the statutory scheme. 187 After acknowledging that this was an area where Congress had the power to legislate, the Court found only a weak federal need for a common law rule to supplement the statutory scheme. 188 The RTC based its major arguments for a federal common law standard of care primarily upon the ground that the banks affected were federally chartered. This alone should supply the reason for the creation of a common law rule, 189 and if it did not, then the federal interest in uniformity 190 should provide the justification. The Court rejected the RTC’s arguments, particularly the arguments based upon

180. See id.
182. Id. at 215.
183. Id. at 216.
184. See id.
185. See id. at 217 (citing Briggs v. Spaulding, 141 U.S. 132 (1891)).
186. See id.
188. See id. at 219.
189. See id. at 221.
190. See id. at 219-20. The Court rejected this argument, noting that of the federally insured banks, only half were federally chartered; any rule that created uniformity for those banks would create a disparity between them and the state chartered banks. See id. at 220.
the federally chartered nature of the banks, and refused to create new common law.191 The Court based its decision on the conclusion that, if there were threats to federal interests, they were not strong enough to warrant use of the judiciary's common law power.192

IV. THE REFUSAL TO CREATE NEW FEDERAL COMMON LAW CREATES A RIFT IN THE CIRCUITS WITH RESPECT TO ESTABLISHED FEDERAL COMMON LAW.

Since O'Melveny & Myers, the Circuit Courts have been faced with questions concerning the continued vitality of D'Oench and the federal holder in due course common law rules following the passage of FIRREA. Though it could be argued that O'Melveny & Myers is not the correct precedent, the D. C. Circuit, in Murphy v. Federal Deposit Ins. Corp.,193 and the Eighth Circuit, in DiVall Insured Income Fund Ltd. Partnership v. Boatmen's First Nat'l Bank,194 have used the case and its gloss on the statute to justify the destruction of these common law rules.

A. Murphy and DiVall: Established Common Law Is Displaced by the Combination of FIRREA and O'Melveny & Myers.

In Murphy, the Court was faced with an investor who sought damages against the FDIC on the theory that the failed bank insured by the FDIC was responsible for the investor’s loss in an unsuccessful real estate venture.195 Murphy had entered into an investment in the Orchid Island Associates Limited Partnership (Orchid Island) by paying $515,000.00 for a “partnership unit.”196 The partnership was in the process of developing the Orchid Island Golf and Beach Club in Florida and Murphy was guaranteed in the investment contract that he would receive a “6.1 multiple return on investment.”197

The FDIC became involved in this action when its insured bank, Southeast Bank, N.A., failed in the 1990’s.198 Southeast Bank had loaned $50,000,000.00 to the Orchid Island partnership in the 1980’s and 1990’s, and had given the partnership a “bridge loan” in order for the partnership to cover operating expenses while it sought to engage in a public bond offering to finance the completion of the Golf and Beach Club.199 The latter loan, though, was supposed to create a lien on the property superior to that of the other lenders.200 As a result, those lenders rejected the bond proposal, Orchid Island defaulted upon its loans, and Southeast foreclosed upon the property.201 Southeast then itself became insolvent, and the FDIC was appointed receiver.202 Murphy sued, seeking to recover for the failure of his investment.203

191. See id. at 221-23. The Court went on to analyze the effect of FIRREA on state law and concluded that FIRREA set a “floor—a guarantee that officers and directors must meet at least a gross negligence standard. It [did] not stand in the way of a stricter standard that the laws of some States provide.” Id. at 674.
192. See id. at 225.
193. 61 F.3d 34 (D.C. Cir. 1995).
194. 69 F.3d 1398 (8th Cir. 1995).
195. See Murphy v. Federal Deposit Ins. Corp., 61 F.3d at 35.
196. See id.
197. Id. at 35.
198. See id.
199. See id.
200. See id.
201. See id.
202. See id.
203. See id.
Foundationally, Murphy's claims against the FDIC were premised upon the idea that Southeast Bank had control over Orchid Island and in so doing, had attained the status of partner or joint venturer. Murphy sought money damages and an order to require the FDIC to give him certain accounting statements. The district court, in granting the FDIC's motion for summary judgment on Murphy's claims, relied upon 12 U.S.C. § 1823(e)(1) and D'Oench to justify its decision. The court denied Murphy's claims, reasoning that the written language in the contracts between Southeast and Orchid Island specifically stated that Southeast would not be considered a partner or joint venturer. Moreover, Murphy had failed to point to a written agreement contradicting this plain language.

In reversing the district court's judgment, the D. C. Circuit went through a two part analysis. It first examined 12 U.S.C. § 1823(e)(1) and 1821(d)(9)(A) and concluded that,

> [b]y their terms, these statutory provisions bar any claim that (1) is based upon an agreement that is either (a) unwritten or (b) if in writing, does not meet the stringent requirements of §§ 1823(e)(1)(B)-(D), and (2) would diminish or defeat the interest of the FDIC in an asset acquired by it in its capacity as receiver of a failed depository institution.

The court then concluded that Murphy's claims were not barred by statute because they were not related to any specific asset. Murphy's allegations only defeated the FDIC's interest in the whole value of Southeast Bank. They did not prevent the FDIC from collecting in full on the particular loan given to Orchid Island and therefore, the court reasoned, there was no diminution of any specific asset as required by 12 U.S.C. § 1823(1)(e).

In the second part of its analysis, the D.C. Circuit concluded that the Supreme Court's reasoning in O'Melveny & Myers "appears to leave no room for a federal common law D'Oench doctrine...." Although it noted that D'Oench was not specifically mentioned in the Supreme Court's opinion, the court went on to state that "the Supreme Court appears to have concluded that the Congress in the FIRREA did indeed address the question previously governed by D'Oench. It follows that the need for a body of federal common law under the rubric of D'Oench has now 'disappeared'...." The D. C. Circuit therefore concluded that the only way for

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204. See id. From this premise, Murphy charged in several counts that Southeast, and therefore the FDIC, was liable for the wrongdoing of the partnership, including failure to register securities, unlawful offer and sale of securities, breach of fiduciary duties, breach of contract, and accounting improprieties. See id. In addition, Murphy contended that Southeast itself had engaged in wrongdoing in connection with this project, specifically fraud and negligent misrepresentation. See id. at 36.

205. See id. at 36.

206. See id.


210. See id. at 37.

211. Id. at 39.

212. Id. at 40. In holding the common law inapplicable, the court specifically rejected several arguments put forward by the FDIC against reading O'Melveny & Myers so broadly. The court rejected the argument that D'Oench had not even been considered by the Supreme Court by noting that both sides had raised the question of the possible effects on D'Oench in their briefs and at oral argument. See id. at 39. It rejected the argument that Langley had already dealt with the preemption question and had not found displacement by noting that Langley was a pre-FIRREA decision and that even then the Supreme Court had intimated that D'Oench was
the FDIC to successfully bar Murphy's claims was through the action of the statute; because the court had concluded that 12 U.S.C. § 1823(e)(1) was no bar, Murphy could survive the motion for summary judgment. The court remanded the case to the district court.

*Murphy* has not been widely used.\(^{213}\) It has been mentioned in a number of opinions, most only noting that the court is not called upon to decide the question raised by *Murphy*.\(^ {214}\) In *DiVall Insured Income Fund, L.P. v. Boatmen's First National Bank*,\(^ {215}\) however, the Eighth Circuit invoked *Murphy* in its decision that the federal holder in due course doctrine was displaced by FIRREA.\(^ {216}\) *DiVall* concerned an action for declaratory judgment in which *DiVall* sought a ruling that it was not liable upon a promissory note that Boatmen's First National (Boatmen's) had acquired from the FDIC.\(^ {217}\) The note had been issued to *DiVall* by Metro North State Bank (Metro) and had been executed by the two general partners of *DiVall*.\(^ {218}\) The note was executed in favor of Metro to provide *DiVall* with working capital and the bank was authorized in the loan agreement to make advances on the loan by wire transfer.\(^ {219}\) The bank
later did make such advances, but they were wired to an account that was in the name of DiVall Reserves but that was not for the benefit of DiVall. Though payments were made on the note, they were not made by DiVall.

Boatmen's acquired the note in late 1992 as part of a purchase and assumption executed by the FDIC after Metro was declared insolvent and went into receivership. Shortly thereafter, the note went into default and Boatmen's demanded payment from DiVall. DiVall instituted this action to get a judgment that the note was unenforceable due to lack of consideration. Boatmen's moved for dismissal, which was treated and granted by the district court as a motion for summary judgment. The district court reasoned that *D'Oench* and 12 U.S.C. § 1823(e)(1) were inapplicable because DiVall's defense did not rest upon an unwritten agreement. It further held that under Missouri law, the note at issue here was not a negotiable instrument. Even so, Boatmen's was held to have the protection of a holder in due course because of the federal common law holder in due course rule and the shelter principle. As a holder in due course, the defense of lack of consideration could not be asserted by DiVall.

On appeal, the Eighth Circuit reversed. The court based its decision upon the Supreme Court's decision in *O'Melveny & Myers* and the D.C. Circuit's decision in *Murphy*, and ruled that the federal holder in due course doctrine had been preempted by the passage of FIRREA. The court then disposed of Boatmen's motion by noting that, first, the bank could not be a holder in due course because the note had a variable interest rate and under Missouri law was not a negotiable instrument. Second, DiVall's defense of a lack of consideration was not foreclosed by 12 U.S.C. § 1823(e)(1) because it referred back to a written agreement, namely the agreement to wire funds as advances on the loan. The court then remanded for trial on the merits of DiVall's defense to the note.

**B. Motorcity of Jacksonville, Ltd v. Southeast Bank: the Eleventh Circuit Distinguishes *O'Melveny & Myers*.**

Not all of the circuit courts have been willing to find displacement by the passage of FIRREA. The Eleventh Circuit, in particular, refused to follow *Murphy*.

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220. See id.
221. See id.
222. See id. at 1399-1400.
223. See id. at 1400.
224. See id.
225. See id.
226. See id.
227. See id.
228. See id. at 1400. The shelter principle allows a transferee such as Boatmen's to assert all of the rights against the maker that the transferor could have asserted. Thus, a transferee from a holder in due course would be able to assert the rights of a holder in due course. See id. at 1400 n.4; U.C.C. § 3-203(b). There is an argument that the *DiVall* court never needed to reach the issue of displacement because the federal holder in due course rule was inapplicable. Several circuits have held that there must first be a negotiable instrument before the FDIC can be a holder in due course. See supra note 111.
230. See id. at 1403.
231. See id. at 1404.
232. See id.
when it decided Motorcity of Jacksonville, Ltd. v. Southeast Bank. Motorcity arose out of a loan agreement between Motorcity of Jacksonville, Ltd. (Motorcity), a car dealership, and Southeast Bank (Southeast). Motorcity alleged that when they approached the bank to obtain financing for the dealership, the investors told the bank that they had no experience in running a dealership. Southeast allegedly replied that this did not present a problem and that “the bank ‘knew what it was doing.’” Both parties discussed their concern about “out of trust” sales. As part of the agreement, Southeast was given the power to audit Motorcity; monthly audits were conducted, eventually resulting in the discovery that a pattern of out of trust sales was occurring at the dealership. Though Southeast sent summaries of these audits to Motorcity, the bank never informed the dealership of the out of trust problem. When Motorcity hired a new general manager in February of 1989, it learned that the lower level managers were using the sales proceeds to pay themselves unearned bonuses. At that point, Motorcity was $400,000 out of trust; when Motorcity notified Southeast of this situation, the bank demanded payment of the full $400,000. Motorcity was unable to comply, and Southeast took possession of the collateral, which included both the dealership itself and $375,000 in certificates of deposit.

This suit was begun by Motorcity in Florida state court, alleging breach of fiduciary duty, breach of oral contract, and negligence. Before trial, however, Southeast was declared insolvent by the Comptroller of the Currency, and the FDIC stepped in as receiver. Motorcity substituted the FDIC, which then removed the action to federal court. After Motorcity amended its complaint to state only a claim for breach of written contract, the district court granted the FDIC’s motion to dismiss. The court also refused to grant Motorcity leave to amend its complaint to reincorporate the state tort claims, reasoning that D’Oench and 12 U.S.C. § 1823(e)(1) would prevent the dealership from stating a claim and that “[t]he genesis of this action is the Southeast floor plan financing agreement, whose written provisions do not support a breach of contract claim against the FDIC. No amount of artful pleading, including further amendments to the complaint, can alter this result.” On appeal, a three judge panel of the court of appeals reversed, holding that “Motorcity’s state law tort claims for negligence and for breach of fiduciary duty were free standing torts, not barred by the D’Oench doctrine.”

233. 83 F.3d 1317 (11th Cir. 1996) (en banc).
234. Id. at 1322.
235. “Out of trust” means that the money paid to purchase a car was not used to pay off the loan the bank had made the dealership to purchase the car; such a practice, if “[c]ontinued unchecked...could pose a threat to a dealership’s financial viability.” Id.
236. See id.
237. See id.
238. See id.
239. See id.
240. See id.
241. See id.
242. See id.
243. Motorcity of Jacksonville, Ltd. v. Southeast Bank, 83 F.3d 1317, 1323 (11th Cir. 1996) (en banc) (quoting from the district court opinion) (internal quotations omitted).
244. Id.
The FDIC's petition for an *en banc* hearing was granted and on rehearing, the Eleventh Circuit upheld the district court, ruling in the process that *D'Oench* and its line of cases had not been displaced by the passage of FIRREA.\(^{245}\)

The Eleventh Circuit reasoned that *O'Melveny & Myers* was not the correct precedent and that instead, it would rely on *United States v. Texas*.\(^{246}\) According to the Eleventh Circuit, *Texas* meant that Congress legislates against a background of federal common law, and established common law principles would remain absent an evident purpose to the contrary.\(^{247}\) The court, however, in surveying the available legislative history, was unable to discover any such purpose.\(^{248}\) Instead, the court felt that

the history of the interaction between the *D'Oench* common law and the statute strongly indicates that Congress did not intend preemption. The statute at issue began in 1950 as a partial codification of the *D'Oench* case. Subsequently, just as the *D'Oench* decision itself was a common law rule fashioned to fill the interstices of federal statutes, courts continued to apply the common law *D'Oench* doctrine beyond the confines of the statutory language in order to fulfill Congress' purposes in enacting § 1823(e)(1). Thereafter, in the intervening forty years, the common law *D'Oench* doctrine and the cases under the statute evolved together, each drawing upon the other.\(^{249}\)

The court concluded that it was "even clearer in this case than in *Texas* that Congress did not intend to preempt the prior federal common law *D'Oench* doctrine."\(^{250}\) The Eleventh Circuit characterized the purpose of FIRREA as "to enhance the FDIC's ability to address the problems created by the increasing number of financial institutions in default."\(^{251}\) Any contrary finding would undermine the purposes of FIRREA by making it more difficult for the FDIC to address the problems surrounding the default of a financial institution.\(^{252}\)

Once the court found that 12 U.S.C. § 1823(e)(1) did not displace *D'Oench*, it turned to Motorcity's arguments. Motorcity attempted to argue that the oral agreements it relied upon to prove its tort claims against Southeast (and thus the FDIC) were not barred by 12 U.S.C. §§ 1823(e)(1) and 1821(d)(9)(A) because it had repaid its loan to the bank. As a result, if it were successful in prosecuting its claims, there would be no impairment of the FDIC's interest in a specific asset because it had repaid its loan to the bank. As a result, if it were successful in prosecuting its claims, there would be no impairment of the FDIC's interest in a specific asset as required by 12 U.S.C. § 1823(e)(1).\(^{253}\) Because 12 U.S.C. § 1823(e)(1) had not displaced *D'Oench*, the court found that it did not need to reach the substance of Motorcity's claims.\(^{254}\) Even if they were outside the statutory scope, *D'Oench* was not limited to barring oral agreements relating to specific assets and thus ap-

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245. *See id.* at 1345.
246. 507 U.S. 529 (1993); *see also supra* notes 71-81 and accompanying text.
248. *See id.* at 1332.
249. *Id.* at 1333.
250. *Id.*
251. *Id.*
252. *See id.* at 1333.
253. *See id.* at 1334.
254. The court specifically declined to address the statutory construction argument in *Murphy* that the combination of 12 U.S.C. §§ 1823(e)(1) and 1821(d)(9)(A) mandated that agreements that did not diminish the FDIC's interest in a specific asset were outside the statutory scheme. *See id.* at 1334.
The mere repayment of a loan did not remove oral agreements from D'Oench's scope. Indeed, to do so would seriously undermine the policies of the D'Oench doctrine: to protect the bank examiners who rely on the bank's records in assessing the bank's condition, to protect the FDIC's ability to insure deposits, and to place the burden on borrowers to make sure that all of the terms of their loan agreements are in writing.

The Eleventh Circuit concluded its analysis by determining that Motorcity's arguments, even those sounding in tort, were based upon oral agreements. Without such agreements, no action could be maintained against the FDIC under state law. The Eleventh Circuit affirmed the trial court's denial of Motorcity's motion to file a second amended complaint.

255. See id. at 1334-35.
256. Id. at 1335.
257. See id. at 1338.
258. See Motorcity of Jacksonville, Ltd. v. Southeast Bank, 83 F.3d 1317, 1340 (11th Cir. 1996) (en bane) ("The written financing agreement gave Southeast the right to audit. The mere conduct of that audit and sending a summary report thereof to Motorcity were entirely consistent with its role as lender. We readily conclude that no fiduciary duty was created under Florida law."); at 1342-43 (holding that Motorcity's negligence claims were also barred because "the Florida case law would imply a tort duty only when actions are undertaken for the benefit of another. It would be inconsistent with well-established Florida law to infer a tort duty merely on account of actions undertaken pursuant to the protection of one's own interests."); and at 1343-44 (holding that the negligence claim is also barred by Florida's economic loss rule which requires that "a purchaser of services may not recover purely economic losses in tort unless the other party's conduct establishes a 'tort distinguishable from or independent of [the] breach of contract'"')(quoting AFM Corp. v. Southern Bell Telephone & Telegraph Co., 515 So.2d 180, 181 (Fla. 1987).
259. See Motorcity of Jacksonville, Ltd. v. Southeast Bank, 83 F.3d at 1344. Since the Eleventh Circuit's en banc decision, Motorcity's petition for certiorari was granted and the Supreme Court vacated the judgment and remanded the case for further consideration in light of its decision in Atherton v. Federal Deposit Ins. Corp. See Hess v. Federal Deposit Ins. Corp., 519 U.S. 1087 (1997). On remand, the Eleventh Circuit concluded that Atherton never addressed the question of whether longstanding federal common law was displaced by FIRREA. See Motorcity of Jacksonville v. Southeast Bank, 120 F.3d 1140, 1143-44 (11th Cir. 1997). Instead, Atherton dealt with pre-Erie cases that the Supreme Court had ruled had not survived Erie. See id. As a result, the Eleventh Circuit reasoned that "the Court obviously never reached or addressed any issue of statutory abrogation of federal common law." Id. at 1143. D'Oench, on the other hand, was decided after Erie, leading the court to decline to accept Motorcity's invitation to overrule D'Oench. With the D'Oench doctrine safely in place as a long-standing federal common law rule, we conclude that the appropriate analysis for the statutory abrogation issue presented in this case is that articulated in United States v. Texas and not that articulated in Atherton and O'Melveny.
Id. at 1144. The court then reinstated both the "en banc opinion published at 83 F.3d 1317," and the "judgment affirming the district court's judgment granting the FDIC's motion to dismiss." Id. at 1145. Motorcity has since filed its petition for certiorari to review the reinstated judgment. See Hess v. Federal Deposit Ins. Corp., 120 F.3d 1140 (11th Cir. 1997), petition for cert. filed, 66 U.S.L.W. 3435 (December 18, 1997) (No. 97-1025). The Supreme Court denied the petition on April 27, 1998. See Hess v. Federal Deposit Ins. Corp., 118 S.Ct. 1559 (1998).
V. THE ELEVENTH CIRCUIT'S MOTORCITY DECISION PROVIDES THE CORRECT RESULT, BOTH SUBSTANTIALLY AND PROCEDURALLY.

The conflict between the circuits created by the Murphy and Motorcity decisions involves more than the question of the FDIC's rights when it acquires an asset after the failure of one of its insured savings institutions. These cases deal with the more fundamental procedural issue of displacement of established federal common law. As such, any rule adopted to deal with the specific issue in Motorcity or Murphy will have ramifications beyond the commercial realm. In its inappropriate reliance upon O'Melveny & Myers, Murphy stands for the proposition, implicit throughout its analysis, that, when faced with a comprehensive statute, federal courts must presume displacement of established federal common law. As previously discussed, this rule upsets established Supreme Court precedent and is likely to result in the disruption and frustration of congressional policies.

A. The Specific Issue in Murphy is Covered by the Statute.

Perhaps the central irony in the D. C. Circuit’s Murphy decision, particularly when considering its potential far reaching consequences, is that the court did not need to find that Murphy's claims were outside the statute. When Congress legislates in an area already occupied by the federal common law, a basic assumption must be that, absent a contrary intention, the statute should be interpreted in such a way so that it is consistent with established common law rules: “The Court has admonished that statutes will not be construed in derogation of the common law unless such an intent is clear.” This version of common law involves the interpretation or gloss to be placed upon a statute and as such is qualitatively different from the “pure” common law rule involved in cases such as D'Oench. “[T]he authority to construe a statute is fundamentally different from the authority to fashion a new rule or to provide a new remedy which Congress has decided not to adopt.” No new rule of decision is being created by the courts; rather, they are using the existing common law as a guide to demonstrate the proper effect of the statute. As the Court stated in Isbrandtsen Co. v. Johnson:

260. The substantive question presented by these cases is a weighty one. Although the banking crisis of the late eighties and early nineties has largely been resolved, at least in part, by a robust economy, this resolution should not prevent concern about the possible effects of a recurrence. The statutory and common law protection of the FDIC discussed in this Comment directly affects the cost to that corporation, and by extension to the taxpayer, of any rescue of an insolvent institution. The more defenses that may be raised against the FDIC when it acts either in its corporate or receivership capacity to resolve a defunct savings institution, the more expensive the cost of that resolution will be. While savings to the FDIC in individual cases might be small, in a large crisis, these small savings could become substantial.

261. Milwaukee v. Illinois, 451 U.S. 304, 339 n.8 (1981) (Blackmun, J. dissenting) (citing Isbrandtsen Co. v. Johnson, 343 U.S. 779, 783 (1952)). See also Graham v. John Deere Co., 383 U.S. 1, 17, 19 (1966) (holding that § 103 of the Patent Act was a “codification of judicial precedents embracing” the prior federal common law and rejecting, for that reason, an argument urging the Court to “find in § 103 a relaxed standard, supposedly a congressional reaction to the ‘increased standard’ applied by this Court in its decisions over the last 20 or 30 years,” instead noting that the statute created “no change in the general strictness with which the overall test is to be applied”).


263. 343 U.S. 779 (1952).
Statutes which invade the common law...are to be read with a presumption favoring the retention of long-established and familiar principles, except when a statutory purpose to the contrary is evident. No rule of construction precludes giving a natural meaning to legislation like this that obviously is of a remedial, beneficial and amendatory character.\textsuperscript{264}

The Supreme Court approved this approach with regard to the \textit{D'Oench} decision when it stated in \textit{Langley} that the statutory language should be construed so as not "to disserve the principle" of \textit{D'Oench}.\textsuperscript{265} In its decision to abrogate \textit{D'Oench}, the \textit{Murphy} court relied only upon the fact that FIRREA was a comprehensive statute; it did not find that there was congressional intent to read the statute inconsistently with the established common law.\textsuperscript{266}

The \textit{Langley} directive is thus still applicable. An application of this principle in this case, then, leads to the conclusion that the specific facts at issue in both \textit{Motorcity} and \textit{Murphy}, though not in \textit{DiVall}, do not require the court to reach the displacement issue at all. The \textit{Murphy} court began its discussion by examining the interplay between 12 U.S.C. §§ 1823(e)(1) and 1821(d)(9)(A).\textsuperscript{267} It concluded that these two provisions imposed a requirement that all agreements asserted against the FDIC could only be barred under the statute if it were shown that the agreements, whether written or unwritten, "would diminish or defeat the interest of the FDIC in an asset acquired by it in its capacity as receiver of a failed depository institution."\textsuperscript{268} The \textit{Murphy} agreement thus escaped the statute because it was a general claim against the savings institution and was therefore unrelated to a specific asset held by the FDIC.\textsuperscript{269} This interpretation of the interplay between the two statutory sections clearly "disserve[s] the principle" of \textit{D'Oench}.\textsuperscript{270} The operative fact in the original \textit{D'Oench} decision as well as in the cases that followed it was the existence of a secret agreement that had the effect of deceiving the banking authorities.

The test is whether the note was designed to deceive the creditors or the public authority or would tend to have that effect. It would be sufficient in this type of case that the maker lent himself to a scheme or arrangement whereby the banking authority on which respondent relied in insuring the bank was or was likely to be misled.\textsuperscript{271}

The \textit{Murphy} court implicitly acknowledged it had not read the statute consistently with \textit{D'Oench} when it considered the displacement issue; displacement need not have been determined if \textit{D'Oench} were inapplicable.

It would not matter that the \textit{Murphy} court's gloss on the interaction between these two statutes is inconsistent with \textit{D'Oench} if its gloss were the only logical reading. It is possible, however, to read these two sections so that they do in fact bar the claims asserted by both \textit{Murphy} and \textit{Motorcity}. 12 U.S.C. § 1821(d)(9)(A) prevents the assertion of any claim that does not meet the requirements of 12 U.S.C. § 1823(e)(1),\textsuperscript{272} while the first part of § 1823(e)(1) reads: "No agreement which

\textsuperscript{264.} Id. at 783.


\textsuperscript{266.} See \textit{Murphy v. Federal Deposit Ins. Corp.}, 61 F.3d 34, 39 (D.C. Cir. 1995).

\textsuperscript{267.} See id. 36-38.

\textsuperscript{268.} Id. at 36.

\textsuperscript{269.} See id. at 37.


tends to diminish or defeat the interest of the Corporation in any asset acquired by it...shall be valid against the Corporation unless such agreement...."273 This introduction can be read to impose a fifth requirement upon agreements that may be asserted against the FDIC. Not only must an agreement be (A) in writing, (B) executed contemporaneously with the acquisition of the asset, (C) approved by the board of directors or loan committee of the savings institution, and (D) continuously in the official records of the institution, but it must also "diminish or defeat" a specific asset acquired by the FDIC.274 Any agreement that does not relate to a specific asset, like a breach of fiduciary duty or similar tort claim, could not fall under 12 U.S.C. § 1823(e)(1). Such an agreement would be an "agreement which does not meet the requirements set forth in section 1823(e) of this title" and therefore "shall not form the basis of, or substantially comprise, a claim against the receiver or the Corporation."275

This reading brings the statute in line with the purpose of D'Oench by making it more difficult for secret agreements to be successfully asserted against the FDIC. It is likely that this would also serve the congressional purpose behind FIRREA. The Murphy reading creates a loophole that, absent the common law, makes it easier for the FDIC to be held liable under state law for the malfeasance of insured savings institutions.276 When FIRREA was passed, Congress was concerned with the potential bankruptcy of one insurance fund, the FSLIC, due to large losses in the thrift industry;277 it would seem to be contrary to that purpose to create a loophole that makes it easier to assert claims against the FDIC. Courts should read the statute to bar claims based upon agreements that do not affect the FDIC's interest in a specific asset.


It is not enough simply to say that the statute reaches the behavior at issue in both Murphy and Motorcity. If FIRREA and the established common law were thereby made entirely consistent, then the problem would disappear. FIRREA does not, however, address the issues covered by the federal holder in due course doctrine and thus there is no statutory construction argument available to deal with the issue raised by the Eighth Circuit's opinion in DiVall. If FIRREA does displace established common law, then the federal holder in due course doctrine is one of the casualties. Under the latter rule, the FDIC will only rarely be a holder in due course under state law.278 The greater danger, though, is taking Murphy as the standard to be applied when determining if new statutes displace established com-

274. See id.
276. The Fourth Circuit has followed Motorcity in declining to follow the Murphy gloss on 12 U.S.C. § 1823(e)(1). See Young v. Federal Deposit Ins. Corp., 103 F.3d 1180, 1189 (4th Cir. 1997) (declining to address the question of "whether Congress limited section 1823(e) to claims that impair the FDIC's interest in a specific asset").
277. See supra Part II.C.
common law. Murphy does not require congressional intent in order to find a displace-
ment. Rather, the court presumes that comprehensive statutes displace the field
turally.279 The only way for federal common law to survive such a statute under
the Murphy rule is for the statute to specifically indicate an intent to allow such a sur-

Even if this were the Supreme Court’s normal approach to established com-
mon law in the face of comprehensive statutes, the policy balance thus struck must be questioned. The Murphy court has not followed the correct Supreme Court precedent. O’Melveny & Myers, the lead case cited by the Murphy court, was readily distinguishable as precedent. Unlike Murphy, O’Melveny & Myers was concerned with the creation of new common law after the passage of a com-
prehensive statute.280 The primary concern with the creation of new common law is that a “carefully considered legislative program[]” will be upset.281 Even though the federal court acts in an area of significant federal interest, respect for a coordinate branch of government argues for abstention from the creation of new common law.282

The same cannot be said when Congress legislates in a field already occupied
by established federal common law.283 In those cases, the Court has required far


282. It should be noted that a judicial gloss upon a statute can radically change the effect of
the statute. The courts have split over the proper analysis to be undertaken in reading 12 U.S.C.
§ 1823(e)(1)(B), the requirement that any secret agreement be executed contemporaneously
with the acquisition of the asset in question. While noting that this requirement effectively
prevents the assertion of all defenses arising out of agreements between third parties and obli-
gors, the majority view reads the provision strictly to bar the defense. See DiMuzio v. Resolu-
should not be applied to bar defenses based upon allegedly fraudulent real estate appraisals and
refusing to recognize an equitable exception to the statute where, as here, “an obligor whose
promissory note is purchased on the secondary market can never execute an agreement contem-
poraneously with the bank’s acquisition of the note…”); Adams v. Madison Realty & Dev., Inc.,
937 F.2d 845 (3d Cir. 1991) (rejecting argument that 12 U.S.C. § 1823(e)(1) should not apply to
those obligors who had no dealings with the federally insured entity); Victor Hotel Corp. v. FCA
Mortgage Corp., 928 F.2d 785 (11th Cir. 1991); Federal Deposit Ins. Corp. v. La Rambala Shopping
Ctr., 791 F.2d 215 (1st Cir. 1986); Federal Deposit Ins. Corp. v. Blue Rock Shopping Ctr.,
Inc., 766 F.2d 744 (3d Cir. 1985) (applying 12 U.S.C. § 1823(e)(1) to accommodation parties to
a note); Chatham Ventures, Inc. v. Federal Deposit Ins. Corp., 651 F.2d 355 (5th Cir. Unit B
Me. 1992); Resolution Trust Corp. v. Crow, 763 F. Supp. 887 (N.D. Tex. 1991). Other courts
have argued that a federal court’s equitable powers allow it to interpret the contemporaneous
requirement in light of “general business practices” or “commercial reality.” See Resolution
Trust Corp. v. Midwest Federal Savings Bank, 36 F.3d 785 (9th Cir. 1993); Federal Deposit Ins.
does not say anything directly about the continued vitality of the D’Oench decision, it is impor-
tant to note that it is not just through “pure” common law that changes in the effect of a statute
can be worked.

283. Of course, the field must be truly occupied. In Milwaukee v. Illinois, 451 U.S. 304
(1981), the Court struck down a federal common law rule that had been created just prior to the
passage of the federal statute. Though the Court had originally suggested that the creation of a
common law rule was appropriate, it had been so prior to legislation. Moreover, the Court had
only suggested the possibility of a common law rule; unlike the D’Oench decision, this rule had
not been created when Congress legislated. There was, therefore, no way Congress could have
approved or disapproved the proposed rule. As such, the proposed common law rule had the
potential of upsetting the congressional plan and could not be retained. See also supra text
accompanying notes 59-70.
more than that the statute at issue simply be comprehensive. In United States v. Texas, the Court was unwilling to find displacement absent the expression of a congressional intent. As enunciated by the Eleventh Circuit, "federal courts are not free to contradict a congressional policy choice that 'speaks directly' to a particular question previously answered by federal common law." Where there is no such explicit congressional directive, the courts are faced with a policy choice between a presumption that the common law is displaced without explicit intent, the Murphy rule, or a presumption that the common law is not displaced in those cases. The failure of the Murphy court was its inability to realize that the latter rule, though it reaches an arguably different result than in O'Melveny & Myers with respect to the vitality of the common law, equally serves the purpose of preventing the disruption of congressional legislative schemes. Maintaining the presumption of the survival of the federal common law, even when Congress passes comprehensive legislation, both protects the continued vitality of the common law and ensures that where Congress is satisfied with a particular line of decisions, it does not have to laboriously enact a statutory equivalent to ensure the survival of the rule. Moreover, the retention of common law rules serves the interest of predictability. By definition any new statute requires interpretation and interpretation can lead to uncertainty. If every common law rule must be codified to survive a comprehensive enactment, then each of these rules will have to be reinterpreted in light of the new statutory language. A well established common law rule could be limited or distorted in much the same way that the Murphy court used 12 U.S.C. § 1823(e) to limit D'Oench.

In the specific instance of the relationship between D'Oench and FIRREA, there is no indication in the legislative history that Congress intended FIRREA to work a change upon established principles. Congress was primarily concerned with protecting the savings industry and staving off the threat of disaster that loomed from the savings and loan crisis. Though Congress made changes to 12 U.S.C. §§ 1823 and 1821 in FIRREA, the specific reasons for those changes were not discussed. There was no indication of an intent either to displace or to disapprove of the D'Oench line of cases. The statute and the common law had been read in conjunction to provide a more complete protection for the FDIC; it seems most likely that Congress intended merely to bolster the statutory side of the equation. Congress was surely aware that the common law and statute were being read together; it had ample opportunity to provide some guidance to the federal courts if it wished the practice to cease with the passage of FIRREA. These speculations aside, the legislative history is perhaps best characterized as inconclusive with regard to the codification of D'Oench.

286. Motorcity of Jacksonville, Ltd. v. Southeast Bank, 83 F.3d 1317, 1331 (11th Cir. 1996) (en banc) (citing Mobil Oil Corp. v. Higginbotham, 436 U.S. 618, 625 (1978) (holding that even in the absence of comprehensive legislation, a federal court could not directly contradict an express statutory provision)).
287. See supra text accompanying notes 131-142.
288. The federal holder in due course doctrine can be included in this description since it derives from D'Oench. See Gunter v. Hutcheson, 674 F.2d 862, 872 (11th Cir. 1982).
Finally, displacement of existing federal common law, particularly in cases where there is no clear indication of congressional intent to do so, can disrupt the federal system. Insofar as Congress passed its legislation depending upon the continued vitality of a uniform federal decision, the displacement of the federal common law returns such issues to the states. Justice Blackmun, in his dissent to *Milwaukee v. Illinois*, pointed out this danger.

By eliminating the federal common law of nuisance in this area, the Court in effect is encouraging recourse to state law wherever the federal statutory scheme is perceived to offer inadequate protection against pollution from outside the State, either in its enforcement standards or in the remedies afforded. This recourse is now inevitable under a statutory scheme that accords a significant role to state as well as federal law. But in the present context it is also unfortunate, since it undermines the Court's prior conclusion that it is federal rather than state law that should govern the regulation of *interstate* water pollution.289

In the present case, displacement of the federal common law would return the FDIC's holder in due course status to the states. The FDIC's attempts to enforce the instruments it obtains would no longer be subject to a uniform law; consequently, its ability to reduce the losses attendant upon the failure of a depositary institution would be far more uncertain, thus potentially frustrating one of the purposes behind FIRREA.290

V. CONCLUSION

The interaction between federal statutes and federal common law is an extremely delicate one. The Supreme Court has managed to create a balance between the competing interests inherent in our federal system of coordinate branches of government. In areas of uniquely federal interest, the federal courts may fashion federal rules of decision. This ensures that the supremacy of federal law is protected, and that federal law remains a uniform body of law.291 The Court has recognized, however, that the judiciary is not the final lawgiving power of the federal government. Congress has the power to determine federal law. Where Congress acts explicitly to overturn court precedent, there is a displacement of federal common law. Likewise, when Congress passes a comprehensive statute, that statute terminates the inchoate power of federal courts to create new law in the substantive area of the statute. The requirement that such action be explicit allows Congress to rely upon those common law rules that it believes work correctly while retaining the power to eliminate a court-made rule it finds inappropriate.

290. Neither the *D’Oench* nor the federal holder in due course doctrines greatly alter the potential outcome under established state law. Although state law would not allow this type of protection to be extended to the FDIC, all noteholders should realize that their instrument could be transferred to a holder in due course. In such cases, any defense they might have because of a secret agreement would be cut off. Thus, the application of federal common law in this instance does not infringe upon or create a result different from the expectations created by settled state law. See Federal Deposit Ins. Corp. v. McCullough, 911 F.2d 593, 603-04 (11th Cir. 1990).
291. See Martin v. Hunter’s Lessee, 14 U.S. (1 Wheat.) 304, 347- 48 (1816) (remarking on the “importance, and even necessity of *uniformity* of decisions throughout the whole United Sates, upon all subjects within the purview of the constitution”).

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Any other rule would disrupt the balance between statutory and common law and would create uncertainty within the system by forcing the replacement of established and known common law rules with uninterpreted statutory rules every time Congress enacted comprehensive legislation on a subject.

The Murphy/DiVall rule upsets this balance with its implication that a congressional enactment can abrogate an established common law rule despite the absence of an explicit intention to do so within either the statute or the legislative history. The danger in these two decisions is that their implication about the correct presumption for survival of federal common law might be transferred to other areas, resulting in disruption and potential frustration of congressional intent. Even though the Supreme Court refused to grant certiorari and decide this issue, the other circuits should follow the Eleventh Circuit's Motorcity decision and prevent a further disruption of the balance between federal statutes and federal common law.

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292. For instance, if Congress neglected to mention D'Oench because under United States v. Texas the common law rule would survive as a supplement to 12 U.S.C. § 1823(e)(1), then the D.C. and Eighth Circuits have frustrated that intent.