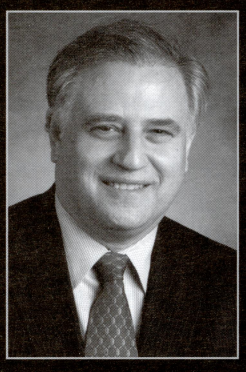
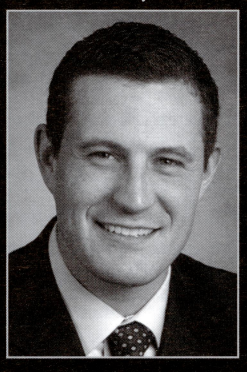
Recent Application of Minnesota's Credit Agreement Statute of Frauds

Inconsistent Application of Minnesota's Credit Agreement Statute of Frauds in Recent Cases

Economic turmoil and a declining financial and real estate market over the past few years have resulted in a significant increase in financial litigation. Although Minnesota's Credit Agreement Statute of Frauds (Minn. Stat. § 513.33) was originally enacted in response to the farm crisis in the early 1980s, it had not regularly been cited in appellate cases since the early 1990s—that is, until seven Minnesota Court of Appeals decisions cited to it in the 17 month period between December 2009 and April 2011. In the previous 15 years, Minnesota appellate courts cited section 513.33 on only three occasions.[1] The last time section 513.33 was cited so frequently by Minnesota appellate courts was in the economic turmoil of the late 1980s and early 1990s, correlating closely to the savings and loan crisis of that era.





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Despite being cited by Minnesota appellate courts a total of 19 times, the provisions of section 513.33 have only been applied by the Minnesota Supreme Court on a single occasion, nearly 20 years ago, in Rural American Bank of Greenwald v. Herickhoff, 485 N.W.2d 702 (Minn. 1992).

In light of the frequent application of section 513.33 in the past year-and-a-half and the shortage of Supreme Court authority regarding its application, this article will address a number of the recent decisions applying section 513.33, focusing on the consistency of the courts' application of the principles supporting the statute, as well as issues that may remain unclear regarding its application.

When section 513.33 was enacted, one of its goals was to provide certainty in lending transactions for lending institutions and borrowers. Over the years, some panels of the Minnesota Court of Appeals have strayed from this basic intent. Overall, the trend of appellate decisions favors creditors, but to obtain the certainty sought by the statute's drafters, the Minnesota Supreme Court may need to address section 513.33 and its application to common claims and defenses, including estoppel.

Basic Purpose of Minnesota's Codified Statute of Frauds for Credit Agreements

The purpose of section 513.33 is to prevent fraud in credit claims. This benefits a large cross-section of society including banks and their depositors. "[R]equiring claims by debtors to be based on written credit agreements does not benefit a small interest group, but is supported by the significant legislative purpose of protecting institutions and their depositors against fraudulent claims."[2]

Section 513.33, subdivision 2, provides that "[a] debtor may not maintain an action on a credit agreement unless the agreement is in writing, expresses consideration, sets forth the relevant terms and conditions, and is signed by the creditor and the debtor." The term "credit agreement" is defined as "an agreement to lend or forbear repayment of money, goods, or things in action, to otherwise extend credit, or to make any other financial accommodation."[3] Significantly, section 513.33, subdivision 3(b), also provides that a "credit agreement may not be implied from the relationship, fiduciary or otherwise, of the creditor and the debtor."

As explained by the Minnesota Supreme Court, "[t]he basic purpose of the writing requirements is to 'provide reasonable safeguards to insure honest dealing and [the statute of frauds] was not enacted to make a fetish of literal statutory compliance or a fetish of requiring a perfect written contract.'"[4]

History of Minnesota's Codified Statute of Frauds for Credit Agreements

Section 513.33 was enacted in 1985. The Minnesota Supreme Court recognized that it was intended to protect lenders from having to litigate claims of oral promises to renew agricultural loans. The farm crisis had "produced cash-strapped and financially unsophisticated farmers who claimed reliance upon their bank officers' oral promises to renew their loans."[5] As a direct result of numerous lawsuits that arose over "alleged oral promises" made by bankers, section 513.33 was "passed to prevent the litigation of such difficult claims." Accordingly, section 513.33 is a remedial statute designed by the Legislature to prevent "difficult claims" against banks based upon alleged oral promises. As such, its "broad language" is intended to be interpreted to prevent claims against banks.[6] However, as noted by the court in Rural American Bank of Greenwald v. Herickhoff, 473 N.W.2d 361, 363 (Minn. Ct. App. 1991), the meaning of the general phrase "any financial accommodation" does "not expand application of the statute to all agreements favoring the debtor."

Recent Application of Minnesota's Codified Statute of Frauds for Credit Agreements

Given section 513.33's history, it is unsurprising that the seven recent Minnesota Court of Appeals decisions citing the statute largely favor creditors. Although section 513.33 was not always applied to bar claims in these cases, the Court of Appeals nonetheless typically found ways to affirm dismissal of claims and defenses alleging promissory estoppel and equitable estoppel against banks and other creditors. The following is a general review of these recent cases followed by a discussion of the individual holdings in three of them:

Hinden v. American Bank of the North, A09-404, 2009 WL 4573909 (Minn. Ct. App. Dec. 8, 2009).
Affirming dismissal of promissory estoppel based on allegation bank would forebear its collection of debt because it was barred by section 513.33.

BankCherokee v. Insignia Development, LLC, 779 N.W.2d 896 (Minn. Ct. App. 2010).
Affirming dismissal of equitable and promissory estoppel defenses because "actions" on oral promises that constitute credit agreements are barred under section 513.33.

Krech v. Krech, A09-1836, 2010 WL 2035838 (Minn. Ct. App. May 25, 2010).
Dismissing alleged fraud claim and oral agreement bank would not foreclose on property as long as interest and taxes were paid because it was barred by section 513.33.

Becker v. Alliance Bank, A09-1871, 2010 WL 2899586 (Minn. Ct. App. Jul. 27, 2010).
Affirming dismissal of oral breach of contract claim as barred under section 513.33.

Grace Capital, LLC v. Mills, A09-1857, 2010 WL 2010 WL 3396817 (Minn. Ct. App. Aug. 31, 2010).
Not considering whether application of section 513.33 would bar fraudulent inducement defense because portions of appellant's fraudulent inducement defense alleging promises of future funding had already been dismissed on alternative grounds as being contrary to express terms of the loan notes at issue.

Highland Bank v. Dyab, A10-824, 2011 WL 781169 (Minn. Ct. App. Mar. 8, 2011).
Equitable estoppel properly dismissed and concluding promissory estoppel did not take subsequent oral agreements out of the statute of frauds under section 513.33.

Brickwell Community Bank v. Wycliff Associates II, LLC, A10-1396, 2011 WL 1237524 (Minn. Ct. App., Apr. 5, 2011).
Section 513.33 bars promissory estoppel claims, but material issues of fact denied summary judgment on equitable estoppel.

1. *BankCherokee v. Insignia Development, LLC*

In BankCherokee v. Insignia Development, LLC, the appellant asserted affirmative defenses including promissory and equitable estoppel, mistake, no meeting of the minds, and contract modification. The trial court granted summary judgment in favor of the bank. The Minnesota Court of Appeals affirmed dismissal of all these affirmative defenses holding they were barred under section 513.33.

The court held that all of the alleged oral "agreements [that appellant sought to prove]

amount to promises to forebear repayment of money or make some other financial accommodation and therefore are 'credit agreements' within the meaning of section 513.33."

Although section 513.33 expressly states that a "debtor may not maintain an action on a credit agreement unless the agreement is in writing, expresses consideration...and is signed by the creditor and the debtor," the court reasoned the "term 'action' as it is used in section 513.33 reasonably encompasses an affirmative defense." Accordingly, the court held that the appellant's affirmative defenses were barred by section 513.33.

In support of this holding, the court cited *Black's Law Dictionary*, "the statute's broad application," and implicit recognition of this holding in the Minnesota Supreme Court's *Rural American Bank of Greenwald v. Herickhoff* decision. The court, however, disregarded several decisions from appellate courts in other states interpreting similar codified credit agreement statutes of fraud as not barring affirmative defenses.[7] Additionally, the court failed to distinguish several cases applying Minnesota law allowing affirmative defenses despite challenges under section 513.33.[8]

The *BankCherokee* opinion is also significant in that it is a published opinion expressly determining that affirmative defenses for equitable and promissory estoppel based on facts pre-dating the written contract were barred as a matter of law pursuant to section 513.33. As discussed below, in the unpublished *Highland Bank v. Dyab* and *Brickwell Community Bank v. Wycliff Associates* cases, other panels of the Minnesota Court of Appeals have not necessarily expressed consistent views.

2. *Highland Bank v. Dyab*

Highland Bank v. Dyab involved an appeal from summary judgment in favor of the respondent, Highland Bank, in its lawsuit against appellant, Dyab, as guarantor of certain loans. In the district court, Dyab asserted affirmative defenses including equitable estoppel and promissory estoppel. The Minnesota Court of Appeals affirmed, relying primarily on the parol evidence rule in conjunction with section 513.33 to bar any alleged prior, contemporaneous, or subsequent oral credit agreements. The court also addressed the relative merits of the defenses of equitable estoppel and promissory estoppel in the context of section 513.33.

In his appeal, Dyab argued the district court erred in concluding that there was no genuine issue of material fact regarding whether Highland Bank breached oral agreements that (1) the loans at issue included 12-month interest-hold-back provisions; (2) Dyab would earn interest on a reserve account at the rate of 4.65 percent, which would be paid to Dyab monthly; and (3) Highland Bank would use funds from the reserve account to make payments on loans if a default or delinquency occurred. None of these oral agreements were expressed in the parties' written loan documents.

First, the court applied the parol evidence rule to dispose of any purported prior oral agreements that contradicted the terms of the written loan agreements. Of note, one of the agreements at issue contained a merger clause, which the court relied on in its determination that extrinsic evidence of prior or contemporaneous oral agreements was inadmissible to prove the meaning of the loan documents. However, another of the

loan agreements did not contain a merger clause. Despite the apparent drafting omission, the court did not look outside what it considered to be a complete integration. According to the opinion, "[t]o allow a party to lay the foundation for such parol evidence by oral testimony that only part of the agreement was reduced to writing, and then prove by parol the part omitted, would be to work in a circle and to permit the very evil which the rule was designed to prevent."

Next, the court turned to section 513.33 to eliminate any remaining subsequent oral agreements. Specifically, it upheld the district court in rejecting Dyab's arguments that the parties orally modified the loan documents to include agreements to hold back loan proceeds to pay interest for 12 months and to use the reserve account to make loan payments.

The court's application of the parol evidence rule in conjunction with section 513.33 dealt an effective one-two punch to Dyab's alleged oral promises. As the court put it, "[b]ecause the parol evidence rule bars appellants from using extrinsic evidence of prior or contemporaneous agreements to explain the meaning of their loan agreements and the statute of frauds in Minn. Stat. § 513.33 bars appellants from asserting claims based on subsequent oral modifications of the written agreements, appellants have not presented admissible evidence of any agreement that is not expressed in the loan documents."

After dealing with Dyab's alleged prior, contemporaneous, and subsequent oral agreements with a straight application of the parol evidence rule and section 513.33, the court considered the merits of Dyab's defenses of equitable estoppel and promissory estoppel under section 513.33. The court acknowledged that in Minnesota, an agreement may be taken out of the statute of frauds by application of the doctrine of equitable or promissory estoppel. Based on this exception, Dyab argued that even if the two alleged subsequent oral modifications of the loan documents were unenforceable under section 513.33, they could still be the basis for applying equitable estoppel and promissory estoppel.

In *Highland Bank*, the court listed six distinct elements that are required to establish the defense of equitable estoppel.[9] However, the court only needed to reach the first element in order to reject Dyab's equitable estoppel defense. Dyab's claim that Highland Bank agreed to use the reserve account to pay monthly loan payments until renters were in place was a broken promise at most, but never a concealment of material facts. Furthermore, even if it were a concealment, the third condition for applying equitable estoppel was not met because the truth about the terms of the agreements was not unknown to Dyab—those terms were stated plainly in the loan documents.

The court also rejected Dyab's promissory estoppel defense. In doing so, it noted that the defense of promissory estoppel will only overcome the statute of frauds "where the detrimental reliance is of such a character and magnitude that refusal to enforce the contract would permit one party to perpetrate a fraud. A mere refusal to perform an oral agreement, unaccompanied by unconscionable conduct, however, is not such a fraud as will justify disregarding the statute." The *Highland Bank* opinion also relied on Minnesota Supreme Court authority reflecting a "desire not to apply an equitable principle to such an extent as to render meaningless the statute of frauds."

The *Highland Bank* opinion did, however, recognize a separate Minnesota Court of Appeals decision where promissory estoppel was applied to reverse a summary judgment based on section 513.33. In Norwest Bank Minnesota, N.A. v. Midwestern Machine Company, 481 N.W.2d 875, 877 (Minn. Ct. App. 1992), the appellant entered into a buy-sell agreement to buy his former partner's interest in a business. The appellant claimed he agreed to the buy-sell plan only with assurances by the bank that the business's existing $5,000,000 line of credit would remain in place after the appellant assumed full ownership of the business. The court in *Norwest Bank Minnesota, N.A.*, ultimately concluded that fact issues existed as to whether a bank employee had promised to indefinitely extend the $5,000,000 credit line to induce the appellant to sign the buy-sell agreement and whether the appellant reasonably relied on the promise. However, as explained in *Highland Bank*, the court in *Norwest Bank Minnesota, N.A.*, neglected to analyze whether facts existed supporting the third element of promissory estoppel.

The court in *Highland Bank* had no trouble applying a full promissory estoppel analysis to conclude that promissory estoppel did not take any of Dyab's alleged oral agreements out of section 513.33. Importantly, the third step of the promissory estoppel analysis—determining whether the promise must be enforced to "prevent an injustice"—is a legal question for the court, as it involves a policy decision.[10] Thus, it was proper for the district court to reject Dyab's promissory estoppel defense where the written loan agreements provided that they may only be modified in writing. Accordingly, "to apply promissory estoppel to an unwritten promise that modifies the parties' original agreements, we would have to conclude that, even though the parties expressly agreed that any modification of their agreements must be in writing, the unwritten promise must be enforced to prevent an injustice."

The *Highland Bank* opinion is significant for its straight-forward application of the parol evidence rule in conjunction with section 513.33 to bar purported prior, contemporaneous, and subsequent oral credit agreements. However, in rejecting the appellant's defenses of equitable estoppel and promissory estoppel, the court in *Highland Bank* may have left the door open. Specifically, by addressing these defenses on their merits, rather than rejecting them by applying section 513.33, debtors in future cases may argue on equitable grounds that section 513.33 does not bar their oral agreements relating to a loan or other financial accommodation.

3. *Brickwell Community Bank v. Wycliff Associates II, LLC*

In Brickwell Community Bank v. Wycliff Associates II, LLC, the Minnesota Court of Appeals, in an unpublished opinion, affirmed the trial court's grant of summary judgment on grounds that section 513.33 barred the appellant's promissory estoppel defense and overruled the trial court's grant of summary judgment on the appellant's equitable estoppel claim. The court held that a counterclaim of equitable estoppel

trumped section 513.33 as a matter of law. This represented a departure from the published decision issued in *BankCherokee.* Accordingly, the unpublished *Brickwell Community Bank* decision may lead to further uncertain application of section 513.33 for lenders and borrowers alike.

In *Brickwell Community Bank,* the court found evidence that the bank: (1) made oral representations about its ability to advance timely additional credit in the amount required by the appellants to continue their business; (2) concealed the "arguably material fact" that it had reached its lending limit with the borrower and could not advance further credit to the borrower without a participating lending institution; and (3) cleared the borrower's overdraft checks that would otherwise have been returned "unpaid" due to insufficient funds, explaining to the borrower it would "document the loan at a later date." On remand, the guarantors and borrower in *Brickwell Community Bank* must litigate "questions of material fact" regarding an alleged oral credit agreement.

The court determined that the bank's purported oral representations, and other evidence, satisfied the prima facie elements of equitable estoppel which it listed as: (1) conduct (i.e., acts, language, or silence) amounting to a representation or concealment of material facts; (2) those material facts are either known by the party to be estopped or circumstances are such that the knowledge can be imputed; (3) the party asserting equitable estoppel does not know the true facts; and (4) the conduct must be done with the intention or expectation it will be acted upon, or at least under circumstances where it is both natural and probable that it will be acted upon.[11] Notably, the *Brickwell Community Bank* decision listed only four elements of equitable estoppel, while the *Highland Bank* and *BankCherokee* decisions listed two additional and material elements of a prima facie case for equitable estoppel. Due to the court's lack of discussion regarding how the prima facie elements of equitable estoppel were satisfied, it is unclear whether this omission impacted the court's ultimate resolution whereby it overruled the lower court's grant of summary judgment on the appellant's equitable estoppel counterclaim.

Thus, in a departure from its other recent decisions addressing section 513.33, the court looked favorably on the debtor's equitable estoppel defense. The court overlooked specific provisions of section 513.33, which provide that unless an agreement satisfies the requirements of subdivision 2 of section 513.33 (i.e., that "the agreement is in writing, expresses consideration, sets forth the relevant terms and conditions, and is signed by the creditor and the debtor"), a creditor's agreement to enter "into a new credit agreement, forbearing from exercising remedies under prior credit agreements, or extending installments due under prior credit agreements" does not give rise to a claim that a new credit agreement is created.[12]

The decision in *Brickwell Community Bank* has created additional uncertainty regarding enforcement of written credit agreements by allowing equitable claims and defenses to interrupt the unfettered application of the parties' written agreements pursuant to section 513.33. With this holding, if a defendant formulates facts sufficient to create a colorable claim of equitable estoppel, then application of the *Brickwell Community Bank* decision results in a trial. Consequently, banks may be less forthcoming on possible loan options for borrowers, and will be more inclined to strictly apply all loan terms. Under the holding in *Brickwell Community Bank,* oral representations, actions, or even mere silence may be alleged to create an enforceable oral promise.

Need for Considered Opinion from the Minnesota Supreme Court

The absence of Minnesota Supreme Court authority regarding the interpretation and application of section 513.33 on key, reoccurring issues allows the Court of Appeals to continue providing inconsistent opinions.

Since the enactment of section 513.33 in 1985, no Minnesota Supreme Court opinion has determined whether a "credit agreement" may be taken outside Minnesota's Credit Agreement Statute of Frauds by equitable or promissory estoppel. Accordingly, this may be viewed as an open issue.

Appellate court decisions since the enactment of section 513.33 have, on occasion, relied on Berg v. Carlstrom, 347 N.W.2d 809 (Minn. 1984), and Lunning v. Land O'Lakes, 303 N.W.2d 452 (Minn. 1980), for purposes of concluding that an agreement may be taken out of the statute of frauds by application of the doctrines of equitable or promissory estoppel.[13] However, both of those cases were decided prior to the enactment of section 513.33. Therefore, they are merely persuasive and not controlling.

Appellate court decisions allowing equitable or promissory estoppel have not addressed how the express terms of section 513.33 can be harmonized with previous decisions that may lead to results contrary to the express terms of section 513.33, which provide that "[a] debtor may not maintain an action on a credit agreement unless the agreement is in writing, expresses consideration, sets forth the relevant terms and conditions, and is signed by the creditor and the debtor." Nor do such decisions reflect the purpose and intent of the Legislature when enacting section 513.33 to prevent the litigation of difficult claims against banks based upon alleged oral representations that were not contained in signed, written credit agreements acknowledged by both the debtor and creditor.

Significantly, decisions post-dating the enactment of section 513.33 also fail to address both the apparent lack of any authority from the Minnesota Supreme Court applying promissory estoppel to take an agreement out of the statute of frauds,[14] as well as the Supreme Court's expressed desire "not to apply an equitable principle to such an extent as to render meaningless the statute of frauds."[15]

Other open issues may also exist. For example, no reported decision appears to have expressly determined whether personal guaranties provided as security for another party's debt obligations lie within the definition of a "credit agreement" under section 513.33. This issue can easily be avoided by drafting language into guaranty agreements expressly providing they constitute credit agreements and/or that they reflect a financial accommodation pursuant to section 513.33. However, enterprising guarantors

facing an enforcement action involving agreements that do not expressly provide they are credit agreements or financial accommodations under section 513.33 may raise this issue. Guidance from the Minnesota Supreme Court would be helpful as many of the recent cases involving section 513.33 also involve enforcement of personal guaranties.

Conclusion

The recent economic climate has resulted in an increase in litigation to obtain payment and enforce terms of credit agreements. As a result, Minnesota's Credit Agreement Statute of Frauds was applied to an increasing number of cases. However, due to inconsistent application by the Minnesota Court of Appeals, both creditors and debtors can cite case law and make arguments that may sway a trial court's decision regarding whether oral representations may create new, or alter existing, credit agreements, under the theories of promissory and equitable estoppel. Clear guidance on these important issues from the Supreme Court would provide a level of certainty benefitting all parties to credit transactions. Until then, creditors should focus on tightening their suite of loan documents and express in writing clearly what is, and what is not, part of each agreement.

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[1] *See* Gruelling v. Wells Fargo, 690 N.W.2d 757 (Minn. Ct. App. 2005); Scally v. Norwest Mtg., Inc., C4-02-2181, 2003 WL 22039526 (Minn. Ct. App. Sep. 2, 2003); The Loan Store v. McConnell, A06-122, 2006 WL 3490807 (Minn. Ct. App. Dec. 5, 2006).

[2] Drewes v. First Nat'l Bank of Detroit Lakes, 461 N.W.2d 389, 392 (Minn. Ct. App. 1990).

[3] Minn. Stat. § 513.33, subd. 1(1).

[4] Rural Am. Bank of Greenwald, 485 N.W.2d at 707 (*quoting* Greer v. Kooiker, 312 Minn. 499, 505, 253 N.W.2d 133, 138 (1977)).

[5] *Id.*

[6] *See* Pako Corp. v. Citytrust, 109 B.R. 368, 377 (D.Minn. 1989); BankCherokee v. Insignia Dev., LLC, 779 N.W.2d 896, 902 (Minn. Ct. App. 2010); Becker v. Alliance Bank, A09-1871, 2010 WL 2899586 (Minn. Ct. App. Jul. 27, 2010).

[7] *See, e.g.*, Maynard v. Cent. Nat'l Bank, 640 So.2d 1212 (Fla. App. 5 Dist. 1994); Hibernia Nat'l Bank v. Contractor's Equip., 804 So.2d 760 (La. Ct. App. 2001); Sees v. Bank One, 839 N.E.2d 154 (Ind. 2005).

[8] *See, e.g.*, Resolution Trust Corp. v. Flanagan, 821 F. Supp. 572 (D. Minn. 1993) (Doty, J.); Rural Am. Bank of Greenwald v. Herickhoff, 485 N.W.2d 702 (Minn. 1992).

[9] Highland Bank v. Dyab, A10-824, 2011 WL 781169 (Minn. Ct. App. Mar. 8, 2011) (*citing* Lunning v. Land O'Lakes, 303 N.W.2d 452, 457 (Minn. 1980)).

[10] Cohen v. Cowles Media Co., 479 N.W.2d 387, 391 (Minn. 1992).

[11] Brickwell Community Bank v. Wycliff Associates II, LLC, A10-1396, 2011 WL 1237524 (Minn. Ct. App., Apr. 5, 2011) (*citing* Del Hayes & Sons, Inc. v. Mitchell, 304 Minn. 275, 283, 230 N.W.2d 588, 593 (Minn. 1975)).

[12] Minn. Stat. § 513.33, subd. 3(3).

[13] *See, e.g.*, Highland Bank, 2011 WL 781169.

[14] *Id.*

[15] Sacred Heart Farmers Co-op Elevator v. Johnson, 305 Minn. 324, 232 N.W.2d 921 (1975).

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