Bank in Missouri Hit for Punitive Damages, Found Liable for Fiduciary's Misappropriation of Funds

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In *Delarosa v. Farmer's State Bank*, the Missouri Court of Appeals, W.D., expounded upon the duty imposed upon Missouri Banks under § 469.270[1] of the Missouri's Uniform Fiduciaries Law ("UFL"). Specifically, the Court addressed account funds being misappropriated by a third-party fiduciary[2]. The Court also affirmed the jury's award of punitive damages against the Bank for its failure to provide accurate discovery responses.

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[1]§ 469.270 of the UFL provides:

> **If a check . . . is drawn by a fiduciary . . . the payee is not bound to inquire whether the fiduciary is committing a breach of his obligation as fiduciary in drawing or delivering the instrument, and is not chargeable with notice that the fiduciary is committing a breach of his obligation as fiduciary unless he takes the instrument with actual knowledge of such breach or with knowledge of such facts that this action in taking the instrument amounts to bad faith. If, however, such instrument is payable to a personal creditor of the fiduciary and delivered to the creditor in payment of or as security for a personal debt of the fiduciary to the actual knowledge of the creditor, or is drawn and delivered in any transaction known by the payee to be for the personal benefit of the fiduciary, the creditor or other payee is liable to the principal if the fiduciary in fact commits a breach of his obligation as fiduciary in drawing or delivering the instrument.**
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> Mo Stat. Ann. (2013) (L. 1959 S.B. 121 § 5, A.L. 2004 H.B. 1511)

[2]474 S.W.3d 240 (2015).

In *Delarosa*, the court held that Missouri banks can be liable for a third-party fiduciary's misappropriation of account funds, if a bank is on notice of the fiduciary misappropriation and the bank receives a "bank benefit." Moreover, a bank can be liable for subsequent misappropriations by a fiduciary, even if a bank receives no further "bank benefit" from any subsequent misappropriations.

The case involved Ms. Coyner, who was appointed the conservator of the Estate of Delarosa (Estate). Ms. Coyner presented three checks to Farmers State Bank (Bank) written on the Estate's checking account. The Bank permitted Ms. Coyner to deposit the checking account funds into her personal checking account and make a loan payment to the Bank on her personal loan. A subsequent conservator, Ms. Hendren, was appointed after Ms. Coyner died. Ms. Hendren identified Ms. Coyner's misappropriation of the Estate's bank account funds and filed a claim against the Bank for conversion and to recover the misappropriated bank account funds in the amount of $39,000.00. The jury returned a verdict for the Estate on its conversion claim and awarded the Estate actual damages in the amount of $39,000.00 and punitive damages in the amount of $150,000.

On appeal, the Bank argued it did not have actual knowledge of Ms. Coyner's misappropriation of account funds, and the UFL does not impose a duty on the Bank in the absence of actual knowledge of the misappropriation. The Bank contended that the verdict director for the Estate's conversion claim should have included a requirement that the Bank had actual knowledge that Ms. Coyner was breaching her fiduciary duty when the Bank accepted the benefit of her loan payment.

The Court disagreed, holding that the UFL requires only that the Bank have "actual knowledge" that the Bank was applying misappropriated account funds to a debt owed the Bank, and not actual knowledge that the fiduciary was breaching a duty. The Court further held the Bank was liable to the Estate for the misappropriated account funds because the Bank had sufficient notice or knowledge that Ms. Coyner was misappropriating the Estate's bank account funds. Although the Bank only received the benefit of her loan payment, the Court also held the Bank liable for Ms. Coyner's subsequent misappropriations that followed her loan payment to the Bank. The Court found that Ms. Coyner's loan payment put the Bank on sufficient notice of her misappropriation of the Estate's bank account funds.

On appeal, the Bank also argued that the trial court erred in submitting a punitive damages instruction as a result of the Bank's discovery practices. The Bank argued that the instruction was in error because there was no clear and convincing evidence of any intentional acts by the Bank that would amount to an evil motive or a reckless disregard for the Estate's rights. At trial, the Estate argued that the Bank covered up Bank records of check transactions in response to the Estate's discovery requests, and did so for many years after Ms. Coyner's misappropriation occurred. The Bank's original responses to the Estate's discovery requests provided that the Bank "*had no records regarding the check transactions*," and that "*the Bank deposited the proceeds of the subject checks into the account for the Estate.*" The litigation continued over a period of many years until the Bank "found" records that showed its original discovery responses were false. The Court held that the Bank had no evidentiary basis for its original discovery responses and the jury could have concluded that the Bank knowingly provided a false statement or acted with reckless indifference to the Estate's rights.

Thus, another take away from this case is that banks and their counsel should be aware of the ramifications of providing incomplete or inaccurate discovery responses, especially when records and information exist that can be used by the bank to accurately respond to discovery requests. During discovery, banks should perform diligent searches for documents that can withstand a court's review and scrutiny.

If you have any questions, please contact your Lathrop Gage attorney or the attorney(s) listed above.