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## ASK KENNEDY

### July 12, 2023

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#### Topics Covered:

- Special Guests: NDBA President and CEO, Rick Clayburgh
- 2023 North Dakota Legislative Summary with Rick Clayburgh
- Member Questions
- An In Depth Look at Electronic Promissory Notes
- NDBA Helpful Resources
- Upcoming NDBA Events

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#### Special Guests: Rick Clayburgh

Rick Clayburgh is the current CEO and President of the NDBA. He has been with the NDBA for over 18 years as the president and has an extensive background in finance and banking. Rick has played a critical role in advocating for legislative changes and updates for the banking and finance industry in North Dakota. He will be discussing the 2023 Legislative Summary from this past session.

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#### 2023 North Dakota Legislative Summary with Rick Clayburgh

Join Rick Clayburgh as he discusses the 2023 North Dakota Legislative Summary, including any relevant new bills, defeated bills, and how those will affect the banking and finance industry. For an electronic copy of the 2023 Legislative Summary, please visit this [link](#).

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#### Member Questions

**Question #1: What are the consequences of failing to register a business that is not organized in the State of North Dakota, but who conducts business in the state, as a foreign entity?**

**Response:** Foreign corporations are prohibited from transacting business in North Dakota until a certificate of authority has been procured from the Secretary of State. N.D.C.C. § 10-19.1-134(1).

Section 10-19.1-142 of the North Dakota Century Code articulates the particular rights of foreign corporations transacting or “doing business” in the state without a certificate of authority:

1. A foreign corporation transacting business in this state **may not maintain** any claim, action, suit, or proceeding in any court of this state until it possesses a certificate of authority.
2. The failure of a foreign corporation to obtain a certificate of authority **does not...prevent the foreign corporation from defending** any claim, action, suit, or proceeding in any court of this state.

**Question #2: What is the procedure for a Sheriff's Levy when serving a garnishment to a bank and are there any specific rules for the delivery of this kind of levy?**

**Response:** Below is a section of the North Dakota Century Code dealing the service of a Notice of Levy which states that it must be served in the same manner as a summons is served, and below that is a portion of Rule 4 of the North Dakota Rules of Civil Procedure which lays out how a summons may be served on a corporation. Service of a Notice of Levy is not the same as service of a Garnishment Summons, because the Garnishment Statutes actually require a different way of service which is much more restrictive than a regular summons.

**NDCC Service of Notice of Levy**

28-21-12. Notice of levy - Service - Contents. In all cases of levy upon personal property, the sheriff or other officer must serve the notice of levy in the same manner as a summons is served in accordance with the North Dakota Rules of Civil Procedure. Such notice must have written or printed upon its face the further notice to the debtor, that if exemptions are claimed or demanded, such claim must be made within ten days after service of notice.

**Rule 4 of the North Dakota Rules of Civil Procedure – Personal Service on a Corporation.**

(2) How Service Made Within the State. Personal service of process within the state must be made as follows:

(D) Serving a Corporation, Partnership, or Association. Service must be made on a domestic or foreign corporation or on a partnership or other unincorporated association, by:

(i) delivering a copy of the summons to an officer, director, superintendent or managing or general agent, or partner, or associate, or to an agent authorized by appointment or by law to receive service of process on its behalf, or to one who acted as an agent for the defendant with respect to the matter on which the plaintiff's claim is based and who was an agent of the defendant at the time of service;

**(ii) if the sheriff's return indicates no person upon whom service may be made can be found in the county, then service may be made by leaving a copy of the summons at any office of the domestic or foreign corporation, partnership, or unincorporated association within this state with the person in charge of the office; or**

(iii) any form of mail or third-party commercial delivery addressed to any of the foregoing persons and requiring a signed receipt and resulting in delivery to that person.

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**Question #3: When implementing dormant account fees on deposit accounts, does sending a change in terms (new disclosure) to customers satisfy the “if contracted for” requirement that N.D.C.C 47-30-2.31 outlines?**

**Response:** North Dakota has adopted the Revised Uniform Unclaimed Property Act as Chapter 47-30.2, N.D.C.C. The Act permits a “holder” (defined as a person obligated to hold for the account of, or to deliver or pay to, the owner, property subject to Ch. 47-30.2) to deduct a dormancy charge from property required to be paid or delivered to the administrator if (a) an enforceable written contract between the holder and the apparent owner authorizes imposition of the charge for the apparent owner’s failure to claim the property within a specified time; and (b) the holder regularly imposes the charge and regularly does not reverse or otherwise cancel the charge. See N.D.C.C. §§ 47-30.2-01(16) and 47-30.2-31(1). The dormancy charge may only be charged until the respective property is deemed abandoned. N.D.C.C. § 47-30.2-31(2).

Regulation DD requires disclosure of account fees and contains specific requirements for changes-in-terms. See 12 C.F.R. § 1030.4(b)(4) and 12 C.F.R. § 1030.5(a). However, banks are not required to disclose incidental fees, such as fees associated with state escheat laws, under section 1030.4 of Regulation DD. See Comment 2 to 12 C.F.R. § 1030.4(b)(4).

Therefore, whether the bank can send out a change-in-terms to implement a new dormancy fee will be dependent upon the terms and conditions of the bank’s existing deposit account (i.e., provisions regarding amendments/modifications/changes-in-terms).

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**Question #4: What perfects a bank’s interest when taking hopper bins as collateral? Is the UCC farm blanket enough or do banks need to be taking a fixture filing as well?**

**Response:** The question of whether bins are equipment or fixtures is often asked and the answer comes down to the definition of a fixture which is the following:

Section 47-01-05 - Fixtures defined

A thing is deemed to be affixed to land when it is attached to it by roots, as in the case of trees, vines, or shrubs, or imbedded in it, as in the case of walls, or permanently resting upon it, as in the case of buildings, or permanently attached to what is thus permanent, as by means of cement, plaster, nails, bolts, or screws.

With that said, I think the most prudent thing is to treat the bins as both equipment and fixtures but filing your UCC-1 Financing statement naming the bins specifically and filing a fixture financing statement in the real estate records, which will require the name of the debtor, the name of the real property owner and a legal description along with the description of the bins. Lastly, if the bins are on land owned by someone else you will want to make sure that you get a severance agreement from the land-owner too.

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**Question #5(A): Regarding UTMA accounts savings accounts, are we allowed to close these accounts upon request – without requiring specific verbiage on the check (meaning no responsibility is held by the bank to ensure these funds are transferred over properly to another UTMA internally or externally.)**

**Response:** The Custodian will have the power to open and close accounts. Sections 47-24.1-12 and 47-24.1-13 outline both the powers of a custodian and responsibility of the custodian.

**Question #5(B): Regarding transacting individuals, both before and after age of 21 (Custodian vs. minor):**

- a. What are the requirements of the appropriate individual allowed to transact prior to age 21 (Custodian only)?
- b. What is the ability to transact on UTMA accounts after age 21 is reached by “minor” (Minor only)?

**Response:** Be cautious with this question! Section 74-24.1-20 determines when the custodianship terminates and that can be either 18 or even 21 depending on how the property was transferred to the custodian on behalf of the minor. See Sections 47-24-05, 47-24-06, and 47-24-07.

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### **An In Depth Look at Electronic Promissory Notes**

House Bill 1082 was passed by the North Dakota legislature and signed by the Governor Burgum on March 20, 2023. This bill contained amendments to various articles of the Uniform Commercial Code and also enacted a new Article 12 dealing with “Controllable Electronic Records.” The passage of this bill has a number of different implications for North Dakota banks, including implications for Electronic Promissory Notes and their value on the secondary market.

See the attached article for an in depth look on what banks need to know regarding Electronic Promissory Notes.

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### **NDBA Helpful Resources**

**FDIC Makes Public April Enforcement Actions** | The FDIC released a list of orders of administrative enforcement actions against banks and individuals in April 2023. Click this [link](#) for more information on the enforcement decisions and orders.

**Small Business Lending Rule FAQ** | The Consumer Finance Protection Bureau has provided a link addressing common questions regarding compliance with the smalling business lending rule. To view the FAQs, please visit this [link](#).

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### **Upcoming NBDA Events in 2023**

NDBA has many exciting and informational events planned for 2023. Below are some special dates to mark on your calendars!

### **SCHOOLS**

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- **2023 Breaking into Banking 201: Analyzing Repayment Sources** | September 7, 2023 | Virtual Training

### **CONFERENCES**

- **BND Update of Legislative Impact** | July 18, 2023 | Virtual Webinar | [Register Here](#)
  - **2023 Group Meetings** | September 11-14, 2023
  - **2023 Ag Credit Conference** | September 27-28, 2023 | Bismarck, ND
  - **Bank Management Conference** | February 16-17, 2024 | Scottsdale, AZ
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## **ELECTRONIC PROMISSORY NOTES: WHAT BANKS NEED TO KNOW**

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By: Ryan Ames

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### ***Background and Overview***

Article 3 of the Uniform Commercial Code (UCC), as adopted in the North Dakota Century Code (N.D.C.C. 41-03), establishes the conditions for an instrument to be negotiable. A key requirement is that the instrument must be signed and written in a physical form. Consequently, an electronic promissory note, or “eNote” would not qualify as a negotiable instrument under Article 3.

Responding to this limitation, the North Dakota legislature enacted the Uniform Electronic Transactions Act or “UETA.” This legislation, which has been universally adopted by every state but New York, provides validity to electronic promissory notes and their value on the secondary market, provided that certain conditions are met. Under UETA, eNotes enjoy the same benefits and defenses afforded to traditional negotiable instruments under Article 3 of the Uniform Commercial Code, allowing them to be sold more easily on the secondary market.

Recently, the 2022 amendments to the Uniform Commercial Code were passed in North Dakota, as House Bill 1082. Importantly, the 2022 Amendments also created a new Article 12 of the UCC which addresses “Controllable Electronic Records,” or “CERs.” Article 12 creates two different subcategories of collateral: (1) Controllable Accounts, and (2) Controllable Payment Intangibles. The Article 12 rules for Controllable Payment Intangibles could provide additional protections for eNotes, in the event the requirements of UETA are not met. These extra safeguards could increase the appeal of eNotes

governed by North Dakota law for buyers in the secondary market.

### ***UETA eNote Requirements***

Electronic promissory notes are referred to in UETA as “**Transferable Records.**” To qualify as a transferable record, the eNote must state the following:

1. Must be payable to the holder at the time it is issued or when it first comes into the holder’s possession;
2. Must be payable on demand or at a definite time; and
3. The person who is required to make payments under the eNote must agree that the electronic record is a transferable record.

UETA affords transferable records the same negotiability benefits provided in Article 3 to the holder who is in “Control” of the transferable record. Namely, the party in control is treated as a holder in due course under Article 3 and allows the holder and a qualifying purchaser to take the transferable record free of competing property claims and security interests.

To satisfy the control prerequisites under UETA, the system responsible for creating, storing, and assigning the transferable record must be able to do the following:

1. It must produce a single unique authoritative copy of the transferable record, which is identifiable and unalterable, except for the allowed

- alterations detailed below;
2. The authoritative copy must identify the person asserting control as;
    - a. The person to which the transferable record was issued; or
    - b. If the transferable record has been transferred, the person to whom the transferable record was most recently transferred;
  3. The transferable record must be maintained by the person asserting control or a designated custodian;
  4. The authoritative copy can only be revised to add or change an identified assignee with the consent of the person asserting control;
  5. All copies can be easily identified as the authoritative copy or a copy of the authoritative copy; and
  6. Any revision to the authoritative copy is readily identifiable as authorized or unauthorized

If the above requirements are met and the eNote becomes a transferable record, which can easily be sold on the secondary market because the purchasers enjoy the same rights and defenses given to the holder in due course of a physical negotiable instrument under N.D.C.C. § 41-03. However, the feasibility of the transaction largely depends on the system used to create, store, and manage the transferable record.

### ***eNotes and UCC Article 12 Controllable Electronic Records***

North Dakota became one of the first states to adopt the 2022 amendments and enact the new Article 12. The 2022 amendments address a limited set of transactions involving emerging technologies, including: virtual currencies, distributed ledger technology, and, to a limited extent, artificial intelligence.

In short, the amendments are a direct response to market concerns about the lack of concrete rules for transactions involving digital assets, including but not limited to the following: (1) negotiability of virtual currencies, (2) certain electronic payment rights, (3) secured lending against virtual currencies, and (4) security interests in electronic money, i.e., central bank digital currencies.

Article 12 was drafted with these concerns in mind, and deals with Controllable Electronic Records or “CERS” which are electronic records capable of being controlled under N.D.C.C. § 41-12-05. This new article creates two new subcategories of collateral: (1) controllable accounts, (2) controllable payment intangibles, both of which must be evidenced by a CER. In this context, eNotes could potentially be considered a controllable payment intangible. This classification would provide an extra layer of security for any eNotes that fail to meet the criteria for a transferable record under UETA.

Under Article 12, if a promise to pay is evidenced by a CER and the person obligated to make payments has agreed to pay the person in control of the CER, the “take-free” rule applies and a qualifying purchaser will take the CER free of competing property interests. Moreover, if the purchaser also agrees to not assert claims or defenses against a transferee, the eNote will have negotiability characteristics similar to those of a negotiable instrument under Article 3.

Before an eNote can be considered a controllable payment intangible, and governed by Article 12, the system it is created/stored on must be able to satisfy the elements of control under N.D.C.C. § 41-12-05. The control requirements resemble those found under UETA, and a system that meets the UETA control criteria will likely satisfy the control requirements outlined in Article 12.

A person has control of a CER if the system that the electronic record is stored and managed give the person:

1. The power to avail itself of substantially all of the benefit of the electronic record (i.e., the right to receive payments under the eNote);
2. The exclusive power to:
  - a. prevent others from availing themselves of substantially all the benefit from the electronic record (i.e., ability to prevent others from receiving payments under the eNote); and
  - b. transfer control of the electronic record to another person.

Article 12 provides some additional protections for eNotes that fail to meet all the transferable record requirements found in UETA. Ensuring that your eNote satisfies the UETA the requirements is preferable, but purchasers on the secondary market may see more value in eNotes governed by North Dakota law because of the overlap between the control requirements found in Article 12 and UETA.

If you have any questions regarding transferable records, controllable payment intangibles and their effects on eNotes, please feel free to reach out to Tracy Kennedy at [tracy@ndba.com](mailto:tracy@ndba.com)