COURT OF APPEALS OF WISCONSIN
DISTRICT III

Herman Grad *et al.*,

Plaintiffs-Appellants,

v. Appeal No. 10-AP-1461

Associated Bank, N.A., Circuit Court No. 09-CV-2949

Defendant-Respondent.

APPEAL FROM THE JUDGMENT OF THE CIRCUIT COURT FOR BROWN COUNTY, CASE NO. 09-CV-2949 THE HONORABLE DONALD R. ZUIDMULDER, PRESIDING

BRIEF OF DEFENDANT-RESPONDENT

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TABLE OF CONTENTS

Page

TABLE OF CONTENTS i

TABLE OF AUTHORITIES iii

ISSUES PRESENTED FOR APPEAL 1

STATEMENT ON ORAL ARGUMENT AND PUBLICATION 3

STATEMENT OF THE CASE 4

FACTUAL HISTORY 6

A. Associated Bank 6

B. The Crown Forex Fraud 6

C. This Litigation 8

SUMMARY OF ARGUMENT 9

ARGUMENT 11

I. The Circuit Court Properly Dismissed The Negligence Claim 11

A. Plaintiffs Fail To Allege That Associated Breached The Applicable Duty Of Care 11

1. *The Wisconsin Supreme Court has held that a bank's duty of care does not require it to detect the fraudulent acts of its accountholders under these circumstances.* 13

2. *Federal banking regulations do not set or expand a bank's common law duties.* 33

B. Public Policy Forecloses The Plaintiffs' Claims. 37

1. *The circuit court properly exercised its discretion to adjudicate the public policy factors at this juncture.* 38

2. *Public policy forecloses any liability to Associated in these circumstances.* 42

II. The Circuit Court Properly Dismissed The Aiding And Abetting Claims. 50

CONCLUSION 57

TABLE OF AUTHORITIES

Cases **Page(s)**

In re Agape Litigation,
681 F. Supp. 2d 352 (E.D.N.Y. 2010) 34

Aiken v. Interglobal Mergers & Acquisitions,
2006 WL 1878323 (S.D.N.Y. July 5, 2006) 35

ALG, Inc. v. Estate of Eldred,
35 P.3d 931 (Kan. App. 2001) 28

Alvarado v. Sersch,
2003 WI 55, 262 Wis.2d 74, 662 N.W.2d 350 (2003) .. 21, 22, 40

Antoniewicz v. Reszcynski,
70 Wis.2d 836, 236 N.W.2d 1 (1975) 40

Armstrong v. Am. Pallet Leasing Inc.,
678 F. Supp. 2d 827 (N.D. Iowa 2009) 35

Athey Products Corp. v. Harris Bank Roselle,
89 F.3d 430 (7th Cir. 1996) 28

B.E.L.T., Inc. v. Wachovia Corp.,
403 F.3d 474 (7th Cir. 2005) 33

Beacon Bowl, Inc. v. Wis. Elec. Power Co.,
176 Wis.2d 740, 501 N.W.2d 788 (1993) 43

Bowen v. Lumbermens Mut. Cas. Co.,
183 Wis.2d 627, 517 N.W.2d 432 (1994) 40

Brunson v. Affinity Fed. Credit Union,
972 A.2d 1112 (N.J. 2009) 28, 31, 32

Carran v. Morgan,
2007 WL 3520480 (S.D. Fla. Nov. 14, 2007) 33

Cefalu v. Cont'l W. Ins. Co.,
2005 WI App. 187, 285 Wis.2d 766,
703 N.W.2d 743 (2005) 41

Cirillo v. City of Milwaukee,
34 Wis.2d 705, 150 N.W.2d 460 (1967) 16

Commercial Discount Corp. v. Milwaukee W. Bank,
61 Wis.2d 671, 214 N.W.2d 33 (1974) .... *passim*

Coopman v. State Farm Fire & Cas. Co.,
179 Wis.2d 548, 508 N.W.2d 610 (Ct. App. 1993) 51

Doe v. Archdiocese of Milwaukee,
2005 WI 123, 284 Wis.2d 307, 700 N.W.2d 180 (2005) 51

In re D.S.,
142 Wis.2d 129, 416 N.W.2d 292 (1987) 39

Edwardson v. Am. Family Mut. Ins. Co.,
223 Wis.2d 754, 589 N.W.2d 436 (Ct. App. 1998) 53

Eisenberg v. Wachovia Bank, N.A.,
301 F.3d 220 (4th Cir. 2002) .... *passim*

Estate of Paswaters v. Am. Family Mut. Ins. Co.,
2004 WI App. 233, 277 Wis.2d 549,
692 N.W.2d 299 (2004) 41

Fandrey ex rel. Connell v. Am. Family Mut. Ins. Co.,
2004 WI 62, 272 Wis.2d 46, 680 N.W.2d 345 (2004) .... *passim*

Fredrickson v. Kabat,
266 Wis. 442, 63 N.W.2d 756 (1954) 53, 54

Gendler v. Sibley State Bank,
62 F. Supp. 805 (N.D. Iowa 1945) 16, 28

Gesell v. First Nat'l City Bank,
260 N.Y.S.2d 581 (N.Y. App. Div. 1965) 28

Giebel v. Richards,
224 Wis.2d 468, 591 N.W.2d 901 (Ct. App. 1999).............. 43, 44

Gilbert v. United Nat'l Bank,
436 N.W.2d 23 (S.D. 1989).. 29

Gritzner v. Michael R.,
2000 WI 68, 235 Wis.2d 781, 611 N.W.2d 906 (2000) ......*passim*

Guidry v. Bank of LaPlace,
740 F. Supp. 1208 (E.D. La. 1990),
aff'd, 954 F.2d 278 (5th Cir. 1992) 28

Hanninen v. Fedoravitch,
583 F. Supp. 2d 322 (D. Conn. 2008) 33

Hass v. Chicago & Nw. Ry.,
48 Wis.2d 321, 179 N.W.2d 885 (1970) 40, 41

Hocking v. City of Dodgeville,
2009 WI 70, 318 Wis.2d 681,
768 N.W.2d 552 (2009).. 13, 22

Hoida, Inc. v. M & I Midstate Bank,
2006 WI 69, 291 Wis.2d 283, 717 N.W.2d 17 (2006) ....*passim*

Hornback v. Archdiocese of Milwaukee,
2008 WI 98, 313 Wis.2d 294, 752 N.W.2d 862 (2008) 40

Kemp v. Wis. Elec. Power Co.,
44 Wis.2d 571, 172 N.W.2d 161 (1969) 16

Kesselman v. Nat'l Bank,
937 P.2d 341 (Ariz. App. 1996) 27

Loyd v. Huntington Nat'l Bank,
2009 WL 1767585 (N.D. Ohio June 18, 2009) 28

Marlin v. Moody Nat'l Bank N.A.,
2006 WL 2382325 (S.D. Tex. Aug. 16, 2006) 35

Mazon Assocs., Inc. v. Comerica Bank,
195 S.W.3d 800 (Tex. App. 2006) 29

McCallum v. Rizzo,
1995 WL 1146812 (Mass. Super. Ct. Oct. 13, 1995)................. 28

Miller v. Wal-Mart Stores, Inc.,
219 Wis.2d 250, 580 N.W.2d 233 (1998) 40

Nat'l Union Fire Ins. Co. v. Allfirst Bank,
282 F. Supp. 2d 339 (D. Md. 2003)... 28

Old Republic Nat'l Title Ins. Co. v. Landmark Closing Co.,
2010 WL 2228436 (E.D. Ark. June 1, 2010) 27

Palsgraf v. Long Island Railroad,
162 N.E. 99 (N.Y. 1928) 22, 25

Patrick v. Union State Bank,
681 So. 2d 1364 (Ala. 1996).. 31, 32

Pfeifer v. Standard Gateway Theater, Inc.
262 Wis. 229, 55 N.W.2d 29 (1952) 16

Portage Aluminum Co. v. Kentwood Nat'l Bank,
307 N.W.2d 761 (Mich. App. 1981) 28

Promissor, Inc. v. Branch Bank & Trust Co.,
2008 WL 5549451 (N.D. Ga. Oct. 31, 2008)............................. 27

Prudential Ins. Co. v. Marine Nat'l Exch. Bank,
371 F. Supp. 1002 (E.D. Wis. 1974) 31

Prudential-Bache Sec., Inc. v. Citibank, N.A.,
536 N.E.2d 1118 (N.Y. 1989) 30

Ralph v. Bank One Wisconsin,
2003 WI App. 22, 259 Wis.2d 933,
657 N.W.2d 439 (Ct. App. 2002) 17

Ralph v. Bank One Wisconsin,
No. 00-cv-010774 (Wis. Cir. Nov. 7, 2001)................... 16, 23, 24

Ramsey v. Hancock,
79 P.3d 423 (Utah App. 2003)... 29

Rieck v. Med. Protective Co.,
64 Wis.2d 514, 219 N.W.2d 242 (1974) 41

Rinehart v. Whitehead,
64 Wis. 42, 24 N.W. 401 (1885) 53

Robertson-Ryan & Assocs., Inc. v. Pohlhammer,
112 Wis.2d 583, 334 N.W.2d 246 (1983) 39, 42

Sawyer v. Midelfort,
227 Wis.2d 124, 595 N.W.2d 423 (1999) 40

Schleicher v. W. State Bank,
314 N.W.2d 293 (N.D. 1982) 28

Schneller v. St. Mary's Hosp. Med. Ctr.,
162 Wis.2d 296, 470 N.W.2d 873 (1991) 38, 39

Schuster v. Alternberg,
144 Wis.2d 223, 424 N.W.2d 159 (1988) 40

SEC v. Cook,
No. 09-cv-03333 (D. Minn., filed Nov. 23, 2009) 8

Shane Smith Enters., Inc. v. Bank of Am., N.A.,
2007 WL 1880201 (E.D. Ark. June 29, 2007) 30, 32

Sheiman v. Lafayette Bank & Trust Co.,
492 A.2d 219 (Conn. App. Ct. 1985) 27

Shearson Lehman Bros., Inc. v. Wasatch Bank,
788 F. Supp. 1184 (D. Utah 1992) 30

Sigler v. Kobinsky,
2008 WI App. 183, 314 Wis.2d 784,
762 N.W.2d 706 (2008) 41

Silverman Partners, L.P. v. First Bank,
687 F. Supp. 2d 269 (E.D.N.Y. 2010) 28

Smith v. AmSouth Bank, Inc.,
892 So.2d 905 (Ala. 2004) 32

Smith v. Citibank (South Dakota), N.A.,
2001 WL 34079057 (W.D. Mo. Oct. 3, 2001) 28

Software Design & Application, Ltd. v. Hoefer & Arnett, Inc.,
56 Cal. Rptr. 2d 756 (Cal. App. 1996) 27

Sroka v. Compass Bank,
2006 WL 2535656 (Fla. Cir. Ct. Aug. 31, 2006) 27

Sterner v. Penn,
583 S.E.2d 670 (N.C. App. 2003) 28

Tensfeldt v. Haberman,
2009 WI 77, 319 Wis.2d 329, 768 N.W.2d 641 (2009) 50

Terry v. Bank of Am., N.A.,
350 F. Supp. 2d 727 (W.D. Va. 2004) 29

Tobias v. County of Racine,
179 Wis.2d 155, 507 N.W.2d 340 (Ct. App. 1993) 43

U.S. Bank Nat'l Ass'n v. Whitney,
81 P.3d 135 (Wash. App. 2003) 29

U.S. Commodity Futures Trading Commission v. Cook,
No. 09-cv-03332, 2010 WL 431595
(D. Minn. Jan. 27, 2010) 8

United States v. Cook,
No. 10-cr00075 (D. Minn. Aug. 25, 2010) 8

Volpe v. Fleet Nat'l Bank,
710 A.2d 661 (R.I. 1998)... 29

Weil v. First Nat'l Bank,
983 P.2d 812 (Colo. App. 1999)... 27

Weiss v. National Westminster Bank, PLC,
453 F. Supp. 2d 609 (E.D.N.Y. 2006)....................................... 56

Williamson v. Liptzin,
539 S.E.2d 313 (N.C. Ct. App. 2000).. 25

Willier, Inc. v. Hurt,
2007 WL 4613033 (S.D. W. Va. Dec. 31, 2007)........................ 29

Winslow v. Brown,
125 Wis.2d 327, 371 N.W.2d 417 (Ct. App. 1985).............. 51, 55

Wyatt v. Gilmore,
290 S.E.2d 790 (N.C. Ct. App. 1982)... 25

Wymore State Bank v. Johnson International Co.,
873 F.2d 1082 (8th Cir. 1989)... 30, 31

Zabka v. Bank of Am. Corp.,
127 P.3d 722 (Wash. App. 2005)................................... 26, 27, 29

Statutes & Regulations

12 C.F.R. § 21.11(k).. 46

31 U.S.C. § 5318(g)(2)(A)(i)... 46

31 U.S.C. § 5322.. 46

Miscellaneous

Restatement (Second) Law of Torts § 876(b) (1979)...................... 56

ISSUES PRESENTED FOR APPEAL

(1) The Wisconsin Supreme Court has held that in the circumstances of this case – where a non-customer sues a bank for failing to prevent fraud committed by a customer – a bank's duty of care requires *only* that, upon the non-customer notifying the bank of a fraud, the bank temporarily freeze its customer's account. Given this express holding, can a third party that did not give the bank such notice nonetheless maintain a suit for negligence, asserting that a bank was negligent in its monitoring of customer accounts?

*The circuit court answered **no**.*

(2) Does a circuit court possesses discretion to adjudicate public policy limitations on tort liability prior to a trial on the merits?

*The circuit court answered **yes**.*

(3) Do public policy considerations bar a negligence claim brought by noncustomers asserting that a bank is liable for failing to detect and prevent fraud by a bank customer against a third party?

*The circuit court answered **yes**.*

(4) Is a circuit court justified in dismissing an aiding and abetting claim where the plaintiff fails to plead that a defendant intended to aid the tortious conduct?

The circuit court answered ***yes***.

STATEMENT ON ORAL ARGUMENT AND PUBLICATION

Because the circuit court correctly applied settled Wisconsin law, Associated Bank does not request oral argument. Associated Bank takes no position as to whether resolution of this matter necessitates publication.

STATEMENT OF THE CASE

Plaintiffs have sued Associated Bank, N.A. ("Associated") to recover substantial sums they lost as victims of an international investment fraud. Associated, however, did not conduct the fraudulent activity; it did not know that fraud was occurring; and it surely did not intend for the plaintiffs to be defrauded. Plaintiffs do not contend otherwise.

Instead, plaintiffs assert that Associated is liable for negligence because it failed to detect that one of its customers was using a normal deposit account and routine banking services for fraudulent ends. Plaintiffs also contend that Associated aided and abetted the fraudulent conduct.

The circuit court properly dismissed this suit because these theories fail as a matter of law. In Wisconsin, "one has a duty to exercise ordinary care *under the circumstances*." *Hoida, Inc. v. M & I Midstate Bank*, 2006 WI 69, ¶ 30, 291 Wis.2d 283, 717 N.W.2d 17 (2006) (emphasis added). Applying that principle, the Wisconsin Supreme Court has firmly delineated a bank's duty of care in the circumstances at issue here – i.e., where a bank's customer is alleged to have defrauded a non-customer. In these particular circumstances,

a bank's duty of care requires *only* that – upon the non-customer notifying the bank of a fraud – the bank freeze its customer's account for sufficient time to permit the non-customer to initiate legal action. Thus, it is incumbent upon non-customers to be vigilant as to attempts to defraud them, to notify the bank, and then to initiate legal process so that deposited funds are frozen pursuant to court order.

That is precisely what the circuit court held here. It found plaintiffs' theory "is made out of just thin air," asking the court to "cobble together a cause of action." R.40:16. The court explained "that unless there is notice to the bank of some irregularity … from a third party,… the bank has no duty to a third party." *Id.* at 17.

This rule is well founded: the national banking system relies on the fundamental principle that a bank must honor its contractual duties to its customers. As the Wisconsin Supreme Court and dozens of courts around the country have held, it simply is not a reasonable duty to require banks to police the activities of their accountholders for the benefit of non-customers. To hold otherwise would, as the circuit court concluded, "create out of nowhere a liability upon a bank and therefore upon the banking industry, a liability for which … it would be near impossible to make a calculus of what the risk of doing

business would be." R.40:18. Plaintiffs' theory, if accepted, would thus lead to limitless liability upon banks for the acts of any miscreant with a bank account, with no clear guidance on how far a bank must go to ferret out another's misconduct, nor what a bank, depending on its degree of suspicion, must do to shield itself from liability.

The circuit court also correctly dismissed plaintiffs' aiding and abetting claims. Intent is an element of that tort, but plaintiffs do not even attempt to allege that Associated Bank intentionally aided the fraudsters.

FACTUAL HISTORY

A. Associated Bank.

Associated, headquartered in Green Bay, Wisconsin, was formed in 1970 by the merger of several community banks. Associated has 291 offices – many tracing their roots to the 1880s or 1890s – and serves 160 communities in Wisconsin, Illinois, and Minnesota. Associated employs over 5,200 residents of these states and provides a range of banking services.

B. The Crown Forex Fraud.

From around July 2006 through July 2009, a Minnesota corporation, Oxford Global Partners LLC, and its Canadian and

Minnesota promoters (collectively the "Oxford Fraudsters" or "the fraudsters") committed a massive investment fraud. R.2:8, ¶ 32. The Oxford Fraudsters raised over $158 million from at least 900 investors by selling investments in a purported foreign currency trading program. They promised investors returns of 10% to 12% with little risk. In truth, however, it appears that the Oxford Fraudsters lost substantial sums of investors' monies, misappropriated these funds for personal uses, misrepresented the finances of the investment fund, and committed several other wrongful acts. R.2:1, ¶ 2.

Among numerous other accounts at a variety of banks, the Oxford Fraudsters opened a bank account at Associated. The fraudsters apparently directed several investors – including the plaintiffs here – to deposit funds in its account at Associated. Plaintiffs to this action allege that they deposited funds in Crown Forex's account at Associated between March 4 and May 28, 2009. R.2:16-17, ¶¶ 68-72. The fraudsters then moved these funds to other accounts and banks, ultimately misappropriating them. R.2:14, ¶ 58.

In November 2009, the Commodity Futures Trading Commission filed a civil suit and the Securities and Exchange Commission filed an enforcement action against the Oxford

Fraudsters. *See U.S. Commodity Futures Trading Commission v. Cook*, No. 09-cv-03332, 2010 WL 431595, at *1 (D. Minn. Jan. 27, 2010); *SEC v. Cook*, No. 09-cv-03333 (D. Minn., filed Nov. 23, 2009). A receiver has been appointed in both actions and has been aggressively pursuing assets from the fraudsters for the benefit of the victims. *See* Order Continuing Appointment of the Temporary Receiver, *U.S. Commodity Futures Trading Commission v. Cook*, No. 09-cv-03332 (D. Minn. Dec. 11, 2009); Order granting Motion to Appoint Receiver, *SEC v. Cook*, No. 09-cv-03333 (D. Minn. Nov. 23, 2009).

In March 2010, the United States filed criminal charges against Trevor Cook. He pleaded guilty, and was sentenced to 25 years imprisonment and also ordered to pay $158,211,092.34 in restitution. Sentencing Judgment at 2, 5, *United States v. Cook*, No. 10-cr00075 (D. Minn. Aug. 25, 2010).

C. This Litigation.

Plaintiffs, a handful of the Oxford Fraudster's victims, brought suit against Associated in the circuit court on October 27, 2009. Plaintiffs have not named the Oxford Fraudsters as defendants in this action.

Plaintiffs first allege that Associated was negligent for failing to detect the Crown Forex fraud. R.2:18-19, ¶¶ 76-83. Plaintiffs assert that "even the bare minimum due diligence and investigation" would have uncovered the fraud. *Id.*:17, ¶ 75. Notwithstanding the alleged obviousness of the scheme, plaintiffs do not allege (in the complaint or at oral argument) that they themselves ever provided Associated with notice of the fraud. R.40:13-14.

Plaintiffs also assert two aiding and abetting theories, arguing that Associated aided and abetted the Oxford Fraudsters in breaching a fiduciary duty (R.2:19-21, ¶¶ 84-91) and in conversion (*id.*:21-22, ¶¶ 92-99). Plaintiffs do not allege, however, that Associated intended to help the fraudsters commit these acts.

Associated moved to dismiss for failure to state a claim. The circuit court heard oral argument and stated the basis for its dismissal on April 7, 2010. The court entered an order dismissing the complaint on April 29, 2010.

SUMMARY OF ARGUMENT

The circuit court properly dismissed all claims against Associated Bank. Plaintiffs' negligence theories fail on multiple grounds. In these circumstances, the Wisconsin Supreme Court has

clearly held that a bank's duty of care requires, and *only* requires, that the bank freeze its customers' accounts upon notice of an adverse claim from a non-customer. This rule is correct; nearly every court that has considered the question has declined to impose any greater duty. Nor is the rule unduly harsh; rather, it allows banks to honor their obligations to their own customers and creates predictability and order essential to the national banking system. Plaintiffs can find no recourse in federal banking regulations, as they neither provide a private cause of action nor alter the well-established rule delimiting the scope of a bank's duty in these circumstances.

Additionally, public policy considerations bar the plaintiffs' claim. If plaintiffs could bring an action for negligence under the circumstances here, banks would instantly be subject to vast, unforeseeable, and unpredictable tort liability; whenever an individual were to commit fraud, plaintiffs subsequently would assert a claim for negligence against the bank where the fraudster kept funds. But Wisconsin law does not tolerate such far-reaching and tenuous theories of liability.

The circuit court was also correct to dismiss the aiding and abetting claim. Plaintiffs do not and cannot allege that Associated

intended the fraudulent scheme. Indeed, plaintiffs expressly allege that *if* Associated had knowledge of the fraud, it would have acted to *prevent* it.

ARGUMENT

I. The Circuit Court Properly Dismissed The Negligence Claim.

A. Plaintiffs Fail To Allege That Associated Breached The Applicable Duty Of Care.

Summary: The circuit court properly dismissed the negligence claim because plaintiffs fail to state a cause of action. Wisconsin law is clear: in the circumstances in which a non-customer alleges it was defrauded by a bank customer, a bank's duty of care requires it to take action only upon notice of the fraud from the non-customer. *See Commercial Discount Corp. v. Milwaukee W. Bank*, 61 Wis.2d 671, 687, 214 N.W.2d 33 (1974).

To state a claim for negligence, the plaintiff's allegations must establish "(1) the existence of a duty of care on the part of the defendant, (2) a breach of that duty of care, (3) a causal connection between the defendant's breach of the duty of care and the plaintiff's injury, and (4) actual loss or damage resulting from the breach." *Hoida,* 2006 WI 69, ¶ 23 (alterations and internal quotation marks omitted; quoting *Gritzner v. Michael R.*, 2000 WI 68, ¶ 19, 235 Wis.2d 781, 611 N.W.2d 906 (2000)).

The circuit court concluded that plaintiffs' allegations do not establish that Associated breached a duty of care under these circumstances. R.40:17. The court explained "that unless there is notice to the bank of some irregularity … from a third party,… the bank has no duty to a third party." *Id.* The court found that the plaintiffs' theory "is made out of just thin air," asking the court to "cobble together a cause of action." *Id.* at 16.

The circuit court was correct. A bank's duty does not extend to affirmatively investigating its clients' activities for possible fraud. Although plaintiffs attempt to find refuge in out-of-state authority, Wisconsin law marches in lockstep with the approach taken by courts across the country. And as numerous of these courts have concluded applying the same principles that the Wisconsin Supreme court has adopted in other contexts, because federal banking regulations do not establish a private cause of action, they have no bearing on the common law duty a bank owes non-customers.

1. *The Wisconsin Supreme Court has held that a bank's duty of care does not require it to detect the fraudulent acts of its accountholders under these circumstances.*

a. The plaintiffs' claim for negligence must fail because, under Wisconsin law, given the circumstances of this case, a bank's duty of care does not require it to undertake the actions the Complaint alleges Associated failed to take. As the Supreme Court explained in *Hoida*, "duty[] involves two aspects: (1) the existence of a duty of ordinary care; and, (2) an assessment of what ordinary care requires under the circumstances." 2006 WI 69, ¶ 27. Accordingly, "a court first must decide whether the defendant owed a duty to the plaintiff." *Id.* ¶ 28. *See also Hocking v. City of Dodgeville*, 2009 WI 70, ¶ 11, 318 Wis.2d 681, 768 N.W.2d 552 (2009) ("Duty has always been a relevant element in Wisconsin's negligence analysis even though cases have more often been limited by the application of public policy factors."). Where there is "no duty under the circumstances, no breach occurred, and there [is] not a viable negligence claim." *Hocking*, 2009 WI 70, ¶ 13.

On two separate occasions, the Wisconsin Supreme Court has considered the "circumstances" where a non-customer asserts a claim

against a bank for failing to detect and prevent the fraudulent misconduct of a bank customer. In both cases, the Court held that in those particular circumstances, "ordinary care" does not require the bank to take any action absent notice from the non-customer of the alleged fraud.

In *Commercial Discount Corp. v. Milwaukee Western Bank*, 61 Wis.2d 671, 687, 214 N.W.2d 33 (1974), the Wisconsin Supreme Court held that: "the only duty owed by a bank to a third person claiming money deposited is not to release the deposit to the depositor unreasonably soon after the claimant makes known his adverse claim." As the court further explained, "the bank owes the third party no duty of inquiry. It only owes the third party claimant a duty to wait a reasonable time after notice of the claim to allow the claimant to begin legal action." *Id.* at 688. Plaintiffs do not contend otherwise; they readily concede that "*Commercial Discount* held that a defendant bank was not liable for funds diverted by a fraudster account holder unless it had specific knowledge of the fraud." Pl. Br. 24.

Plaintiffs nonetheless seek to distinguish *Commercial Discount* on the basis that it addresses aiding and abetting liability rather than negligence. Pl. Br. 24. But the Court's reasoning applied generally to

"tort," and is equally applicable to negligence. It explained that "the liability of a bank to an adverse claimant to a deposit is based on tort and ... to constitute a 'tort' there must be a duty owing by one party to another and a breach of that duty." *Commercial Discount*, 61 Wis.2d at 687.

Moreover, although plaintiffs' first cause of action against Associated is couched as "negligence," plaintiffs' negligence theory is otherwise indistinguishable from the "aiding and abetting" theory in *Commercial Discount.* The crux of the theory that the Court considered in *Commercial Discount* was that the defendant bank debited funds from its customer's account even though the bank "knew or should have known of the plaintiff's interest in the funds on deposit" because the bank had the "means of knowledge." *See Commercial Discount*, 61 Wis.2d at 679, 687. This is no different than plaintiffs' negligence theory here: that Associated is liable because it could have detected the fraud.

Plaintiffs' attempt to distinguish *Commercial Discount* because it adopts Iowa law and "Iowa has not adopted Wisconsin's universal duty of care" (Pl. Br. 25) also is wholly unpersuasive. In *Commercial Discount*, the Supreme Court adopted its own characterization of

Gendler v. Sibley State Bank, 62 F. Supp. 805 (N.D. Iowa 1945), as binding law for Wisconsin. *See Commercial Discount*, 61 Wis.2d at 688 (incorporating relevant aspects of *Gendler* as "the applicable law" in Wisconsin). At least two decades earlier, the Wisconsin Supreme Court had adopted the universal duty standard of care in *Pfeifer v. Standard Gateway Theater, Inc.* 262 Wis. 229, 55 N.W.2d 29 (1952), and restated the principle repeatedly thereafter. *See, e.g.*, *Cirillo v. City of Milwaukee*, 34 Wis.2d 705, 711, 150 N.W.2d 460 (1967); *Kemp v. Wis. Elec. Power Co.*, 44 Wis.2d 571, 581, 172 N.W.2d 161 (1969).

Against this historical backdrop, there can be no doubt that when the Wisconsin Supreme Court decided *Commercial Discount* – and adjudicated the scope of a bank's duties when the bank "receiv[es] a deposit of money belonging [not to its customer but] to another person" (61 Wis.2d at 687) – it did so with full recognition of the universal standard of care Wisconsin had long-since adopted. *Commercial Discount* plainly delineates the duty of care a bank owes in these circumstances.

A circuit court recently read *Commercial Discount* precisely this way. *See Ralph v. Bank One Wisconsin*, No. 00-cv-010774 (Wis.

Cir. Nov. 7, 2001); R.16. The Court of Appeals, in an unpublished opinion, affirmed that judgment in its entirety. *See Ralph v. Bank One Wis.,* 2003 WI App. 22, 259 Wis.2d 933, 657 N.W.2d 439 (Ct. App. 2002).

In *Ralph*, the plaintiff – who had no relationship with the defendant bank – sued, alleging that the bank failed to detect the fraudulent conduct of its depositor. R.22:28-32. The plaintiff's allegations were notably similar to those here: the plaintiff alleged that the bank was negligent, in part, by failing to question or stop certain unusual and irregular transactions by which the fraudster withdrew funds and also for failing to detect that the customer was not a valid business entity. *Id.* For example, although the fraudster told the bank she was going to use the funds for a complex investment, she withdrew funds for personal travel expenses, an automobile, a home equity loan, and credit card debt. *Id.* Applying *Commercial Discount*, the court found that:

> The bank has no duty to question the transactions or to regulate the transactions or to refuse to comply with the transactions requested by the depositor. They can only delay payment if notice of a potential problem is brought to their attention, and the plaintiff did not bring such notice to their attention. Without that notice, they must

> pay on the demand amounts requested by the depositor. They have no other option.

R.16:11 (Hearing Tr., 10/29/2001, at 11). The court also rejected the view that *Commercial Discount* was limited to aiding and abetting cases.

The Wisconsin Supreme Court quite recently confirmed the limited scope of a bank's duty of care to noncustomers in *Hoida*. There, a customer of the bank "fraudulently misappropriated approximately $650,000 of the project's construction loan proceeds." 2006 WI 69, ¶ 1. A subcontractor filed suit against the bank, arguing that the bank was negligent for failing to detect the customer's fraudulent conduct. *Id.* Like plaintiffs here, the subcontractor pointed to asserted "basic industry standards," such as supposed obligations "to identify the subcontractors and materialmen for the project; to verify that sufficient work on the project had been completed to 'justify disbursement'; and to collect lien waivers." *Id.* ¶ 20. And just like plaintiffs in this action, the subcontractor contended that "if the [bank] does not complete these tasks, it is reasonably foreseeable that subcontractors and materialmen will be harmed." *Id.*

The court firmly rejected the subcontractor's negligence theory, holding that "[the bank's] duty of care under the circumstances did not include the obligation to undertake" the fraud prevention tasks that the subcontractor "[sought] to impose" on it. *Hoida*, 2006 WI 69, ¶ 39. That is because the subcontractor had "no special relationship, such as a fiduciary relationship" with the bank. *Id.* ¶ 34. The court in *Hoida* thus recognized that a bank's duty does not extend to detecting and preventing fraudulent activities by its customers, even in the face of asserted industry standard practices.

Plaintiffs' attempts to escape *Hoida* are unavailing. They suggest that *Hoida* supports their view that "a contextual approach to duty" is necessary. Pl. Br. 23. That contention does not advance plaintiffs' argument because this is exactly how the circuit court approached the issue here. In *Hoida*, the Court examined the litany of "basic industry standards" that the subcontractor contended created a duty of care for the bank, and rejected wholesale the notion that detecting and preventing fraud by its customer against a third party was within the ambit of the bank's duties. Likewise, here the circuit court considered "industry standards" and concluded that Associated does not owe a duty of care to plaintiffs in light of the circumstances.

R.40:8-9 (considering duty in light of regulations on banking industry).

Plaintiffs assert that no "red flags" were present in *Hoida*. But that is not what the subcontractor pleaded in that matter. Rather, the subcontractor, just like the plaintiffs here, pleaded that the bank missed several warning signs that could have been helpful in avoiding the eventual fraud. *Hoida*, 2006 WI 69, ¶ 20. For example, the plaintiff there claimed that industry standards required the bank to investigate a lien on the project and to assess whether sufficient construction work had occurred prior to disbursing additional funds, either of which the plaintiff contended could have detected the fraud. *Id*.

Plaintiffs are also wrong to contend that *Hoida*'s holding is inapplicable here because, in that case, the bank's contract with its fraudster customer limited its liability. To be sure, the bank contractually disclaimed certain duties to the fraudster. *Hoida*, 2006 WI 69, ¶ 38. But the subcontractor's claims were not predicated on a contractual relationship – indeed it had none with the bank – but on general negligence theory. The defendant bank in *Hoida* certainly

could not contractually disclaim tort liability to an entity with which it had no contractual relationship.

Plaintiffs' contract argument also misses a more fundamental point in *Hoida*: where a contract already governs the relationship between two parties, courts should be reluctant to impose an inconsistent or differing duty in tort. 2006 WI 69, ¶¶ 38-39. Thus, given that a bank has a contract only with its customer, "a bank deposit account is for the benefit and convenience of the depositor." *Commerical Discount*, 61 Wis. at 687. If the non-customer wishes to interfere with ordinary functioning of that contractual relationship, it is "claimant's duty to promptly institute necessary legal proceedings to stop payment to [a] depositor by a court order or process." *Id.*

Like *Commercial Bank, Hoida* teaches that the precept – that there is 'duty owed to the world' – does not mean that the duty is boundless. In *Hoida*, Justices Bradley and Butler dissented based on the exact same theory that plaintiffs now ask this Court to adopt. The dissent contended that the *Hoida* majority had misapplied *Gritzner*, 2000 WI 68, and *Alvarado v. Sersch*, 2003 WI 55, ¶ 18, 262 Wis.2d 74, 662 N.W.2d 350 (2003) – the same two cases on which plaintiffs primarily rely (Pl. Br. 18). *See Hoida*, 2006 WI 69, ¶¶ 56, 57

(Bradley, J., dissenting). The dissent expressly acknowledges that the majority "limits liability based on duty" (*id.* ¶ 65), and the dissenters would have instead held that "the *existence* of a duty is always present in an ordinary negligence determination" (*id.* ¶ 73). In rejecting this position, the *Hoida* majority plainly concluded that the scope of duty must be tailored to the circumstances, and that it would not be reasonable to impose a broad duty in the context of a claim against a bank for failing to prevent losses to noncustomers.

Plaintiffs' position presumes that the *Hoida* dissent had carried the day. It did not. Nor has this view had success following *Hoida*. For example, just last year in *Hocking*, that Court, citing *Hoida*, explained that "[w]hile Wisconsin has adopted the minority view from *Palsgraf v. Long Island Railroad,* 162 N.E. 99 (N.Y. 1928), which established that everyone owes a duty to the world at large, the duty owed to the world is not unlimited but rather is restricted to what is reasonable under the circumstances. *Hoida*, 291 Wis.2d 283, ¶¶ 30-32." *Hocking*, 2009 WI 70, ¶ 12. Plaintiffs simply cannot ignore *Hoida*'s fundamental teaching.

Associated does not suggest that *Commercial Discount* and *Hoida* overrule cases like *Gritzner* and *Alvarado*. However, they

serve to establish – unequivocally – the scope of the duty of care of a bank in precisely the circumstances before this Court. That is to say, in the particular circumstances of a claim by non-customers against a bank for failing to detect or prevent a bank customer from defrauding them, a bank's duty does not extend to monitoring its customer's accounts for fraudulent activities. The Wisconsin Supreme Court has rejected imposing such a broad duty on banks. Instead, a bank's duty to non-customers claiming an interest in customer funds is far narrower: upon notice by a claimant, it must freeze customer funds for a reasonable period to permit judicial action. This duty, as plaintiffs admit, is not implicated here.

Not only is this the clear law of Wisconsin, but it is a fundamentally sound rule. A bank simply cannot be tasked with investigating all its customers for possible fraud; as the circuit court concluded, this is an impossible duty. *See* R.40:18. And, as the court in *Ralph* explained, it is a duty that would interfere with a bank's obligation to "pay on the demand amounts requested by the depositor" that is essential for the banking system to function. R.16:11. Commercial *Discount* and *Hoida* thus foreclose plaintiffs' negligence claim.

b. Perhaps recognizing that their claim is not cognizable under Wisconsin law, plaintiffs seek refuge in the law of other states. Pl. Br. 19-21. Plaintiffs' endeavor is misguided because, as *Commercial Discount*, *Hoida*, and *Ralph* demonstrate, plaintiffs are wrong to assert that the question here is one "of first impression under Wisconsin law." *Id.* at 19. The Court need not look outside Wisconsin in order to adjudicate this case.

Regardless, out-of-state law unquestionably demonstrates that *Commercial Discount*, *Hoida*, and *Ralph* (as well as the conclusion of the court below and the position advocated by Associated here) are firmly aligned with the overwhelming majority approach. As the United States Court of Appeals for the Fourth Circuit recently explained, "[c]ourts in numerous jurisdictions have held that a bank does not owe a duty of care to a noncustomer with whom the bank has no direct relationship." *Eisenberg v. Wachovia Bank, N.A.*, 301 F.3d 220, 225 (4th Cir. 2002) (collecting several cases).

Eisenberg – which was decided under the law of North Carolina, a state that, like Wisconsin, follows the *Palsgraf* dissent[1] – rejected a claim materially indistinguishable from the claim plaintiffs press here. There, a fraudster opened an account at the defendant bank in the name of "Bear Stearns." *Eisenberg*, 301 F.3d at 222. The defendant bank's policies did "not restrict the name under which a new customer may open a bank account" and the bank's employees "did not verify that [the fraudster] was authorized to operate under the name Bear Stearns." *Id.* Misrepresenting himself as a vice president of Bear Stearns, the fraudster directed the victims to deposit funds with the defendant bank, which he then withdrew and converted. *Id.*

The victims sued the bank, alleging that it "negligently allowed [the fraudster] to establish and operate a fraudulent bank account" and was "liable for its employee's negligence in allowing [the fraudster] to open the bank account without proper verification." *Eisenberg*, 301 F.3d at 222. The Fourth Circuit, however, was "persuaded by the

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[1] *See Williamson v. Liptzin*, 539 S.E.2d 313, 319 (N.C. Ct. App. 2000) ("[T]he plaintiff does not have to prove that the defendant foresaw the injury in its precise form. … *see also* Palsgraf … (Andrews, J., dissenting)."); *Wyatt v. Gilmore*, 290 S.E.2d 790, 791 (N.C. Ct. App. 1982) (same).

reasoning articulated in the numerous cases holding that a bank does not owe noncustomers a duty of care." *Id.* at 227. The court explained that holding otherwise "would be contrary to the normal understanding of the purpose of a bank account and would expose banks to unlimited liability for unforeseeable frauds." *Id.* at 226.

A Washington state appellate court has followed *Eisenberg* in another case with facts highly analogous to those alleged here. *See Zabka v. Bank of Am. Corp.*, 127 P.3d 722 (Wash. App. 2005). Plaintiffs, at the fraudster's direction, transferred funds to accounts at the defendant bank. *Id.* at 722-23. They sued the bank, providing evidence that the bank "failed to follow standard procedures and monitor transactions according to its own internal standards." *Id.* at 725. The court nonetheless rejected the plaintiffs' negligence claim, explaining that "[m]any other jurisdictions have held that third party non-customers are not owed a duty of care by a bank . . . ." *Id.* at 724. As the court further noted, "the bank was not in the best position to protect the [plaintiffs] – the [plaintiffs] were. Had they investigated [the fraudsters], or demanded paperwork and evidence of legitimacy of those entities themselves, their injury could have been avoided." *Id.* at 725.

Eisenberg and *Zabka* represent the predominant view as to the scope of a bank's duty of care to non-customers. State and federal courts in at least twenty-seven states have likewise concluded that, as a general matter, banks owe no duty of care to non-customers: Arizona,[2] Arkansas,[3] California,[4] Colorado,[5] Connecticut,[6] Florida,[7] Georgia,[8] Illinois,[9] Iowa,[10] Kansas,[11] Louisiana,[12] Maryland,[13]

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[2] *Kesselman v. Nat'l Bank*, 937 P.2d 341, 343 (Ariz. App. 1996) ("A bank has no duty to third parties to disclose information about a customer's account.").

[3] *Old Republic Nat'l Title Ins. Co. v. Landmark Closing Co.*, 2010 WL 2228436, at *2 (E.D. Ark. June 1, 2010) ("The general rule in Arkansas and elsewhere is that banks do not owe noncustomers a duty to exercise reasonable care.").

[4] *Software Design & Application, Ltd. v. Hoefer & Arnett, Inc.*, 56 Cal. Rptr. 2d 756, 760 (Cal. App. 1996) ("[A]bsent extraordinary and specific facts, a bank does not owe a duty of care to a noncustomer.").

[5] *Weil v. First Nat'l Bank*, 983 P.2d 812, 814 (Colo. App. 1999) ("Courts in other jurisdictions have generally held that a bank does not owe such duties of care to a noncustomer.")

[6] *Sheiman v. Lafayette Bank & Trust Co.*, 492 A.2d 219, 222 (Conn. App. Ct. 1985).

[7] *Sroka v. Compass Bank*, 2006 WL 2535656, at *1 (Fla. Cir. Ct. Aug. 31, 2006) ("[A]s a matter of law, a bank does not owe a duty to non-customers regarding the opening and maintenance of its accounts").

[8] *Promissor, Inc. v. Branch Bank & Trust Co.*, 2008 WL 5549451, at *5 (N.D. Ga. Oct. 31, 2008) (there is a "host of persuasive authority standing for the proposition that a bank owes no duty to a noncustomer in the opening of an account").

Massachusetts,[14] Michigan,[15] Missouri,[16] New Jersey,[17] New York,[18] North Carolina,[19] North Dakota,[20] Ohio,[21] Rhode Island,[22] South

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[9] *Athey Products Corp. v. Harris Bank Roselle*, 89 F.3d 430, 435 (7th Cir. 1996) (Illinois law) ("[A] lender owes no duty to protect third parties from the credit risk of an insolvent borrower.").

[10] *Gendler*, 62 F. Supp. 805.

[11] *ALG, Inc. v. Estate of Eldred,* 35 P.3d 931, 934 (Kan. App. 2001).

[12] *Guidry v. Bank of LaPlace*, 740 F. Supp. 1208, 1218 (E.D. La. 1990) ("[I]t is well established Louisiana law that a bank ... owes absolutely no duty, fiduciary or otherwise, towards third persons with whom a [bank] customer does business."), *aff'd*, 954 F.2d 278 (5th Cir. 1992).

[13] *Nat'l Union Fire Ins. Co. v. Allfirst Bank*, 282 F. Supp. 2d 339, 345 (D. Md. 2003).

[14] *McCallum v. Rizzo*, 1995 WL 1146812, at *2 (Mass. Super. Ct. Oct. 13, 1995) ("[T]here is an abundance of precedent from other jurisdictions holding that a bank owes no duty of care to third parties who are not bank customers.")

[15] *Portage Aluminum Co. v. Kentwood Nat'l Bank*, 307 N.W.2d 761 (Mich. App. 1981).

[16] *Smith v. Citibank (South Dakota), N.A.*, 2001 WL 34079057, at *2 (W.D. Mo. Oct. 3, 2001) ("[B]anks do not owe a duty to noncustomers").

[17] *Brunson v. Affinity Fed. Credit Union*, 972 A.2d 1112, 1123 (N.J. 2009).

[18] *Gesell v. First Nat'l City Bank*, 260 N.Y.S.2d 581, 581-82 (N.Y. App. Div. 1965) (per curiam); *Silverman Partners, L.P. v. First Bank*, 687 F. Supp. 2d 269, 281 (E.D.N.Y. 2010) ("Generally, banks owe no duty of care to their non-customers.").

[19] *Sterner v. Penn*, 583 S.E.2d 670, 672-73 (N.C. App. 2003).

[20] *Schleicher v. W. State Bank,* 314 N.W.2d 293, 297 (N.D. 1982).

[21] *Loyd v. Huntington Nat'l Bank*, 2009 WL 1767585, at *13 (N.D. Ohio June 18, 2009) ("Generally courts have held that a depositary bank does not owe any duty to a non-customer.").

Dakota,[23] Texas,[24] Utah,[25] Virginia,[26] Washington,[27] and West Virginia.[28] Plaintiffs ask this Court to stand against the consistent practices of courts in dozens of other states.

Plaintiffs' reference to scattershot cases does nothing to undercut the substantial weight of this authority. Unlike *Eisenberg* and *Zabka*, cases that address situations almost identical to those alleged here, plaintiffs' out-of-state authority is factually dissimilar and represents fringe positions that have been routinely and specifically rejected by courts across the country.

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[22] *Volpe v. Fleet Nat'l Bank*, 710 A.2d 661, 664 (R.I. 1998) ("[T]he bank owes no duty of care to a noncustomer with whom it has no relationship.").

[23] *Gilbert v. United Nat'l Bank*, 436 N.W.2d 23, 27 (S.D. 1989) ("Courts have recognized that a stranger to a bank-depositor relationship is owed no duty in the absence of a contract, statute, or other special circumstance giving rise to such a duty.").

[24] *Mazon Assocs., Inc. v. Comerica Bank*, 195 S.W.3d 800, 807 (Tex. App. 2006).

[25] *Ramsey v. Hancock*, 79 P.3d 423, 427 (Utah App. 2003) ("[A] bank does not owe a duty to a noncustomer payee.").

[26] *Terry v. Bank of Am., N.A.*, 350 F. Supp. 2d 727, 729 (W.D. Va. 2004) ("The plaintiffs acknowledge that a bank ordinarily owes no duty of care to a noncustomer.").

[27] *U.S. Bank Nat'l Ass'n v. Whitney*, 81 P.3d 135, 141 (Wash. App. 2003) ("A bank owes no duty of care to a noncustomer with whom it has no relationship.").

[28] *Willier, Inc. v. Hurt*, 2007 WL 4613033, at *8 (S.D. W. Va. Dec. 31, 2007).

Plaintiffs cite (Pl. Br. 20) *Wymore State Bank v. Johnson International Co.*, 873 F.2d 1082, 1086 (8th Cir. 1989), a case that involved the question of whether Section 3-405 of the Uniform Commercial Code – which addresses fictitious payees when an employee writes a fraudulent check – acts as a defense to a negligence claim. The Eighth Circuit found that the UCC did not provide such a defense and permitted the claim to proceed. Of course, the UCC is not at issue in this case.

Moreover, the "overwhelming majority of jurisdictions" have rejected *Wymore*. *Shearson Lehman Bros., Inc. v. Wasatch Bank*, 788 F. Supp. 1184, 1193 (D. Utah 1992) (collecting cases). As one court recently summarized, "[i]n cases where a noncustomer asserted a negligence claim against a bank for failing to prevent a customer of the bank from depositing stolen checks, the overwhelming majority of courts have ruled that the bank did not owe a duty of reasonable care to the noncustomer." *Shane Smith Enters., Inc. v. Bank of Am., N.A.*, 2007 WL 1880201, at *2 (E.D. Ark. June 29, 2007). For example, the New York Court of Appeals has concluded that "a bank's negligence is irrelevant under UCC 3-405." *Prudential-Bache Sec., Inc. v. Citibank, N.A.*, 536 N.E.2d 1118, 1124 (N.Y. 1989). A federal court

in Wisconsin has likewise held that a bank has no tort liability in such circumstances. *See Prudential Ins. Co. v. Marine Nat'l Exch. Bank*, 371 F. Supp. 1002, 1003 (E.D. Wis. 1974).

Nor do plaintiffs find support in *Patrick v. Union State Bank*, 681 So. 2d 1364 (Ala. 1996). There, an impostor, using a stolen temporary driver's license, opened an account in plaintiff's name and. passed bad checks. This led to plaintiff's arrest. *Id.* at 1365-66. Plaintiff then sued the bank for negligence. *Id.* at 1366. The bank argued that it had no duty of care because it had "absolutely no relationship" with the plaintiff. *Id.* at 1369. The court disagreed as a matter of fact: "[t]he bank undeniably *thought* that it had a relationship with [the plaintiff] when it opened the account for, and gave checks to, an impostor." *Id.* Here, however, there simply is no relationship between the plaintiffs and Associated.

Patrick (like *Wymore*) also has been roundly rejected by other courts. As the New Jersey Supreme Court explained last year, "[t]he expansive holding in *Patrick* ... has met with near universal disapproval." *Brunson v. Affinity Fed. Credit Union*, 972 A.2d 1112, 1123 (N.J. 2009). That court explained that "[w]ithin its own state, *Patrick* has been distinguished,... and its value as precedent has been

limited exclusively to a repetition of the elements of a common law tort. In other jurisdictions, *Patrick* has fared far worse. Federal courts either have rejected or limited *Patrick's* import. Courts in other states have been equally reticent to embrace *Patrick's* reach." *Id.* at 1123-24 (extensive citations omitted).[29] Following the majority lead, *Brunson* rejected *Patrick*, concluding it would not create "a new cause of action for negligent investigation" against a bank, so as not to "impose a duty of care on banks in respect of a total stranger." *Id.* at 1125.

The circuit court was not only correct in its interpretation of *Commercial Discount* and *Hoida*, but its decision also lies within the heartland of modern tort jurisprudence. Courts across the country routinely refuse to recognize negligence claims against banks brought by total strangers. Looking outside Wisconsin simply reaffirms the

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[29] As *Brunson* explained, it appears *Patrick* has been largely rejected even by the court that decided it. The Alabama Supreme Court has since noted that "[e]very court that has examined the issue has answered that banks owe no duty of care to noncustomers." *Smith v. AmSouth Bank, Inc.*, 892 So.2d 905, 909 n.2 (Ala. 2004). A federal court opined that "the opinion in *Smith* suggests that Alabama would, if asked, join the courts that have ruled that banks owe no duty of care to noncustomers." *Shane Smith Enters.*, 2007 WL 1880201, at *2.

correctness of this State's approach to the duty of care a bank owes non-customers.

2. *Federal banking regulations do not set or expand a bank's common law duties.*

In contending that Associated was negligent, plaintiffs heavily rely on supposed "red flags" – which plaintiffs identify now with the benefit of hindsight – that they allege federal banking regulations should have caused Associated to spot. But despite the long history of federal regulations guiding bank conduct, courts have consistently rejected imposing a common-law duty of care grafted from these regulations.

To begin, it is clear that the federal banking regulations on which plaintiffs rely do not themselves create a private cause of action. *See B.E.L.T., Inc. v. Wachovia Corp.*, 403 F.3d 474, 476 (7th Cir. 2005) (regulation requiring banks to report "'any known or suspected Federal criminal violation'" did not create a private cause of action); *Hanninen v. Fedoravitch*, 583 F. Supp. 2d 322, 326 (D. Conn. 2008); *Carran v. Morgan*, 2007 WL 3520480, at *5 (S.D. Fla. Nov. 14, 2007) ("Of course, there is no private right action for failure

to file a suspicious activity report."). Plaintiffs do not suggest otherwise.

Instead, plaintiffs contend that Associated's supposed failure to adhere to these standards supports a common law cause of action. But as abundant authority demonstrates, because the Wisconsin Legislature and the U.S. Congress have declined to create private causes of action for the asserted regulatory violations that plaintiffs allege, plaintiffs cannot create a backdoor common-law tort remedy. In *In re Agape Litigation*, 681 F. Supp. 2d 352, 360 (E.D.N.Y. 2010), for example, the plaintiffs (victims of a Ponzi-scheme who sued the bank at which their funds were deposited) attempted to bolster their negligence claim by alleging that the bank "breached a duty of care imposed by the monitoring requirements of the Bank Secrecy Act." *Id.* The court, restating "the general rule that banks do not owe non-customers a duty to shield them against intentional torts committed by bank customers" (*id*), rejected this theory: "because the Bank Secrecy Act does not create a private right of action, the Court can perceive no sound reason to recognize a duty of care that is predicated upon the statute's monitoring requirements." *Id.*

Likewise, in *Marlin v. Moody Nat'l Bank N.A.*, 2006 WL 2382325, at *7 (S.D. Tex. Aug. 16, 2006), where the plaintiffs alleged that "the Bank Secrecy Act imposes a duty on banks to investigate, prevent money laundering, and report suspicious activity," the court flatly rejected this argument:

> The obligation under that statute is to the government rather than some remote victim. The obligation is not to roam through its customers looking for crooks and terrorists. By that act, banks do not become guarantors of the integrity of the deals of their customers. It does not create a private right of action and, therefore, does not establish a standard of care.

Id. So too in *Armstrong v. Am. Pallet Leasing Inc.*, 678 F. Supp. 2d 827, 875 (N.D. Iowa 2009) ("Because the Bank Secrecy Act does not permit a private right of action, it follows that it cannot be construed as giving rise to a duty of care flowing to plaintiffs in this case.") and *Aiken v. Interglobal Mergers & Acquisitions*, 2006 WL 1878323, at *2 (S.D.N.Y. July 5, 2006) (rejecting plaintiffs' attempt to bootstrap asserted violations of the Bank Secrecy Act and the Patriot Act into a negligence because the court may not "impose a duty of care based upon a statute that does not permit a private right of action"). Courts have consistently and uniformly rejected attempts to smuggle federal banking regulations into state tort actions.

That is precisely the approach taken by the lower court here. The court noted that "the banking industry is among the most highly regulated industries that we have. It is regulated at the Federal level. It is regulated at the State level.... [N]owhere do I hear anyone saying that any banking regulation that would carry with it some duty that the civil courts could ... enforce." R.40:8. It thus concluded that if the banking industry "should be subjected to the type of lawsuits that would be suggested in this case," such a decision "should be made by the State Legislature." *Id.*:17-18.

Whether private liability should stem from a bank's purported failures to catch certain regulatory "red flags" is a question left solely to the legislatures. "[T]he judiciary is limited to applying the policy the legislature has chosen to enact, and may not impose its own policy choices." *Fandrey ex rel. Connell v. Am. Family Mut. Ins. Co.*, 2004 WI 62, ¶ 16, 272 Wis.2d 46, 680 N.W.2d 345 (2004). Particularly given that federal and state legislatures heavily regulate the banking industry, this Court must resist plaintiffs' efforts to create a common-law backdoor to claims that the legislatures have declined to adopt. *Cf. Hoida*, 2006 WI 69, ¶ 48 ("We cannot establish a common law

claim that would contravene [a] legislative choice. If a new claim is to be established ..., it is for the legislature to do so, not this court.").

B. Public Policy Forecloses The Plaintiffs' Claims.

Summary: The circuit court was correct both in adjudicating the public policy limitations at this stage in the proceeding and in holding that those limits must foreclose plaintiffs' claims.

Wisconsin law holds that "even when a duty of care exists and the other elements of negligence have been established, public policy considerations may preclude liability." *Gritzner*, 2000 WI 68, ¶ 24. Thus, irrespective of whether Associated owes a duty of care in the particular circumstances of this case, dismissal of this suit is appropriate because the underlying claim runs contrary to this State's long-standing public policy principles.

The circuit court correctly concluded that public policy precludes the manipulation of tort law "to create out of nowhere a liability upon a bank and therefore upon the banking industry, a liability for which the Court is satisfied it would be near impossible to make a calculus of what the risk of doing business would be." R.40:18. As the circuit court explained, plaintiffs' theory would require a bank "to be alerted ... to be watching every depositor in

their account ... on some screening methodology of which none exists." *Id.*

The circuit court was equally correct to conclude that it had discretion to decide the application of public policy limitations at this time. The court explained that it has an "obligation, because of the enormous expense of litigation, to stop litigation at the very threshold if a Court is satisfied that it has no merit.... [T]o require defendants and for that matter plaintiffs to expend thousands of dollars developing a lawsuit to which a trial court judge is satisfied has no merit is an enormous injustice ...." R.40:18-19. Considering public policy at "the threshold level," the court found, is necessary to "cease[] costly litigation." *Id.*: 20.

1. *The circuit court properly exercised its discretion to adjudicate the public policy factors at this juncture.*

a. Although this Court reviews the lower court's decision with respect to the merits of the public policy question *de novo*, the circuit court's decisions as to docket and trial management – including its decision to consider public policy factors at this stage of the proceeding – is subject to review for an abuse of discretion only. *See Schneller v. St. Mary's Hosp. Med. Ctr.*, 162 Wis.2d 296, 305-06,

470 N.W.2d 873 (1991) (modification of scheduling order reviewed for abuse of discretion); *In re D.S.*, 142 Wis.2d 129, 133-34, 416 N.W.2d 292 (1987) (wide discretion of court to apply procedural statutes). The decision as to when to decide the public policy question is no different than any other form of discretionary trial management decision concerning the order in which evidence or arguments will be heard. Lest there be any doubt, plaintiffs concede that "a circuit court has ***discretion*** to consider whether to preclude liability at an earlier stage." Pl. Br. 28 (emphasis added).

A court abuses its discretion only if it "failed to exercise its discretion or if there was no reasonable basis for its decision." *Robertson-Ryan & Assocs., Inc. v. Pohlhammer*, 112 Wis.2d 583, 587, 334 N.W.2d 246 (1983); *Schneller*, 162 Wis.2d at 306 ("The test is not whether this court as an original matter would have denied the motion; it is whether the circuit court abused its discretion in doing so.").

b. There is no basis to reverse the lower court's discretionary decision to address the public policy question at the early stages of the litigation. The Wisconsin Supreme Court has made clear that "where the facts are simple to ascertain and the public

policy questions have been fully presented," it is permissible for a court to "review public policy and preclude liability before trial." *Alvarado*, 2003 WI 55, ¶ 18. "The application of public policy considerations is solely a function of the court, and does not in all cases require a full factual resolution of the cause of action by trial before policy factors will be applied by the court." *Hass v. Chicago & Nw. Ry.*, 48 Wis.2d 321, 326-27, 179 N.W.2d 885 (1970) (citation omitted). This is particularly true where, like here, "the record ... indicates that in rendering the judgment on the pleadings, the trial judge fully addressed the policy issues he found determinative." *Schuster v. Alternberg*, 144 Wis.2d 223, 241, 424 N.W.2d 159 (1988).

Indeed, scores of courts have adjudicated the public policy question prior to a trial on the merits. *See, e.g.*, *Hornback v. Archdiocese of Milwaukee*, 2008 WI 98, ¶ 52, 313 Wis.2d 294, 752 N.W.2d 862 (2008); *Fandrey*, 2004 WI 62, ¶ 6; *Gritzner*, 2000 WI 68, ¶ 5; *Sawyer v. Midelfort*, 227 Wis.2d 124, 141, 595 N.W.2d 423 (1999); *Miller v. Wal-Mart Stores, Inc.*, 219 Wis.2d 250, 265, 580 N.W.2d 233 (1998); *Bowen v. Lumbermens Mut. Cas. Co.*, 183 Wis.2d 627, 655, 517 N.W.2d 432 (1994); *Schuster*, 144 Wis.2d at 241; *Antoniewicz v. Reszcynski*, 70 Wis.2d 836, 839, 236 N.W.2d 1

(1975); *Rieck v. Med. Protective Co.*, 64 Wis.2d 514, 517, 219 N.W.2d 242 (1974); *Hass*, 48 Wis.2d at 322; *Sigler v. Kobinsky*, 2008 WI App. 183, ¶ 12, 314 Wis.2d 784, 762 N.W.2d 706 (2008); *Cefalu v. Cont'l W. Ins. Co.*, 2005 WI App. 187, ¶ 20, 285 Wis.2d 766, 703 N.W.2d 743 (2005); *Estate of Paswaters v. Am. Family Mut. Ins. Co.*, 2004 WI App. 233, ¶ 13, 277 Wis.2d 549, 692 N.W.2d 299 (2004). Resolving public policy at this juncture is no extraordinary measure.

The facts alleged here, as relevant to public policy, are straightforward: plaintiffs assert that Associated is liable for a multi-million dollar, international investment fraud committed by an Associated Bank customer, because Associated, like plaintiffs themselves, failed to detect any wrongdoing. The circuit court correctly found that Wisconsin public policy does not permit such broad and unpredictable liability to be imposed on financial institutions. As shown below, that determination did not depend on resolving the factual questions plaintiffs suggest, such as "what level of inquiry a bank must engage in when opening a new account" or "what level of monitoring of accounts a bank must undertake." Pl. Br. 28. To the contrary, whether the public policy of this State permits a non-customer third party to assert a negligence claim against a bank

under these circumstances is not a close question, and no further factual development is needed to conclude that the circuit court correctly decided this issue.

The circuit court's determination here – that no set of facts, if proven by plaintiffs, could overcome this public policy limitation on state tort law – is an eminently "reasonable basis for its decision" to resolve this issue at the outset. *Robertson-Ryan*, 112 Wis.2d at 587.

2. *Public policy forecloses any liability to Associated in these circumstances.*

The circuit court correctly applied the public policy factors to find that Associated cannot be held liable based on plaintiffs' allegations here. Several public policy factors may foreclose liability on a negligence claim, including:

> (1) [T]he injury is too remote from the negligence, (2) the injury is too wholly out of proportion to the tortfeasor's culpability, (3) in retrospect it appears too highly extraordinary that the negligence should have resulted in the harm, (4) allowing recovery would place too unreasonable a burden on the tortfeasor, (5) allowing recovery would be too likely to open the way for fraudulent claims, and (6) allowing recovery would enter a field that has no sensible or just stopping point.

Gritzner, 2000 WI 68, ¶ 27. "[I]f any one of the six ... criteria is satisfied, [a court] must relieve the negligent defendant of liability."

Giebel v. Richards, 224 Wis.2d 468, 474-75, 591 N.W.2d 901 (Ct. App. 1999). Here, several factors support the decision to block the plaintiffs' claims against Associated.

a. Remoteness. A tort claim is foreclosed as too remote when the injury is too "removed or separated from the negligence in time, place, or sequence of events." *Beacon Bowl, Inc. v. Wis. Elec. Power Co.*, 176 Wis.2d 740, 762, 501 N.W.2d 788 (1993). In *Tobias v. County of Racine*, 179 Wis.2d 155, 162, 507 N.W.2d 340 (Ct. App. 1993), the court held that, under the remoteness doctrine, "[t]he act of a third person in committing an intentional tort or crime is a superseding cause" that cuts off negligence liability. The only exception is if the defendant could foresee "that a third person would commit a crime against [plaintiff] *because of* the opportunity created by the [defendant's] negligence." *Id.*, 179 Wis.2d at 163 (emphasis in original).

Here, the Oxford Fraudsters' crimes are not alleged to have occurred *"because of"* any "opportunity" that Associated Bank is alleged to have created. To the contrary, the complaint's allegations make clear that the fraud had been going on for several years before any of the Oxford Fraudsters opened an account at Associated. Even

assuming lapses in Associated's compliance policy, there is no basis for concluding that those lapses made a multimillion dollar, international criminal fraud a "likelihood" – particularly given that the fraud pre-dated the alleged lapses. *Giebel*, 224 Wis.2d at 475-76 (garbage arson was not a "likelihood" from defendant having negligently allowed garbage to accumulate; reversing negligence judgment).

b. Burden. Liability is also inappropriate because, as a matter of law, "allowance of recovery would place an unreasonable burden on the [allegedly] negligent" party. *Fandrey*, 2004 WI 62, ¶ 15 n.12 (internal quotation marks omitted). Here, plaintiffs seek to impose on banks an obligation to detect customer wrongdoing based on so-called "red flags." Plaintiffs identified these red flags only with the benefit of hindsight, and many of the supposed red flags were instead reasonable transactions for an international investment company, *e.g.*, "large dollar wire transfers were received … [and] followed shortly thereafter by large dollar wire transfers out"; transfers were directed to "offshore banking centers in high-risk jurisdictions." R.2:14-15, ¶¶ 59, 60.

If such scant and debatable clues were sufficient to impose liability, banks would have to attempt to analyze millions of transactions – an exceedingly expensive proposition that is almost certain to fail and be second-guessed. As the circuit court explained, under this approach, it would be "near impossible [for a bank] to make a calculus of what the risk of doing business [with any particular customer] would be." R.40:18.

Moreover, even if a bank were to "detect" (R.2:7, ¶ 29) possible fraud by identifying red flags, that alone would do nothing to help fraud victims. To benefit persons like the plaintiffs – and what these plaintiffs would require the bank to do upon "detecting" the fraud – the bank would have to (1) freeze the accounts at issue, (2) alert law enforcement, and (3) alert plaintiffs so that they could pursue the frozen assets. Requiring banks to freeze accounts based on such so-called "indicia" of fraud not only would place an undue burden on them (and would expose them to customer suits disputing their *ad hoc* extrajudicial decisions to freeze deposited assets), but also would burden their customers, commerce, and the interstate banking system.

As for alerting law enforcement, the proper means for banks to do so, pursuant to federal regulations, is through the filing of

Suspicious Activity Reports ("SARs"). To avoid tipping off criminals, however, federal law strictly prohibits banks from revealing if and when they have filed SARs. *See* 31 U.S.C. § 5318(g)(2)(A)(i) (protecting confidentiality of SARs); 12 C.F.R. § 21.11(k) (same); 31 U.S.C. § 5322 (imposing criminal penalties for violations of these provisions). A bank may not reveal that it has filed a SAR even to defend itself against allegations – like plaintiffs' here – that the bank failed to alert the authorities. *Id.* Imposing liability based on allegations that a bank is criminally prohibited from contradicting is the epitome of an unreasonable burden. Similarly, it *must* be contrary to public policy to extend to banks a duty to notify non-customers of suspicious activity of their customers – it would undercut, if not violate, the federal law that *prohibits* banks from disclosing when they have filed a SAR.

Plaintiffs suggest that their proposed liability theory does not establish too great a burden because "[m]any jurisdictions impose liability on banks in similar circumstances." Pl. Br. 33. But, as recounted above (*see*, *supra*, 24-32), this claim could not be farther from the truth. Courts around the country specifically decline to impose such liability precisely because it would impose far too great a

burden on financial institutions. Indeed, as the circuit court recognized, under the plaintiffs' theory there is no way for a bank to manage its risk. R.40:5. Rather, a bank "would never know from one day to the next whether they are on the hook for a 100 million dollars." *Id.* at 5-6.

c. **Proportionality.** Additionally, plaintiffs' claim must fail because the asserted injury is not proportional to the negligent conduct alleged. This factor requires comparing "the degree of negligence and the degree of injury." *Fandrey*, 2004 WI 62, ¶ 15 n.12 (internal quotation marks omitted). Plaintiffs predominately fault Associated for administrative shortcomings, relying chiefly on allegations that "Associated Bank's compliance program and/or its execution of that program were deficient" (R.2:8, ¶ 30) and fell short of "federal banking regulations" (*id.*:2, ¶ 4). For this alleged conduct, Plaintiffs would hold Associated liable for a $100+ million Ponzi scheme, committed by an international network of criminals over several years. Imposing liability would be disproportionate because the wrong alleged to have been committed by Associated cannot compare to the massive intentional torts committed by the Oxford Fraudsters. *Cf. Fandrey*, 2004 WI 62, ¶¶ 33-35 (holding that

negligence in leaving door unlocked was disproportionate to dog bite friend's child suffered upon entering house).

d. No just or sensible stopping point. In *Fandry*, the court held that "[p]erhaps the strongest factor weighing against imposing liability" on homeowners who negligently failed to lock their door, which allowed a friend's child to enter the home and suffer a dog bite injury, was that such liability would lack a sensible or just stopping point: "For example, were we to allow liability here, the door would be open to imposing liability on a homeowner when a burglar enters his or her home and is injured." 2004 WI 62, ¶¶ 36, 39. The same problem applies here. If a bank is to be liable if it (negligently) fails to detect, and then report and/or freeze criminal proceeds, the door is open for banks to be held liable for all injuries caused (even outside the U.S.) by petty narcotics traffickers who use a local bank account to facilitate crimes. There is simply no limit to the reach of criminal misconduct for which a party could assert a bank is liable. Public policy forecloses such extenuated theories of liability.

Plaintiffs contend that banking regulations would provide a meaningful limit to the liability of the banks. Pl. Br. 34. But as plaintiffs' brief makes clear, the regulations are highly subjective:

banks file SARs if a transaction is "suspicious" and, as plaintiffs assert, "[t]he level of due diligence and investigation that banks must perform is not the same for all customers or for all accounts." Pl. Br. 8. Accordingly, the legislature left enforcement of those regulations to bank supervisors with no financial incentive to find fault. For just the same reasons, those regulations cannot provide meaningful boundaries to tort liability.

Likewise, plaintiffs offer no stopping point to the reach of their liability theory. They allege that the Oxford Fraudsters transferred certain monies from Associated Bank to accounts at other banks. R.2:14, ¶ 58. Presumably those banks could become liable for negligence, too, should plaintiffs' theory be accepted. And liability may extend yet further. For example, if the investors themselves were negligent in providing money to a fraudulent scheme without first performing due diligence, under plaintiffs' theories the investors would become cross-liable to each other. That is to say, under plaintiffs' theory, if plaintiffs had exercised reasonable care when making the investment and thus uncovered the fraudulent scheme, every investor could have had an opportunity to blow the whistle to

the benefit of others. Public policy, however, limits liability from extending so far.

II. The Circuit Court Properly Dismissed The Aiding And Abetting Claims.

Summary: The circuit court properly concluded that plaintiffs' aiding and abetting theories must fail because plaintiffs cannot allege that the Bank intended to aid the Oxford Fraudsters.

The circuit court was likewise correct to conclude that plaintiffs' aiding and abetting claims fail as a matter of law. As Associated's briefing clearly spelled out to that court, the complaint falls far short of alleging the requisite intent necessary for an aiding and abetting theory. And this issue is now squarely before this court and ripe for adjudication.

In order to hold an individual liable for the intentional torts of another via an aiding and abetting theory, a plaintiff must plead and then prove both an *actus reas* as well as *mens rea*. Thus, "[a] person is liable in tort for aiding and abetting if the person (1) undertakes conduct that as a matter of objective fact aids another in the commission of an unlawful act; and (2) consciously desires or intends that his conduct will yield such assistance." *Tensfeldt v. Haberman*, 2009 WI 77, ¶ 26 n.12, 319 Wis.2d 329, 768 N.W.2d 641 (2009).

Intent is thus an essential element of an aiding and abetting theory: "Mere presence, with no effort to prevent unlawful conduct, is not aiding and abetting unless an intent to assist is communicated." *Winslow v. Brown*, 125 Wis.2d 327, 336-37, 371 N.W.2d 417 (Ct. App. 1985). *See also Coopman v. State Farm Fire & Cas. Co.*, 179 Wis.2d 548, 562, 508 N.W.2d 610 (Ct. App. 1993) ("A person is liable in a civil action for aiding and abetting if the person undertakes conduct that aids another in the commission of an unlawful act *and the person consciously desires or intends that his conduct will yield such assistance*." (emphasis added)). Without intent, there can be no aiding and abetting liability.

Indeed, when a plaintiff "only raises an inference" that a defendant "knowingly agreed to accompany" a tortfeasor in an intentional tort, this is insufficient to raise a triable question of fact for a jury. *Winslow*, 125 Wis.2d at 336. Instead, a plaintiff must plead supportable factual allegations that a defendant actually intended for the tort to occur. And the plaintiff must do so by "set[ting] forth a statement of circumstances, occurrences and events in support of the claim presented." *Doe v. Archdiocese of Milwaukee*, 2005 WI 123, ¶

36, 284 Wis.2d 307, 700 N.W.2d 180 (2005) (internal quotation marks omitted).

Plaintiffs never allege that Associated Bank *intended* to assist the Oxford Fraudsters. Plaintiffs offer no fact, circumstance, or occurrence to suggest that Associated desired or intended for the Oxford Fraudsters to commit intentional torts against the plaintiffs. Quite to the contrary, plaintiffs asserted that if Associated had known of the fraud, it would have acted to stop it. *See* R.2:2, ¶ 4 (knowledge of the fraud "would have ... caused Associated Bank to freeze the accounts and immediately report the suspicious facts and circumstances to law enforcement"). Indeed, this assertion is the crux of their negligence theory. Plaintiffs argue that Associated was negligent because, in their view, if Associated had known about the fraudulent conduct, it would have somehow acted.

Perhaps recognizing this sizable hole in their legal theory, plaintiffs suggest (Pl. Br. 38) that a jury could infer intent simply from the bank's presence at the commission of a tortious act. That is incorrect; this precise argument has been flatly rejected by Wisconsin courts. For example, one court explained that the "mere presence" of a defendant at the scene of a tortious act coupled with "the fact that

they made no effort to prevent the unlawful conduct, is not sufficient to impose liability." *Edwardson v. Am. Family Mut. Ins. Co.*, 223 Wis.2d 754, 765, 589 N.W.2d 436 (Ct. App. 1998) (internal quotation marks omitted). Wisconsin law has held for well over a hundred years that "mere presence at the commission of an assault and battery, or other wrongful act, does not render a person liable as a participator therein." *Rinehart v. Whitehead*, 64 Wis. 42, 24 N.W. 401 (1885) (internal quotation marks omitted).

Fredrickson v. Kabat, 266 Wis. 442, 63 N.W.2d 756 (1954), is not to the contrary. Plaintiffs' selective citation of *Fredrickson* distorts its holding. Plaintiffs cite *Fredrickson* as follows:

> [E]vidence that a person is present at the commission of an assault and battery, without disapproving or opposing it, is evidence from which … the jury may infer that he assented thereto, and lent to it his countenance and approval, and was thereby aiding and abetting the same.

Pl. Br. 38 (quoting *Fredrickson*, 266 Wis. at 446-47). But the portion plaintiffs omit from the quote changes its entire meaning. The quote in whole actually reads:

> [E]vidence that a person is present at the commission of an assault and battery, without disapproving or opposing it, is evidence from which, ***in connection with other circumstances***, the jury may infer that he assented

> thereto, and lent to it his countenance and approval, and was thereby aiding and abetting the same.

Fredrickson, 266 Wis. at 446-47 (emphasis added; internal quotation marks omitted). This is no trivial omission. The preceding sentence explains that "[a] mere bystander at the commission of an assault and battery does not become liable as a participant because he does not interfere to prevent it." *Id.* at 47. Thus *Fredrickson* squarely stands for the proposition that presence alone is never a sufficient basis by which a jury can find intent.

Fredrickson itself illustrates that a defendant's presence at the commission of a tort is only relevant when there exist "other circumstances" evidencing a defendant's intent. There, Frederickson sued several defendants for assault. The jury found one defendant, Kabat, liable via an aiding and abetting theory. As the Wisconsin Supreme Court explained, Kabat could only be held liable because there were *other circumstances* indicating his intent in addition to his mere presence:

> Such 'other circumstances' which the jury could and doubtless did connect and consider are that Kabat's conduct inside the club caused Fredrickson to eject him, that Kabat particularly resented this because, as he testified, he was a veteran and Fredrickson 'was probably not even overseas', that his friends were acting

> to avenge him and that he used foul language to Fredrickson immediately after their act. Kabat has not attempted to disassociate himself from the others of his group.

Fredrickson, 266 Wis. at 447.

Plaintiffs' argument that Associated was "willfully blind" (Pl. Br. 39) is simply a different way of alleging that Associated was present at the commission of the intentional tort and took no steps to prevent the fraud. Even if true, this fails to show that Associated ever harbored the requisite intent for the underlying tort violations plaintiffs allege the Oxford Fraudsters committed. Try as they might, plaintiffs cannot dispense with the intent requirement of aiding and abetting under Wisconsin law.

Although plaintiffs' inability to allege intent on the part of Associated is, by itself, fatal to the aiding and abetting theories, the claims fail for an additional reason: routine banking services provided to customers cannot qualify as "substantial assistance" (or "objective fact") necessary to establish aiding and abetting liability.

Winslow explained that an essential element of aiding and abetting liability is that an individual "as a matter of objective fact" actually aids the underlying violation. *Winslow,* 125 Wis.2d at 335.

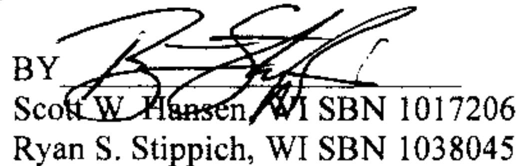
Applying the Restatement (Second) Law of Torts § 876(b) (1979), which requires a plaintiff to prove that a defendant provided "substantial assistance," *Winslow* explained that "[t]he 'substantial assistance or encouragement' requirement is comparable to the 'assistance as a matter of objective fact' requirement . . . ." *Winslow,* 125 Wis.2d at 336.

Plaintiffs cannot meet this showing here because normal banking activities, such as the maintenance of bank accounts, cannot count as such substantial assistance. For example, *Weiss v. National Westminster Bank, PLC*, 453 F. Supp. 2d 609, 621 (E.D.N.Y. 2006), explained that "[t]he mere maintenance of a bank account and the receipt or transfer of funds" cannot "constitute substantial assistance." Plaintiffs' theory thus must be rejected on this alternative basis.

CONCLUSION

For the foregoing reasons, Associated Bank respectfully requests that this Court affirm the trial court's judgment.

Dated this 11th day of October, 2010.



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COURT OF APPEALS OF WISCONSIN
DISTRICT III

Herman Grad *et al.*,

Plaintiffs-Appellants,

v. Appeal No. 10-AP-1461

Associated Bank, N.A., Circuit Court No. 09-CV-2949

Defendant-Respondent.

FORM AND LENGTH CERTIFICATION

I hereby certify this brief conforms to the rules contained in section 809.19(8)(b) of the Wisconsin Statutes for a brief and appendix produced with a proportional serif font. This brief conforms to the length limitations set forth in Wis. Stat. Rule 809.19(8)(c) as the brief is 10,925 words.

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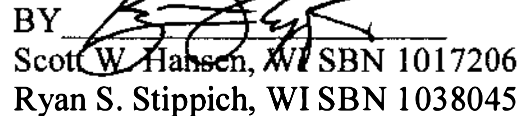

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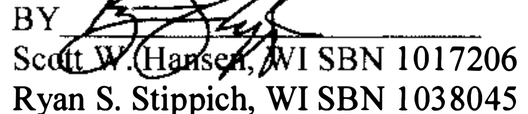

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Circuit Court No. 09-CV-2949

CERTIFICATE OF SERVICE

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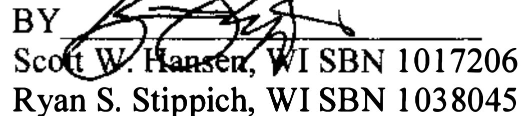
BY 
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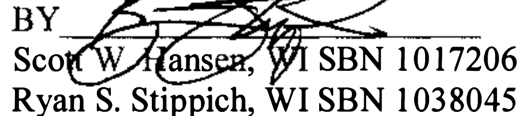

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