

**IN THE IOWA DISTRICT COURT FOR POLK COUNTY**

<b>LUANA SAVINGS BANK,</b>  <b>Plaintiff,</b>  vs.  <b>FEDERAL HOME LOAN BANK OF DES MOINES,</b>  <b>Defendant.</b>	<b>Case No. EQCE085919</b>  <b>ORDER RE: DEFENDANT’S MOTION TO DISMISS</b>
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**I. INTRODUCTION**

The court has before it defendant Federal Home Loan Bank of Des Moines’ (“FHLB”) motion to dismiss filed on December 23, 2020. Plaintiff Luana Savings Bank (“LSB”) filed a resistance on January 19, 2021. The court heard the parties’ arguments at a hearing on February 19, 2021. Kevin J. Driscoll, Jessica McKinney, and Todd W. Ruskamp represented FHLB. John E. Lande represented LSB. The court now enters its order on the motion.

**II. FINDINGS OF FACT**

FHLB is one of eleven federally-established banks created by the Federal Home Loan Bank Act.<sup>1</sup> It is privately-capitalized and owned as a cooperative by its member institutions.<sup>2</sup> FHLB allows its members access to a stable source of collateralized loans or advances that members can use to support mortgage lending, economic development, and affordable housing in the communities FHLB serves.<sup>3</sup> To maintain funds, FHLB is self-capitalizing.<sup>4</sup> To become a member of FHLB and to receive advances, an institution must purchase FHLB activity-based stock.<sup>5</sup>

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<sup>1</sup> Answer to Amended Petition and Amended Counterclaims, at 10, ¶ 2 (Polk Cty Dist. Ct. Feb. 8, 2021).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.* at 10, ¶ 3.

<sup>4</sup> *Id.* at 10, ¶ 4.

<sup>5</sup> *Id.*

LSB is a member institution of FHLB and has been a participating financial institution (“PFI”) in FHLB’s Mortgage Partnership Finance (“MPF”) program since 2007.<sup>6</sup> The relationship between FHLB and LSB is governed by several contracts, including (1) a Master Transaction Agreement (“MTA”) dated June 11, 2018 and its attendant Guides, (2) an Advances, Pledge and Security Agreement (“APSA”) dated May 3, 2006, and (3) a Participating Financial Institution Agreement (“PFIA”) dated July 2, 2007.<sup>7</sup> FHLB also had a Capital Plan dated May 31, 2015.<sup>8</sup>

Under the MPF program, LSB sold thousands of residential mortgage loans to FHLB while retaining the servicing rights for the loans.<sup>9</sup> After a mortgage loan originated by LSB was closed, LSB sold the loan to FHLB.<sup>10</sup> In most cases, FHLB paid a premium to purchase the loan.<sup>11</sup> FHLB then held the mortgage loans on its balance sheet while LSB handled the servicing of the loans, which included billings to borrowers, payment collection, and customer service.<sup>12</sup>

LSB earned profits from receiving a premium on loans sold to FHLB and from collecting servicing fees over the life of the loan where it retained servicing rights.<sup>13</sup> FHLB expected to earn profits, which FHLB would distribute to member banks as dividends, through interest paid by borrowers over the life of the loans held by FHLB.<sup>14</sup>

In 2015, LSB asked FHLB whether LSB could repurchase loans it had previously sold to FHLB.<sup>15</sup> The PFIA and related FHLB guidelines do not permit members to repurchase loans

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<sup>6</sup> *Id.* at 10, ¶ 5.

<sup>7</sup> *Id.* at 10–11, ¶ 6.

<sup>8</sup> Amended Petition, at 2, ¶ 12 (Polk Cty Dist. Ct. Dec. 3, 2020).

<sup>9</sup> Answer to Am. Pet. and Am. Countercls., at 11, ¶ 7.

<sup>10</sup> *Id.* at 11, ¶ 8.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> Answer to Am. Pet. and Am. Countercls., at 11, ¶ 9.

<sup>14</sup> *Id.* at 11, ¶ 10.

<sup>15</sup> *Id.* at 11, ¶ 11.

without written permission.<sup>16</sup> FHLB advised LSB of these terms and did not grant LSB written permission to repurchase loans.<sup>17</sup>

Notwithstanding FHLB's response, LSB began to repurchase loans from FHLB under the guise of the underlying borrowers refinancing the loans.<sup>18</sup> LSB submitted payoff amounts on loans as the servicer, ostensibly as a result of a borrower refinancing the loan.<sup>19</sup> Because LSB was the loan servicer, upon payment of the loan balance, FHLB returned the original promissory note to LSB to be returned to the borrower.<sup>20</sup> Rather than immediately cancelling the note, LSB held the note and continued to collect monthly loan payments, including interest, and loan servicing fees without advising the borrower that it had paid the loan balance and now held the loan, rather than FHLB.<sup>21</sup> LSB would later advise the borrowers of refinancing opportunities.<sup>22</sup> LSB then sold loans for the same borrower and secured by the same property to FHLB a second time after refinancing the loan that LSB had repurchased from FHLB months earlier.<sup>23</sup>

In 2019, FHLB discovered LSB's actions and questioned LSB about the suspected conduct.<sup>24</sup> LSB acknowledged it had been repurchasing loans.<sup>25</sup> On March 2, 2020, FHLB provided notice to LSB of LSB's default under the governing documents due to unauthorized repurchases.<sup>26</sup>

LSB has a demand deposit account ("DDA") at FHLB to facilitate transactions with

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<sup>16</sup> *Id.* at 11, ¶ 12.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.* at 11, ¶ 13.

<sup>19</sup> *Id.*

<sup>20</sup> *Id.* at 12, ¶ 14.

<sup>21</sup> *Id.* at 12, ¶ 15.

<sup>22</sup> *Id.* at 12, ¶ 17.

<sup>23</sup> *Id.* at 12, ¶ 18.

<sup>24</sup> *Id.* at 12, ¶ 19.

<sup>25</sup> *Id.* at 12, ¶ 20.

<sup>26</sup> *Id.* at 12, ¶ 23.

FHLB.<sup>27</sup> According to § 4.2.2 of the Capital Plan, FHLB committed to repurchase its stock from LSB that exceeds the thresholds required for member stock holdings.<sup>28</sup> Section 2.2 of the Capital Plan states that FHLB should place proceeds from stock repurchases into LSB's DDA.<sup>29</sup> Since March 2020, FHLB has not paid proceeds from the repurchase of LSB's stock to the DDA, but instead placed the proceeds in a certificate of deposit where LSB cannot access the funds.<sup>30</sup>

Section 3.4 of the Capital Plan states that FHLB must pay any declared dividends on its stock to the members holding its stock.<sup>31</sup> FHLB has withheld certain declared dividends from LSB and placed the funds in the same certificate of deposit where LSB cannot access the funds.<sup>32</sup> The PFIA contains a broad setoff provision, which allows FHLB to withhold funds from LSB based on any indebtedness of LSB to FHLB.<sup>33</sup>

The APSA secures advances that federal law authorizes FHLB to make to its member financial institutions.<sup>34</sup> Section 1 of the APSA states, "Nothing contained in this Agreement or the Member Policies and Procedures shall be construed as an agreement or commitment by the Bank to grant any Advance hereunder. The Bank expressly reserves its right and power to either grant or deny in its sole discretion any Advance."<sup>35</sup> Since FHLB discovered LSB's alleged misconduct, FHLB has denied LSB access to advances, including the ability to roll over current outstanding advances into a new term at a lower interest rate and overnight advances.<sup>36</sup> LSB is unable to utilize

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<sup>27</sup> Am. Pet. at 3, ¶ 22.

<sup>28</sup> *Id.* at 3, ¶ 16.

<sup>29</sup> *Id.* at 3–4, ¶ 23.

<sup>30</sup> *Id.* at 4, ¶¶ 24–25.

<sup>31</sup> *Id.* at 5, ¶ 34.

<sup>32</sup> *Id.* at 5, ¶ 35.

<sup>33</sup> Ex. C, PFIA, § 4.8.

<sup>34</sup> Am. Pet. at 5, ¶ 40.

<sup>35</sup> Ex. B, APSA, § 1.

<sup>36</sup> Am. Pet. at 6, ¶ 43.

low interest rates for funds FHLB previously advanced to LSB.<sup>37</sup> LSB does not have access to an important source of liquidity.<sup>38</sup>

On December 28, 2020, LSB missed a required payment to FHLB of \$10,000,000 for matured advances made by FHLB to LSB.<sup>39</sup> On December 30, 2020, FHLB issued a written notice of default and acceleration of advances to LSB declaring all advances and other charges due and payable as a result of LSB's defaults under the parties' agreements, including the payment default on December 28.<sup>40</sup> FHLB alleges LSB owes a principal balance of \$364,785,792.75 for advances as of December 30, 2020, plus accrued interest of \$771,174.17 and prepayment fees of \$14,624,539.41.<sup>41</sup>

On May 20, 2020, LSB filed its petition, alleging that FHLB is improperly withholding funds from stock repurchases and declared dividends. LSB sought relief in six counts: (I) declaratory judgment, (II) conversion, (III) breach of contract, (IV) promissory estoppel, and (V) unjust enrichment, and (VI) injunction. On June 19, 2020, FHLB filed its answer, affirmative defenses, and counterclaims, stating it was entitled to setoff due to LSB's contractual breaches, and asserting claims for breach of contract and negligent misrepresentation. LSB moved to dismiss FHLB's negligent misrepresentation claim on July 9, 2020. The court denied LSB's partial motion to dismiss on October 6, 2020.

LSB amended its petition on December 3, 2020. LSB added allegations that FHLB is improperly refusing to give LSB advances. LSB now seeks relief in nine counts: (I) declaratory judgment related to setoff, (II) declaratory judgment related to advances, (III) conversion, (IV)

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<sup>37</sup> *Id.* at 6, ¶ 45.

<sup>38</sup> *Id.* at 6, ¶ 46.

<sup>39</sup> Answer to Am. Pet. and Am. Countercls., at 14, ¶¶ 32–33.

<sup>40</sup> *Id.* at 14, ¶ 34.

<sup>41</sup> *Id.* at 14, ¶ 35.

breach of contract related to dividends and repurchase proceeds, (V) breach of contract related to advances, (VI) breach of fiduciary duty, (VII) promissory estoppel, (VIII) unjust enrichment, and (IX) injunction. On February 8, 2021, FHLB filed an answer to LSB's amended petition and amended counterclaims, wherein it denied the allegation in count III and refrained from answering for any of the other counts. FHLB now alleges counterclaims for (I) breach of contract related to loan repurchases, (II) breach of contract related to collateral delivery, (III) breach of contract related to payment default, (IV) negligent misrepresentation, (V) declaratory judgment, and (VI) injunction.

On December 23, 2020, FHLB filed a motion to dismiss counts I, II, IV, V, VI, VII, VIII, and IX of LSB's amended petition based on the failure to state a claim. FHLB argues it did not waive its ability to object to counts I, IV, VII, VIII, and IX when it filed its original answer, because LSB's filing of the amended petition gave FHLB another opportunity to file a motion to dismiss.

FHLB argues counts II and V fail, because the APSA reserves discretion for FHLB to decide whether to grant advances, the APSA did not incorporate federal regulations, and federal regulations give FHLB full discretion. FHLB argues count VI fails, because FHLB giving advances to LSB was an arms-length lender-borrower relationship. FHLB believes counts I, IV, and IX fail, because LSB does not have standing to enforce the capital plan, FHLB has some discretion about whether to repurchase stock, and the capital plan allows setoff. FHLB argues counts VII and VIII fail, because LSB's claims rely on written contracts, precluding recovery based on implied agreement.

On January 19, 2021, LSB filed a resistance. LSB argues FHLB waived its ability to object to counts I, IV, VII, VIII, and IX when it filed its original answer on June 19, 2020. LSB believes it stated a claim for counts II and V, because the APSA incorporated federal regulations that restrict

FHLB's discretion to not make advances. LSB argues it stated a claim for count VI, because it owns activity based stock in FHLB and because Congress intended FHLB to assist local communities beyond what a regular bank would do. LSB argues it stated a claim for counts I, IV, and IX, because it can enforce the capital plan as an intended beneficiary and the capital plan requires FHLB to repurchase stock and give the proceeds to LSB. Finally, LSB contends it stated a claim for counts VII and VIII, because it is pleading the implied contract claims in the alternative.

### III. STANDARD OF REVIEW

A court may grant a motion to dismiss based on (1) lack of subject matter jurisdiction, (2) lack of personal jurisdiction, (3) insufficiency of the original notice or its service, or (4) failure to state a claim upon which any relief may be granted.<sup>42</sup> “Under our rules of civil procedure, a party need not conform to technical forms of pleading.”<sup>43</sup> “Rather, ‘[e]ach averment of a pleading shall be simple, concise, and direct.’”<sup>44</sup> “In Iowa, ‘notice pleading’ is all that is required.”<sup>45</sup> “Nearly every case will survive a motion to dismiss under notice pleading.”<sup>46</sup> Notice pleading requires the petition “contain factual allegations that give the defendant ‘fair notice’ of the claim asserted so the defendant can adequately respond to the petition.”<sup>47</sup> “The ‘fair notice’ requirement is met if a petition informs the defendant of the incident giving rise to the claim and of the claim's general nature.”<sup>48</sup> A plaintiff is not required to set forth specific legal theories for recovery in the petition.<sup>49</sup> The only issue when considering a motion to dismiss is the “petitioner's right of access to the

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<sup>42</sup> Iowa R. Civ. P. 1.421(1).

<sup>43</sup> *Cemen Tech, Inc. v. Three D Industries, L.L.C.*, 753 N.W.2d 1, 12 (Iowa 2008).

<sup>44</sup> *Id.* (citing Iowa R. Civ. P. 1.402(2)(a)).

<sup>45</sup> *Id.* at 12.

<sup>46</sup> *U.S. Bank v. Barbour*, 770 N.W.2d 350, 353 (Iowa 2009).

<sup>47</sup> *Id.* at 354 (quoting *Rees v. City of Shenandoah*, 682 N.W.2d 77, 79 (Iowa 2004)).

<sup>48</sup> *Id.* at 354.

<sup>49</sup> *Cemen Tech, Inc.*, 753 N.W.2d at 12.

district court, not the merits of his allegations.”<sup>50</sup> “In determining whether to grant the motion to dismiss, a court views the well-pled facts of the petition ‘in the light most favorable to the plaintiff with doubts resolved in that party's favor.’”<sup>51</sup> “A motion to dismiss admits the allegations of the petition and waives any ambiguity or uncertainty in the petition.”<sup>52</sup> “A motion to dismiss is sustainable only when it appears to a certainty that the [the party seeking relief] would not be entitled to relief under *any state of facts that could be proved* in support of the claims asserted.”<sup>53</sup>

#### IV. CONCLUSIONS OF LAW

##### A. Waiver

LSB argues FHLB waived its ability to file a motion to dismiss for counts I, IV, VII, VIII, and IX when it filed its original answer on June 19, 2020. FHLB argues the amended petition resets the timing giving FHLB another opportunity to object for failure to state a claim.

“Motions attacking a pleading must be served before responding to the pleading . . . .”<sup>54</sup> “[A] motion to dismiss a pleading for failure to state a claim on which any relief can be granted must be filed before answer.”<sup>55</sup> Filing an answer constitutes a waiver of any motion to dismiss for failure to state a claim.<sup>56</sup>

In its amended petition, LSB re-plead the same six counts and added three new counts. The

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<sup>50</sup> *Rieff v. Evans*, 630 N.W.2d 278, 284 (Iowa 2001) (citations omitted).

<sup>51</sup> *Geisler v. City Council*, 769 N.W.2d 162, 165 (Iowa 2009) (citing *Haupt v. Miller*, 514 N.W.2d 905, 911 (Iowa 1994)).

<sup>52</sup> *Leuchtenmacher v. Farm Bureau Mut. Ins. Co.*, 460 N.W.2d 858, 861 (Iowa 1990).

<sup>53</sup> *Penn. Life Ins. Co. v. Simoni*, 641 N.W.2d 807, 810 (Iowa 2002) (emphasis added) (citation omitted).

<sup>54</sup> Iowa R. Civ. P. 1.441(1).

<sup>55</sup> *Johnston v. Percy Const., Inc.*, 258 N.W.2d 366, 370 (Iowa 1977).

<sup>56</sup> *Id.* See also *Powell v. Khodari-Intergreen Co.*, 303 N.W.2d 171, 174-75 (Iowa 1981) (motion to dismiss must be filed before answer); *Riediger v. Marrland Dev. Corp.*, 253 N.W.2d 915, 916 (Iowa 1977); *Grinnell State Bank v. Jones*, 884 N.W.2d 223 (Table), 2016 WL 1683119, at \*1 (Iowa Ct. App. Apr. 27, 2016) (filing of motion to dismiss seven months after the answer is untimely); *In re Marriage of Glade*, 501 N.W.3d 563, 565 (Iowa Ct. App. 1993).

fact that LSB reorganized its petition and re-filed the six counts does not reset the clock for FHLB. The six counts originally pled are the same in the amended petition and rely on the same factual allegations as set forth in the original petition. FHLB waived its motion to dismiss with respect to LSB's original claims by filing its answer on June 19, 2020. The filing of the amendment asserting three new claims does not allow FHLB to file a motion to dismiss on five of those six claims.<sup>57</sup> The court denies FHLB's motion to dismiss for counts I, IV, VII, VIII, and IX.

### **B. Obligation to Make Advances**

LSB argues that FHLB's discretion to decline to make advances to LSB is limited. LSB believes the APSA incorporates federal regulations that restrict FHLB's discretion. LSB contends that even if the APSA does not incorporate federal regulations, FHLB must still comply with the regulations. LSB alleges that FHLB exercised its discretion in bad faith and did not deny advances to LSB for one of the enumerated reasons in 12 C.F.R. section 1266.4(a).

FHLB argues it has full discretion whether to make advances to its member institutions. FHLB contends the APSA does not incorporate federal regulations and that federal regulations provide no private cause of action under which LSB can enforce the regulations. FHLB believes the APSA and the federal regulations provide FHLB unfettered discretion to deny advances to LSB.

FHLB argued it is under no contractual duty to make advances to LSB. Section 1 of the APSA gives FHLB full discretion about whether to make advances: "Nothing contained in this Agreement or the Member Policies and Procedures shall be construed as an agreement or commitment by the Bank to grant any Advance hereunder. The Bank expressly reserves its right and power to either grant or deny in its sole discretion any Advance."<sup>58</sup> In addition, FHLB

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<sup>57</sup> FHLB did not file a motion to dismiss on count III.

<sup>58</sup> Ex. B, APSA, § 1.

complied with the implied covenant of good faith and fair dealing. FHLB could not have exercised its rights under section 1 of the APSA in bad faith by declining to make advances to LSB. The implied covenant “does not give rise to new substantive terms that do not otherwise exist in the contract.”<sup>59</sup> The contract explicitly reserves FHLB’s right to decline to make advances to LSB. LSB bargained away its ability to object to FHLB’s exercise of discretion. FHLB complied with the implied covenant by exercising its right.

The APSA incorporates 12 C.F.R. section 1266.4(a)(2), but does not incorporate section 1266.4(a)(1). A recital of the APSA states: “WHEREAS, the Bank may from time to time make available extensions of credit to the Member (“Advances”), in accordance with the Federal Home Loan Bank Act, the regulations and directives of the Federal Housing Finance Board . . . .”<sup>60</sup> Incorporation requires a clear and specific reference to the extrinsic document or statute.<sup>61</sup> An express citation is not necessary for incorporation as long as the reference is clear and specific.<sup>62</sup> The extent to which an extrinsic document or statute becomes part of a contract may be limited to the purposes indicated in the contract.<sup>63</sup>

While the recital does not expressly cite section 1266.4, its reference to “the regulations and directives of the Federal Housing Finance Board” is sufficiently clear and specific. Other language in the recital limits which specific regulations the contract incorporates. The recital does not contain language imposing an obligation on FHLB to deny advances only based on the grounds in section 1266.4(a)(1). It states that FHLB “may from time to time make available” advances in

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<sup>59</sup> *Bagelmann v. First Nat. Bank*, 823 N.W.2d 18, 34 (Iowa 2012) (citation omitted).

<sup>60</sup> Ex. B, APSA, Recitals.

<sup>61</sup> *Longfellow v. Sayler*, 737 N.W.2d 148, 154 (Iowa 2007).

<sup>62</sup> *Johnson v. Baum*, 788 N.W.2d 397 (Table), 2010 WL 2757192, at \*3–\*4 (Iowa Ct. App. July 14, 2010).

<sup>63</sup> *Longfellow*, 737 N.W.2d at 154 (citing 11 Richard A. Lord, *Williston on Contracts* § 30:19, at 202 (4th ed. 1999)).

accordance with federal regulations. The word “may” indicates the recital gives FHLB discretionary authority to make advances as long as it complies with federal regulations. This means that FHLB may only make advances if it “determines that it may safely make such advance or renewal to the member . . . .”<sup>64</sup> The recital says nothing about the circumstances in which FHLB may limit or deny a member’s application for an advance. Therefore, LSB can only enforce the circumstances in which FHLB may make an advance under section 1266.4(a)(2), not the circumstances in which FHLB can limit or deny advances under section 1266.4(a)(1). LSB may be able to challenge improper advances FHLB actually made, assuming LSB had standing, but cannot challenge FHLB’s decision not to make an advance.

Without incorporation, LSB cannot enforce section 1266.4(a)(1) pursuant to its breach of contract claim. Further, there is no private right of action to enforce the regulation directly. Even if FHLB did not comply with section 1266.4(a)(1) when it declined to make advances to LSB, LSB does not have a remedy under the APSA or federal law.

Because FHLB has no contractual obligation to provide advances, LSB cannot recover for FHLB’s failure to provide advances under any state of facts that LSB could prove. The court grants FHLB’s motion to dismiss on counts II and V.

### **C. Fiduciary Duty**

LSB alleges that FHLB owed LSB fiduciary duties because LSB owns activity-based stock in FHLB and because Congress established FHLB to provide liquidity and support to local communities. LSB alleges that FHLB breached its fiduciary duties by failing to provide advances to LSB and by failing to treat LSB on an equal basis with all other FHLB members.

FHLB contends it did not owe fiduciary duties to LSB because their relationship was an

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<sup>64</sup> 12 C.F.R. § 1266.4(a)(2).

arms-length borrower-lender relationship. FHLB believes LSB's argument in LSB's partial motion to dismiss that the parties' relationship was arms-length undermines LSB's current stance that FHLB owed a duty to LSB. FHLB believes the activity-based stock was not equity stock giving rise to fiduciary duties. FHLB argues that the lack of any obligation for it to provide advances under the APSA and federal law means it could not have breached any duty for failing to provide LSB with advances.

LSB's argument in its partial motion to dismiss does not undermine its position. Relationships can be complex. Some parts of a relationship may be arms-length, while others may give rise to tort or fiduciary duties. For example, a bank may serve as the trustee of a trust and owe fiduciary duties to the beneficiaries. A beneficiary could open a checking account with the bank, for which the bank would not owe fiduciary duties, without affecting the bank's fiduciary duties related to the trust. In the partial motion to dismiss, LSB argued the relationship where it serviced FHLB's loan portfolio was arms-length. For this motion to dismiss, LSB argues FHLB owed LSB fiduciary duties related to providing regular advances as an important source of liquidity. LSB's arguments deal with distinct parts of the parties' relationship.

“A fiduciary relationship is one in which a person is under a duty to act for the benefit of another as to matters within the scope of the relationship.”<sup>65</sup> A fiduciary relationship

embrac[es] both technical fiduciary relations and those informal relations which exist wherever one man trusts or relies upon another. One founded on trust or confidence reposed by one person in the integrity and fidelity of another. A ‘fiduciary relation’ arises whenever confidence is reposed on one side, and domination and influence result on the other; the relation can be legal, social, domestic, or merely personal. Such relationship exists when there is a reposing of faith, confidence and trust, the placing of reliance by one upon the judgment and advice of the other.<sup>66</sup>

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<sup>65</sup> *Stotts v. Eveleth*, 688 N.W.2d 803, 811 (Iowa 2004).

<sup>66</sup> *Id.* (citing *Econ. Roofing & Insulating Co. v. Zumaris*, 538 N.W.2d 641, 647 (Iowa 1995)).

“Because the circumstances giving rise to a fiduciary duty are so diverse, whether such a duty exists depends on the facts and circumstances of each case.”<sup>67</sup>

FHLB’s discretion whether to give LSB advances under the APSA and 12 C.F.R. section 1266.4(a) does not preclude possible fiduciary duties related to providing advances. The particular circumstances of the parties’ relationship could give rise to fiduciary duties that require FHLB to exercise its discretion in good faith.

FHLB correctly points out that the activity-based stock LSB purchased to become a member institution is not ordinary equity stock. FHLB argues that no fiduciary duties attach to the activity-based stock, because the activity-based stock lacks the characteristics of ordinary equity stock that give rise to fiduciary duties to shareholders. LSB did not purchase the stock to hold an equity stake in FHLB or to obtain a return on its investment, rather LSB had to purchase the stock as a condition to receiving loans in FHLB’s lending program. LSB is not beholden to the whims of majority shareholders who can deprive LSB of the value of their equity. Instead, how many mortgages a member sells to FHLB and how many loans a member takes out affects the amount of activity-based stock a member holds. LSB could sell its stock back to FHLB by decreasing the amount of business LSB does with FHLB.

Despite these characteristics, the court cannot say that under no set of facts would FHLB owe fiduciary duties to LSB. The activity-based stock has unique characteristics and LSB may be able to show that LSB placed confidence and trust in FHLB by purchasing it. LSB cannot immediately sell all of its shares, but must wait until its ongoing business with FHLB terminates. LSB is entitled to dividends from FHLB depending on FHLB’s earnings.<sup>68</sup> The value of LSB’s activity based stock may change depending on FHLB’s actions. LSB relies on the availability of

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<sup>67</sup> *Id.*

<sup>68</sup> Capital Plan § 3.4.

FHLB's advances as a member institution. LSB identified FHLB's overnight advances as part of LSB's contingency funding plan that LSB must maintain as a regulated financial institution. These characteristics make LSB reliant on FHLB and may give rise to fiduciary duties.

Congressional intent also supports LSB's contention that FHLB owes fiduciary duties to LSB. FHLB is a unique entity created by Congress to provide assistance to community banks like LSB. Since the Great Depression, Congress has repeatedly opened and expanded the use of Federal Home Loan Bank programs to support community banking.<sup>69</sup> Professor Hurley, a director of the Federal Home Loan Bank of Boston, explained:

The liberalization of the types of allowable collateral used to procure advances and the allowable uses of advances, like the liberalization of FHLB membership, signals a push by Congress to prop up those areas of the economy worst hit by economic downturns: community and agricultural banks and the constituents they serve.<sup>70</sup>

Because Congress intended FHLB to provide advances to community banks like LSB to support local communities, FHLB may have fiduciary duties to LSB related to providing advances.

LSB pled sufficient facts to give FHLB notice of the grounds for LSB's fiduciary duty claim. The court denies FHLB's motion to dismiss for count VI.

## V. RULING

**IT IS THEREFORE ORDERED** that FHLB's motion to dismiss is:

**GRANTED** regarding counts II and V, and **DENIED** regarding counts I, IV, VI, VII, VIII, and IX.

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<sup>69</sup> Cornelius Hurley & Rebecca Hicks Gallup, *The Federal Home Loan Bank System: A Vehicle for Job Creation and Job Retention*, 30 Rev. Banking & Fin. L. 609, 622 (2011).

<sup>70</sup> *Id.*



State of Iowa Courts

**Case Number**  
EQCE085919  
**Type:**

**Case Title**  
LUANA SAVINGS BANK V FEDERAL HOME LOAN BANK  
OTHER ORDER

So Ordered

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Lawrence P. McLellan, District Court Judge,  
Fifth Judicial District of Iowa

Electronically signed on 2021-04-06 10:05:15