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# AN EPOCH IN THE HISTORY OF NATIONAL BANKING ASSOCIATIONS

By WILLIAM L. TRAVIS\*

Congress, in the exercise of its authority, has power to create a bank,<sup>1</sup> and the National Bank Act of 1864, creating a system of national banks as agencies of the Federal Government to provide a national currency, is constitutional.<sup>2</sup> Being creations of Congress, such associations enjoy only the statutory powers granted them and such incidental powers as may be necessary to carry out the intent and purpose for which the express powers are conferred. "The measure of their powers is the statutory grant and powers not conferred by Congress are denied. For the Act under which national banks are organized, constitutes a complete system for their government."<sup>3</sup> In the words of the Supreme Court, "Authority is thus given to transact such a banking business as is specified, and all incidental powers necessary to carry it on are granted. These powers are such as are required to meet all the legitimate demands of the authorized business, and to enable a bank to conduct its affairs, within the general scope of its charter, safely and prudently."<sup>4</sup>

The chief purpose of this article is to present, from a review of recent expressions of the courts, a number of definite

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\*Of the Hammond Bar.

<sup>1</sup> *McCulloch v. Maryland*, 4 Wheat. 316, 45 L. Ed. 579; *Farmers Nat. Bank v. Dearing*, 91 U. S. 29, 23 L. Ed. 196, *Pollard v. State*, 65 Ala. 628; *Flint v. Boston*, 99 Mass. 141, 96 Am. Dec. 713; *Stetson v. Bangor*, 56 Me. 274.

<sup>2</sup> *Davis v. Elmira Savings Bank*, 161 U. S. 275, 16 S. Ct. 502, 40 L. Ed. 700, and cases cited *supra* n. 1.

<sup>3</sup> *Texas & Pac. Ry. Co. v. Pottorff*, 291 U. S. 245, 54 S. Ct. 416, 78 L. Ed. 777 (1934); *First Nat. Bank v. Missouri*, 263 U. S. 640; *First Nat. Bank v. Converse*, 200 U. S. 425, 439, 26 S. Ct. 306, 50 L. Ed. 537; *First Nat. Bank v. Hawkins*, 174 U. S. 364, 19 S. Ct. 739, 43 L. Ed. 1007, *California Nat. Bank v. Kennedy*, 167 U. S. 362, 17 S. Ct. 831, 42 L. Ed. 198; *Logan County Nat. Bank v. Townsend*, 139 U. S. 67, 73, 11 S. Ct. 496, 35 L. Ed. 107, 110; *Charlotte First Nat. Bank v. National Exchange Bank*, 92 U. S. 122, 128, 23 L. Ed. 679, 681; *Baltimore & Ohio Ry. v. Smith*, 56 F. (2d) 799 (1932); *Williams v. Merchants Nat. Bank*, 42 F. (2d) 243.

<sup>4</sup> *Charlotte First Nat. Bank v. National Exchange Bank*, *supra* n. 3.

and indicated limitations imposed upon national banking associations and to record a few *ultra vires* practices that have been indulged in by some of them under an erroneous conception of their powers. Such a review will not only show that a banking practice commonly pursued may be illegal,<sup>5</sup> but will also exhibit a tendency on the part of the courts to confine such banks strictly to the exercise of their chartered powers, while Congress progressively broadens the field of their activities.<sup>6</sup>

## II

### GENERAL POWERS

In addition to the usual banking and corporate powers necessary for their organization, operation, and management, national banks, by the Act of June 3, 1864, in general terms, were given the power to have succession for twenty years, which was later increased to ninety-nine years<sup>7</sup> and still later to an unlimited time subject to termination only by Congress, forfeiture, dissolution or insolvency;<sup>8</sup> to make contracts; to sue and be sued, complain and defend in any court of law or equity, as fully as natural persons, and to exercise all such incidental powers as shall be necessary to carry on the business of banking, by discounting commercial paper, by receiving deposits, by buying and selling exchange, coin and bullion, by loaning money on personal security, by obtaining, issuing and circulating notes as provided by law.<sup>9</sup> The definition of these powers, in the main, is self-explanatory and requires no particular comment, except for the construction of the power *to make contracts*, and *the incidental powers as shall be necessary to carry on the business of banking*. The general phraseology employed in granting those two powers has given

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<sup>5</sup> Texas & Pac. Ry. Co. v. Pottorff, *supra* n. 3.

<sup>6</sup> Texas & Pac. Ry. Co. v. Pottorff, *supra* n. 3.

<sup>7</sup> R. S. Sec. 5136 and 12 U. S. C. A. Sec. 24, as amended by Act of July 1, 1922, c. 257, 42 Stat. 767

<sup>8</sup> R. S. Sec. 5136 and 12 U. S. C. A. Sec. 24, as amended by Act of Feb. 25, 1927, c. 191, Sec. 2, 44 Stat. 1226, June 16, 1933, c. 89, Sec. 16, 48 Stat. 184, Aug. 23, 1935, c. 614, Sec. 308, 49 Stat. 709, 12 U. S. C. A. Supp. 1935, Sec. 24.

<sup>9</sup> R. S. Sec. 5136, as amended, 12 U. S. C. A. Supp. 1935, Sec. 24.

birth to considerable litigation from which we may now derive a fairly accurate conception of the scope and limitations of those two grants of power, and, because many of the activities of a bank, directly or indirectly, touch upon and are concerned with the exercise of those two powers, much of this effort will be focused upon the meaning of those clauses of the Act, as interpreted by the courts.

Although given the power *to make contracts*, it is obvious that the grant is limited, not only by the other provisions of the same section from which that power is derived and by Section 82 of the same title, but also by the further limitation that the scope of the banking business must be confined to conducting the charter powers *safely* and *prudently*,<sup>10</sup> which as we shall hereafter note, restricts the activities in dealing in investment securities and in securing repayment of deposits.

### III

#### POWER TO DEAL IN INVESTMENT SECURITIES

National banks were specifically given power by the amendment to Section 24 of the Act<sup>11</sup> to deal in investment securities *without recourse*. The term, "without recourse", as used in the Act, has been held to mean without recourse in its broad and non-technical sense, precluding any form of arrangement or agreement in consequence of which a national bank is obligated to save a purchaser harmless from loss incurred as a result of his purchase, and hence a contract entered into contemporaneously with a sale, to repurchase bonds sold to a customer at par, violates the statute and is *ultra vires*, unenforceable, and the bank is not estopped to disaffirm the contract because the customer is chargeable with knowledge of the bank's limited power to contract.<sup>12</sup>

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<sup>10</sup> Charlotte First Nat. Bank v. National Exchange Bank, *supra* n. 3, Texas & Pac. Ry. Co. v. Pottorff, *supra* n. 3; Eastern Township Bank v. Vermont Nat. Bank, 22 Fed. 186.

<sup>11</sup> R. S. Sec. 5136 and 12 U. S. C. A. Sec. 24, as amended by Act of Feb. 25, 1927, *supra* n. 8.

<sup>12</sup> Avotin v. Atlas Exchange Nat. Bank, 295 U. S. 209, 55 S. Ct. 674, 79 L. Ed. 1393 (1935), *aff'g.* 275 Ill. App. 530; Kimen v. Atlas Exchange Nat.

Since June 16, 1934, the effective date of the Amendment of 1933 to Section 24, the business of dealing in securities and stocks has been limited "to purchasing and selling such securities and stocks without recourse, solely upon the order, and for the account of, customers; and in no case for its own account, and the association shall not underwrite any issue of securities or stock. Provided, that the association may purchase for its own account investment securities under such limitations and restrictions as the Comptroller of the Currency may by regulation provide."<sup>13</sup> Definition of the term, "investment securities", is left to the discretion of the Comptroller, but in a general way is declared to be, . . . "marketable obligations . . . in the form of bonds, notes and/or debentures." Certain obligations of the United States, the several states and their political subdivisions are exempted from the limitation. No authority is granted by the Act to acquire shares of stock in any corporation, but investment in stock in a company engaged in the safe-deposit business is permitted to the extent of fifteen per cent of its unimpaired and fully paid capital stock and surplus.

Prior to the enactment of the Amendment in 1927 conferring the qualified power to deal in such securities, national banks, while not expressly prohibited, were impliedly prohibited by a failure to grant the power, from dealing in stocks or bonds of other corporations except when such securities were acquired as collateral or in settlement of a debtor's obligations.<sup>14</sup> The power is now exercised under the super-

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Bank, 295 U. S. 215, 55 S. Ct. 677, 79 L. Ed. 1398, *Greene v. First Nat. Bank*, 172 Minn. 310, 215 N. W. 213. Cf. *Citizens Nat. Bank v. Pigford (Allen)*, — Miss. —, 167 So. 627 (1936), Docketed by U. S. Supreme Ct. Aug. 11, 1936, *Citizens Nat. Bank v. Golden*, — Miss. —, 166 So. 745 (1936), Docketed U. S. Supreme Ct. Aug. 1936, and *Citizens Nat. Bank v. Bullard*, — Miss. —, 168 So. 52, Docketed U. S. Supreme Ct. Aug. 1936; (holding national bank liable for damages for deceit and fraudulent representations as to bonds being represented as guaranteed by surety companies, notwithstanding R. S. Sec. 5136, parag. (7) as amended.)

<sup>13</sup> R. S. Sec. 5136, as amended by Act of Feb. 25, 1927, 12 U. S. C. A. Supp. 1935, Sec. 24(7).

<sup>14</sup> *McCreery v. Equitable Bank*, 203 U. S. 584; *First Nat. Bank v. Converse*, *supra* n. 3, *Shaw v. National German Bank*, 199 U. S. 603, 26 S. Ct.

vision and control of the Comptroller to a large extent under the Act of 1933.

## IV

## POWER TO SECURE REPAYMENT OF DEPOSITS

By the Act of 1864 and amendments thereto<sup>15</sup> national banks are designated as depositaries of public monies and financial agents of the United States, and authorized to give satisfactory security for such deposits. Prior to the Amendment of June 25, 1930,<sup>16</sup> great uncertainty existed over the question as to whether the power to receive public deposits and give security for their safe-keeping was restricted to deposits of the Federal Government and its instrumentalities, or whether the Act was broad enough to cover public deposits also of any state or its political subdivisions. If it were held that no such power existed under the above provision, then the inquiry arose as to whether the power might be exercised as a necessary incident to the power to receive deposits and to carry on the banking business.

Recently the Supreme Court of the United States definitely determined that prior to the Amendment of 1930 such banks had *no* power to give security, by pledging its assets, to secure *any public deposits of a state or its political subdivisions*, notwithstanding a contrary assumption prevailing among the officers charged with administration of the Act; and the Court expressed the further opinion that, since the Amendment of 1930, such association may pledge their assets and give security for such public funds *only* when located in a state in which state banks are similarly authorized.<sup>17</sup>

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750, 50 L. Ed. 328; *Scott v. DeWeese*, 181 U. S. 202, 21 S. Ct. 585, 45 L. Ed. 322; *Robinson v. Southern National Bank*, 180 U. S. 295, 21 S. Ct. 383, 389, 45 L. Ed. 536; *First Nat. Bank v. Hawkins*, *supra* n. 3; *California Nat. Bank v. Kennedy*, *supra* n. 3, *Charlotte First Nat. Bank v. National Exchange Bank*, *supra* n. 3, *Schofield v. Goodrich*, 98 Fed. 271; *First Nat. Bank of Vernon v. Federal Land Bank*, 93 Ind. App. 15, 177 N. E. 462 (1931).

<sup>15</sup> R. S. Sec. 5153, 12 U. S. C. A. Sec. 90.

<sup>16</sup> R. S. Sec. 5153, as amended June 25, 1930, c. 604, 46 Stat. 809; 12 U. S. C. A. Supp. 1935, Sec. 90.

<sup>17</sup> *City of Marion v. Sneed*, 291 U. S. 262, 54 S. Ct. 421, 78 L. Ed. 787 (1934).

In another case decided on the same day the Court held that such banks, both before and since the amendment, have been without power to give security for private deposits.<sup>18</sup> This holding refutes and repudiates the contention that the exercise of the power to pledge security for safe-keeping is a necessary incident to receiving deposits. On the contrary, the Court took the position that such a practice is inimical to safe banking, tends to destroy confidence in banks, and preclude the uniform treatment intended to be accorded by the *ratable distribution* provisions of the National Bank Act relating to administration of insolvent institutions.

The Amendment of 1930, hereinabove referred to, provides that: "Any association may, upon the deposit with it of *public money* of a *State or any political subdivision* thereof, give security for the safe-keeping and prompt payment of the money so deposited, *of the same kind* as is authorized by the *law of the State* in which such association is located in the case of other banking institutions in the state."<sup>19</sup> (Italics mine). It is apparent that the portions of the amendment italicized above are subject to wide and variable interpretations. An attempt will be made, therefore, to devote some consideration to the terminology used and to the interpretations placed upon the subject clauses by the courts in recent cases.

While the Supreme Court declared in the City of Marion decision<sup>20</sup> that the Amendment empowers national banks to secure deposits of a State or its political subdivision only in states where state banks are so authorized, it did *not* attempt to define what is meant by "public money", nor what funds constitute "monies of a State or political subdivision thereof", nor what is "security", nor what is deemed to be "the law of the State", nor what methods may be employed in the exercise of the power granted. However, many of those questions have been answered and a fairly well defined conception of the terms and effect of the Amendment has been outlined by the precedents now established by the courts.

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<sup>18</sup> Texas & Pac. Ry. Co. v. Pottorff, *supra* n. 3 (1933).

<sup>19</sup> *Supra* n. 16.

<sup>20</sup> *Supra*, n. 17.

The term "public money of a State or political subdivision thereof" has been held not to include a deposit of litigants' awards by a clerk of a state court;<sup>21</sup> nor bankruptcy funds, generally;<sup>21½</sup> nor a deposit of a state bank's receiver, whether appointed by a state court or by the state banking commissioner.<sup>22</sup> On the other hand, it has been held that where costs and fees are recognized as public funds under the state depository law, such funds, when deposited by the proper clerk of a court chargeable with their custody, constitute public funds of the county, as a political subdivision of the state, within the purview of the Act.<sup>23</sup> Deposits by the Comptroller of Currency, consisting of assets of insolvent national banks, are permitted to be secured under authority of another section, but this privilege does not extend to securing deposits of the United States Shipping Board Merchant Fleet Corporation, nor to deposits of the Alien Property Custodian.<sup>24</sup> A pledge made to a road district in Texas has been held not to come within the permitted classes.<sup>25</sup> However, a pledge made to a town in a state where the *public policy* of that state permits such pledges to be made by its state banks, is valid;<sup>26</sup> and a pledge made prior to 1930, but approved subsequent to the effective date of the amendment of that year, securing deposits of a city treasurer, has been held valid.<sup>27</sup> Furthermore, it has been held that where a good faith effort has been made, the mere failure to strictly

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<sup>21</sup> Utter v. Eckerson, 78 F (2d) 307 (1935).

<sup>21½</sup> Irving Trust Co. v. U. S., 83 F (2d) 20 (1936), Phelps v. Citizens Union National, 13 F Supp. 623 (1936).

<sup>22</sup> Griffin v. Royal, 70 F (2d) 103 (1934), Harrell v. Lawhead, 13 F. Supp. 298 (1936).

<sup>23</sup> Utter v. Eckerson, *supra* n. 21 (1935).

<sup>24</sup> O'Connor v. Rhodes, 79 F (2d) 146, *aff'd* — U. S. —, 80 L. Ed. 143 (1936), construing R. S. Sec. 5234, 12 U. S. C. A. Sec. 192.

<sup>25</sup> Pottorff v. El-Paso Hudspeth Road Dist., 62 F (2d) 498 (1935), *cert. den.* 289 U. S. 724, 53 S. Ct. 522, 77 L. Ed. 1474 (1933).

<sup>26</sup> Standard Inv. Co. v. Snow Hill, 78 F (2d) 33 (1935); Hellowell v. Hempstead, 10 F. Supp. 771 (1935).

<sup>27</sup> Ross v. Knott, 13 F Supp. 963 (1936), Haynes v. Woodward, 6 F Supp. 270 (1934).



comply with a state depository law will not vitiate a pledge, if otherwise permitted;<sup>28</sup> nor will the mere failure of the board of directors to adopt a resolution approving the pledge render it void.<sup>29</sup>

The meaning of "security . . . of the same kind as is authorized by the law of the state . . .", is indicated by a recent decision of the Supreme Court wherein it was held that the term is not restricted to include a pledge of specific assets only, but embraces also the giving of a bond with surety and creating a lien on all of the bank's assets as security for the prompt payment of the deposit.<sup>30</sup> The Court gave the word "security" a liberal interpretation, in order, as the Court stated, that national banks might be placed upon an equal footing with state banks and thereby give effect to the paramount purpose of the amendment to prevent unfair and destructive competition between the two banking systems.

The laws and decisions of the courts of any given state must control the question as to whether state banks have the power to give security of a kind sought to be hypothecated by a national bank doing business in such state, and the *law* of any such state is expressed by constant practices, by the interpretations of the officials charged with supervision over such banks, and by the statutory, constitutional, or judicial pronouncements of the state.<sup>31</sup> While it is recognized that national banks are Federal instrumentalities and controlled by the paramount law of the United States, nevertheless, they are subject to state laws unless the latter are in conflict with some Federal law, or unless the state law tends to impair or defeat the purpose intended by the National Bank Act.<sup>32</sup>

The Circuit Court of Appeals, Ninth Circuit, in a very current case dealing with the amendment of 1930, in succinct language said, "To summarize our views under this heading,

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<sup>28</sup> *Texas & Pac. Ry. v. Pottorff*, *supra* n. 3 (1933); *Capital Loan & Sav. Assn. v. Olympia Nat. Bank*, 80 F (2d) 561 (1936); *Fidelity & Deposit Co. v. Kokrda*, 66 F (2d) 641 (1933).

<sup>29</sup> *Kavanaugh v. Fash*, 74 F (2d) 435 (1935).

<sup>30</sup> *Lewis v. Fidelity & Deposit Co.*, 292 U. S. 559, 54 S. Ct. 848, 78 L. Ed. 1425, 92 A. L. R. 803 (1934).

<sup>32</sup> *Lewis v. Fidelity & Deposit Co.*, *supra* n. 30 (1934), citing cases.

therefore, we hold that the appellants are entitled to invoke the state statutes for the purpose of ascertaining whether *any* security for public deposits is permitted by state law, and, if so, what *kind*, but not for the purpose of questioning the size of the public deposit, or the amount of security given by the bank; for the provisions of state law as to amount of security or of public deposits are for the protection of the state and not of banks. . . .”

“Furthermore where the public policy of a state favors the protection of public deposits by means of security to be given by depositaries, contracts for that purpose will be sustained, regardless of technical deficiencies.”<sup>33</sup>

It now seems to be recognized that the giving of security for public deposits may be accomplished by a pledge of assets to a *surety* on the bank's depositary bond, in lieu of a pledge direct to the depositor, and this is so because, while the amendment limits the giving of security to the *same kind* as is authorized by the law of the state, it is not limited to giving it in the same *manner*.<sup>34</sup>

## V

### MISCELLANEOUS REGULATIONS · DIRECTORS' QUALIFICATIONS — LOAN LIMITS—INTEREST RATES — REAL ESTATE LOANS

New regulations have been imposed upon a national banking association requiring its directors, consisting of not less than five nor more than twenty-five, to be bona fide owners of stock in such association of a par value of not less than twenty-five hundred dollars; and, requiring each director to be a citizen of the United States, and not less than three-

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<sup>33</sup> Capital Sav. & Loan Assn. v. Olympia Nat. Bank, *supra* n. 28 (1936).

<sup>34</sup> Capital Sav. & Loan Assn. v. Olympia Nat. Bank, *supra* n. 28 (1936); Fidelity & Deposit Co. v. Kokrda, *supra* n. 28 (1933), Ross v. Knott, *supra* n. 27 (1936), Haynes v. U. S. F & G. Co., 6 F. Supp. 272 (1934). Cf. Lewis v. Fidelity & Deposit Co., *supra* n. 30 (1934), where the surety company, as assignee of State Treasurer, was permitted to enforce a lien created in favor of the depositor by a Georgia statute against the bank's assets.

fourths of them to be residents of the state in which the bank is situated, or within a radius of fifty miles thereof.<sup>35</sup>

The total obligations of any person, company, corporation, or firm to a national bank can not exceed ten per cent of the unimpaired, paid in capital and surplus.<sup>36</sup> By the latest amendment the term "obligations" has been specifically defined.<sup>37</sup>

The former section of the Act fixing interest rates<sup>38</sup> has been amended to provide an option to collect interest at rates not exceeding one per cent in excess of the discount rate on ninety day commercial paper at the Federal Reserve Bank of the district, or at the rate prescribed for state banks, or at seven per cent if there be no rate fixed by state law, whichever is greater, and branch banks are governed by the rate prevailing in the place where the branch is located.<sup>39</sup>

Loans on improved real estate, including improved farm and residential properties, secured by first liens are now authorized to be made by such banks,<sup>40</sup> and they may acquire obligations so secured, *when the entire amount thereof* is sold to the purchasing bank. Such loans may not exceed fifty per cent of the appraised value of the securing property, and may mature not later than five years, unless they be amortized loans for not more than sixty per cent of the appraised value, which may, in that event, mature over a ten year period with the installments amortizing at least forty per cent of the principal within the first ten years. Real estate loans are limited to an aggregate amount not exceeding the unimpaired paid in capital stock and surplus, or sixty per cent of its time and savings deposits, which ever is greater.

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<sup>35</sup> 12 U. S. C. A. Supp. 1935, Secs. 71a, 72.

<sup>36</sup> R. S. Sec. 5200, as amended, 12 U. S. C. A. Supp. 1935, Sec. 84. First mortgage bonds of a manufacturing company held by a national bank, where such bonds are not readily marketable nor widely distributed, have been held not to be "investment securities" in which such bank might acquire up to 25% of its capital and surplus, but "obligations" within the meaning of the above section limiting purchases to not more than 10%, notwithstanding Act of Feb. 25, 1927, 44 Stat. 1226, 12 U. S. C. A. Sec. 24(7), *Anderson v. Akers*, 7 F Supp. 924.

<sup>37</sup> *Supra* n. 36.

<sup>38</sup> R. S. Sec. 5197, 12 U. S. C. A. Sec. 85.

<sup>39</sup> 12 U. S. C. A. Supp. 1935, Sec. 85.

A provision of the same section, immediately hereinabove referred to, authorizes such banks to "make such loans in an aggregate sum including in such aggregate any such loans on which it is liable as indorser or guarantor or otherwise equal to 25 per centum of the amount of the capital stock of such association actually paid in and unimpaired and 25 per centum of its unimpaired surplus fund, or to one-half of its savings deposits, at the election of the association subject to the general limitation contained in section 84 of this title." It is not clear what is meant by the term "loans on which it is liable as indorser or guarantor, or otherwise". Heretofore, the policy of the Congress<sup>41</sup> has been to prevent national banks from becoming liable as indorser, guarantor, or surety for another's benefit, and such contracts or engagements by which they might become so liable have been held to be *ultra vires*, void, and unenforceable.<sup>42</sup> It is assumed, therefore, that the Act of 1935 does not remove the inhibitions against becoming liable as indorser, surety, or guarantor for another, but merely reaffirms the right to indorse or guarantee negotiable obligations upon transferring or discounting them in the ordinary course of business, which has been recognized as the exercise of a legitimate and necessary incidental power.<sup>43</sup>

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<sup>40</sup> 12 U. S. C. A. Supp. 1935, Sec. 371. See also the regulations issued by the Comptroller of Currency Sept. 4, 1935, 3 U. S. L. Wk. 26.

<sup>41</sup> See: 12 U. S. C. A. Supp. 1935, Sec. 24; 12 U. S. C. A. Sec. 92; 12 U. S. C. A. Supp. 1935, Sec. 92.

<sup>42</sup> *Farmers & Miners Bank v. Bluefield Nat. Bank*, 11 F. (2d) 83 (1926), *cert. den.* 46 S. Ct. 483, *Mowen v. Needles Nat. Bank*, 94 Fed. 925, *affg.* 87 Fed. 430, *cert. den.* 176 U. S. 682, 20 S. Ct. 1024, 44 L. Ed. 637 (1900), *Consolidated Nat. Bank v. Anglo & London Paris Bank*, 34 Ariz. 160, 269 Pac. 68, *cert. dismissed as improvidently granted* 280 U. S. 526, 50 S. Ct. 87, 74 L. Ed. 593 (1929), *Border Nat. Bank v. American National*, 282 Fed. 73, *app. dismissed* 260 U. S. 701, 43 S. Ct. 96, 67 L. Ed. 471, *Barron v. McKinnon*, 179 Fed. 759; *Peoples Nat. Bank v. Southern States Finance Co. (N. C.)*, 133 S. E. 415, *Tallapoosa First Nat. Bank v. Monroe*, 135 Ga. 614, 69 S. E. 1123, 32 L. R. A. (N. S.) 550; *McQueen v. First Nat. Bank*, 36 Ariz. 74, 283 Pac. 273 (1929), *Ellis v. Citizens National*, 25 N. M. 319, 183 Pac. 34, 6 A. L. R. 166, *Board of Comm. of Lake County v. Citizens Trust & Sav. Bank (Ind. App.)*, 123 N. E. 130; and cases cited to 12 U. S. C. A. Sec. 24, n. 101-104 incl.

<sup>43</sup> *Peoples Bank v. Manufacturer's Nat. Bank*, 101 U. S. 181, 25 L. Ed. 907, *Bowen v. Needles Nat. Bank*, *supra* n. 42; *Farmers and Miners Bank v. Blue-*

If a national bank could be said to be empowered, by the foregoing provision, to make itself liable in the capacity as indorser, surety, or guarantor upon real estate bonds evidencing loans upon real property, the Act of 1935 would, indeed, violate the long established policy of Congress denying such power. If any such effect were intended, it is difficult to understand why the restrictions upon dealing in investment securities are retained.<sup>44</sup> It is believed, therefore, that the Act merely contemplated that such obligations, incurred within the usual course of business as heretofore permitted, should be included in a computation of the aggregate of this type of loans permitted by the loan limits.

Loans for the construction of buildings on such properties, maturing within six months, are not considered as real estate loans, but are classed as commercial loans. Immediately following the clause relating to construction loans is a *proviso* to the effect that such banks may not *invest in*, or be liable on any such loans in an aggregate amount in excess of fifty per cent of its unimpaired, paid in capital. This proviso appears to apply only to the subject immediately preceding it, namely, loans on construction of buildings, maturing within six months. At least, this interpretation would follow if the general rule of statutory construction relating to provisos is followed.<sup>45</sup>

## VI

### TRUST POWERS AND DUTIES

National banks derive their power from the Federal Reserve Act to perform fiduciary functions.<sup>46</sup> Under a delegation of authority the Federal Reserve Board is given power to permit national banks to act as trustees, executors, administrators, registrars of stocks and bonds, guardians, assignees, receivers, committees for lunatics, or in any other fiduciary capacity in which state banks are permitted to act under the law of a state in which such associations are located.

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field Nat. Bank, *supra* n. 42; Peoples Nat. Bank v. Southern States Finance Co., *supra* n. 42; Thomas v. City Nat. Bank, 40 Neb. 501, 58 N. W. 943, 24 L. R. A. 263.

<sup>44</sup> 12 U. S. C. A. Supp. 1935, Sec. 24.

<sup>45</sup> 59 C. J. 1090, Sec. 640.

<sup>46</sup> 12 U. S. C. A. Sec. 248(k).

The Act requires the banks exercising fiduciary duties to segregate the assets of the trust estate from the general assets of the bank and to keep a separate trust department reflecting its trust and other fiduciary transactions. Funds so held are not to be used by the bank unless it first sets aside securing assets, approved by the Board, to secure their repayment. In the event of a failure of the bank, the beneficiaries of such deposits or funds so held have a lien on the securing assets in addition to their general claim, so that, while no preference is given, it is generally recognized that as to such secured funds the claimants may receive dividends on the full amount of their claims until those dividends, added to the amount realized from the proceeds of the sale of the securing assets, are sufficient to satisfy those claims in full.<sup>47</sup> This is known as the "*English Chancery Rule*", which prevails in the Federal courts; but elsewhere either the "*Bankruptcy Rule*", allowing a claim for the balance only after deductions for payments made out of proceeds of the collateral, or the "*Maryland Rule*", providing for the computation of dividends on the balance due at any dividend period after crediting previous dividends, is invoked.<sup>48</sup> The Banking Act of 1935, insofar as fiduciary transactions are concerned, has not changed the substance of the Act except to provide a method whereby banks could surrender their trust duties.<sup>49</sup>

The grant of power to act as fiduciaries imposes a further restriction in that *no deposits subject to check, or the deposit of checks, drafts, bills of exchange or other items for collection*, are permitted to be received in the trust department, but this restriction has been so construed that a deposit in the trust department, under a contract specifying that same might be transferred to any person on order of the depositor, is not deprived of the securing lien as a trust deposit, where it

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<sup>47</sup> Aldrich v. Chemical Nat. Bank, 176 U. S. 618, 20 S. Ct. 498, 44 L. Ed. 611, Merrell v. National Bank, 173 U. S. 131, 19 S. Ct. 360, 43 L. Ed. 640; Capital Sav. & Loan Assn. v. Olympia Nat. Bank, *supra* n. 28 (1936), Gamble v. Wimberly, 44 F (2d) 329; Washington v. Dexter Nat. Bank, 263 Fed. 304. *Contra*: American Surety Co. v. National Bank, 17 F (2d) 942.

<sup>48</sup> 3 Michie, Banks & Banking, 218, Sec. 158.

<sup>49</sup> 12 U. S. C. A. Supp. 1935, Sec. 248(k).

was designated on the trust ledger as "uninvested trust funds" and was, in fact, awaiting investment.<sup>50</sup> The bank itself, as distinguished from its customers, in the ordinary course of its fiduciary functions may deposit such trust funds in the trust department.<sup>51</sup>

Although the delegation of power to the Federal Reserve Board to permit associations to act as fiduciaries has been attacked as an unconstitutional delegation of power by Congress,<sup>52</sup> it is now well settled that the delegation of authority to the Board and the exercise of the power by the banks is constitutional,<sup>53</sup> and takes precedence over any laws of the states attempting to deny the exercise of such fiduciary duties.<sup>54</sup>

Assuming that a national bank, acting as a fiduciary, deposited trust funds in its commercial department instead of in its trust department—could it be said that the *cestui* would thereby be deprived of the benefit of the lien of the securing assets posted to secure the trust department liabilities? Logically, and in good conscience, it would seem that the bank's act could not defeat the beneficiary's right to the protection afforded by the posted securities, because the provisions of the Act requiring segregation appear to be mandatory, and the courts would probably say that the omission on the part of the bank to do what is required to do could not alter the relationship nor defeat the claimant's right to a secured claim. Unfortunately this rule has not yet been clearly enunciated, but it is supported to some extent, at least, by two district court decisions.<sup>55</sup>

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<sup>50</sup> *Richman v. First Methodist Church*, 76 F (2d) 344, *cert. den.* *Long v. First Methodist Church*, 56 S. Ct. 107, 80 L. Ed. 109 (1935).

<sup>51</sup> *Carcaba v. McNair*, 68 F (2d) 793 (1935).

<sup>52</sup> *People v. Brady*, 271 Ill. 100, 110 N. E. 864.

<sup>53</sup> *First National Bank v. Fellows*, 244 U. S. 416, 37 S. Ct. 734, 61 L. Ed. 1233, L. R. A. 1918C 283, Ann. Cas. 1918D, 1169 (1917), *rev.* *Fellows v. First Nat. Bank*, 192 Mich. 640, 159 N. W. 335.

<sup>54</sup> *U. S. v. Duncan*, 265 U. S. 19, 44 S. Ct. 427, 68 L. Ed. 881 (1924), *rev. State ex rel. Burnes v. Duncan*, 302 Mo. 130, 257 S. W. 784.

<sup>55</sup> *Taylor v. Picher*, 13 F Supp. 857 (1936), *Marvin v. First National*, 10 F Supp. 275 (1935).

## VII

EFFECT OF CONSOLIDATION ON FIDUCIARY RELATIONSHIPS  
OF CONSOLIDATED AND CONSTITUENT BANKS

The provisions of the National Bank Act as originally enacted<sup>56</sup> invited considerable apprehension concerning the effect of the consolidation of two national banks, or the conversion of a state bank into a national bank, or the consolidation of a state bank with another bank under the charter of a national banking association.<sup>57</sup> Because of the failure of Congress to provide the states with visitorial or supervisory control over national banks exercising fiduciary functions, no little amount of opposition was encountered by such associations from the several states which inclined to the view that the Federal agencies were invading a field believed to be peculiarly within the exclusive domain of the states.<sup>58</sup>

In a rather recent case<sup>59</sup> before the United States Supreme Court, it was contended in the briefs and arguments that the Federal Government, in the exercise of its admitted power to create fiscal agencies, has power, if necessity demands, to preserve those instrumentalities from ruinous competition by requiring all banks to become national banks,<sup>60</sup> subject to Federal control, and *a fortiori* the enlargement of their powers to provide for succession, upon consolidation or transformation, to the fiduciary functions exercised by constituent state banks would come within the broad power to establish and preserve them as useful and successful agencies by protecting them from unfavorable or discriminatory competition.<sup>61</sup> The Court failed to indicate whether the theory

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<sup>56</sup> Acts Nov. 7, 1918, c. 809, Secs. 1, 2, and Dec. 23, 1913, c. 6, Sec. 8; 12 U. S. C. A. Secs. 33, 34, 35, 40 Stat. Secs. 1043, 1044, and 38 Stat. Sec. 258.

<sup>57</sup> Wilson, *Injunctions and Attachments Against National Banks* (July, 1934), 20 Am. Bar. Assn. Jour. 399, 401.

<sup>58</sup> Wilson, *Injunctions and Attachments Against National Banks*, *supra* n. 57. <sup>59</sup> *Ex Parte* Worcester County Nat. Bank, 279 U. S. 347 (1929).

<sup>60</sup> *Veazie Bank v. Fenno*, 8 Wall. 533.

<sup>61</sup> *Casey v. Galli*, 94 U. S. 673, *Iowa Light Co. v. First Nat. Bank*, 250 Mass. 353, *Mercantile Trust Co. v. San Joaquin Agricultural Corp.*, 265 Pac. 583, *McElwain v. Primavera*, 167 N. Y. S. 815; *Chicago Title Co. v. Zinser*, 264 Ill. 31, *In re Berghoff's Will*, 206 N. Y. 309; *In re Turner's Estate*, 277 Pa. St. 110; *Pet. of Bank*, 249 Mass. 240. (All cited in briefs filed in *Ex Parte* Worcester County Nat. Bank, *supra* n. 59.)



advanced met with its approval, but it did declare, quite definitely, with respect to probate matters, that the purpose of the Act of 1927<sup>62</sup> was not to excuse compliance with the regulatory statutes of the several states, but to require, instead, that the consolidated bank account as a fiduciary *de son tort* and to apply to the state court for appointment as successor to the constituent bank. Under the court's decision the obvious effect of a consolidation is to transfer the property held by a constituent bank under supervision of a probate court, to the consolidated bank to be accounted for by the latter, *de son tort*, unless the state law recognizes the consolidated bank as a qualified successor without formal application or appointment.

It has been said that, as a corollary to the power to create, Congress has power "to attach to national banks that which in its judgment is relevant to make the business of the bank successful."<sup>63</sup> It has also been held that Congress has the power to invest such associations with the right to qualify and compete on the same basis with state banks in the exercise of fiduciary functions, notwithstanding the inhibitions of a state statute calculated to discriminate against them.<sup>64</sup> It seems to be established also that while Congress is admitted to have the power to compel the several states to accept national banks as fiduciaries on an equal basis with state banks, it is an unwarranted and unconstitutional interference with the autonomy of a state to attempt to coerce the latter, arbitrarily, to accept a consolidated bank in the place and stead of its constituent bank as an executor under a will or in any other peculiarly personal fiduciary capacity, because the difference in entities and the personal element are factors which prohibit an involuntary substitution or succession.<sup>65</sup>

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<sup>62</sup> Act of Feb. 25, 1927, c. 91, Sec. 3, 44 Stat. 1224, 1225.

<sup>63</sup> First Nat. Bank v. Fellows, *supra* n. 53.

<sup>64</sup> Missouri v. Duncan, 265 U. S. 18, 24, 44 S. Ct. 427, 68 L. Ed. 881 (1924).

<sup>65</sup> *Ex Parte* Worchester County Nat. Bank, *supra* n. 59; Stevens v. First Nat. Bank, 173 Ga. 332, 160 S. E. 243 (1931), *cert. den.* 284 U. S. 684, 52 S. Ct. 201, 76 L. Ed. 578 (1932), Hofheimer v. Seaboard Citizens Nat. Bank, 154 Va. 392, 153 S. E. 656, *aff'd*: 154 Va. 896, 156 S. E. 581 (1931), *cert. den.* 283

The amendments<sup>66</sup> to the Act restate the purpose of Congress in much clearer terms, and provide that the corporate entity of constituent banks should be deemed to be merged into and continued in the consolidated association.<sup>67</sup> This provision removes the possible argument that Congress did not intend to invest the consolidated bank with the power sought to be exercised,<sup>68</sup> but it may still be contended with the support of eminent authority<sup>69</sup> that a constituent bank has no such property right, insofar as trustees and conservators appointed by probate courts are concerned, as to pass to its successor national bank by consolidation. This rule was apparently regarded as an exception to the general rule and was not invoked by the same Court, however, in a case<sup>70</sup> where a constituent bank was designated as trustee under a mortgage indenture securing payment of a bond issue. The Court pointed out that in such a case the rights of the parties are chiefly contractual in nature, which was apparently deemed to be such as would pass as an asset to the consolidated bank. Since there is now no question as to the continuance of the corporate identity of the constituent bank in the consolidated bank, it is quite likely that in most cases the courts, hereafter, will hold, as a general rule (with a few exceptions in cases of a peculiar type above noted) that the consolidated bank as an incident to the consolidation succeeds to the fiduciary rights and duties of the absorbed bank.<sup>71</sup>

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U. S. 855, 51 S. Ct. 648, 75 L. Ed. 1462 (1931). *Contra: In re Barreiros Estate*, 125 Cal. App. 153, 13 P. (2d) 1017, 1024 (1932), *Adams v. Atlantic Nat. Bank*, 115 Fla. 399, 155 So. 648 (1934), *Alt v. Liberty Nat. Bank*, 260 Ky. 87, 83 S. W. (2d) 866 (1935).

<sup>66</sup> 12 U. S. C. A. Supp. 1935, Secs. 33, 34a.

<sup>67</sup> 12 U. S. C. A. Supp. 1935, Sec. 34a.

<sup>68</sup> *Petition of Commonwealth-Atlantic Nat. Bank*, 249 Mass. 440, 144 N. E. 443, *cert. den.* 266 U. S. 617, 45 S. Ct. 98, 69 L. Ed. 470.

<sup>69</sup> *Petition of Commonwealth-Atlantic Nat. Bank*, 261 Mass. 217, 158 N. E. 780 (1927), holding that the designation of a bank as a fiduciary by a probate court is not a property right in which it has a vested right.

<sup>70</sup> *Iowa Light, Heat & Power Co. v. First Nat. Bank*, 250 Mass. 353, 354, 145 N. E. 433 (1924). *Accord. First Nat. Bank v. Chapman*, 160 Tenn. 72, 22 S. W. (2d) 245 (1929), *Bayer v. Barrett*, 71 Cal. App. 620, 15 P. (2d) 801 (1932).

<sup>71</sup> *Wilson, Injunctions and Attachments Against National Banks*, 20 Am.

## VIII

## INSOLVENCY AND RECEIVERS

## A

*Federal Deposit Insurance Corporation—Its Functions and Duties—The Banking Act of 1935.*<sup>72</sup>

Notwithstanding any other provisions of law, the Comptroller of Currency is required to appoint the Federal Deposit Insurance Corporation as receiver of a closed bank if it be an insured national bank.<sup>73</sup> Likewise, the Corporation is empowered and directed to accept appointments as receiver of closed state banks where authorized by state law.<sup>74</sup> On failure of insured national banks, provision is made for payment of the insured deposits immediately by the Federal Deposit Insurance Corporation which, in turn, is subrogated to the claim of the depositor so paid. In other insured banks the Federal Deposit Insurance Corporation is forbidden to make payments of insured deposits until the rights of the depositors receiving the benefits of the insurance are transferred to the Federal Deposit Insurance Corporation in a satisfactory manner, either by assignment, operation of law of the state, order of court or otherwise.<sup>75</sup>

Supervision over such closed national banks is still retained by the Comptroller and he is given wide discretion in waiving compliance by the Federal Deposit Insurance Corporation to regulatory provisions applying, in general, to receivers.<sup>76</sup>

The Act of 1935 will make the Federal Deposit Insurance Corporation receiver of practically every national bank hereafter closed, and, with several of the states already permitting or directing that the Corporation be made receiver of closed

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Bar Assn. Jour. 402 n. 62 (July, 1934), *First Nat. Bank v. Fellows*, *supra* n. 53; *Missouri v. Duncan*, *supra* n. 64.

<sup>72</sup> Breckenridge, *The Banking Act of 1935*, 22 Am. Bar Assn. Jour. 93 (Feb. 1936).

<sup>73</sup> 12 U. S. C. A. Supp. 1935, Sec. 264L(3).

<sup>74</sup> 12 U. S. C. A. Supp. 1935, Sec. 264L(5).

<sup>75</sup> 12 U. S. C. A. Supp. 1935, Sec. 264L(7).

<sup>76</sup> 12 U. S. C. A. Supp. 1935, Sec. 264M(1).

state banks, it is quite likely that ultimately nearly all closed banks in the country will be administered by the Corporation under supervision of the Comptroller of Currency.<sup>77</sup>

The general provisions of the National Bank Act relating to administration of insolvent associations, except as modified by the Act of 1933, are retained and made applicable where the affairs of the association are wound up by the Federal Deposit Insurance Corporation.<sup>78</sup> Little change has been effected in the substantive law governing insolvent national banks. The status of the receiver as a Federal instrumentality or Federal officer<sup>79</sup> as distinguished from that as an officer of a court<sup>80</sup> has not been changed, so that the Federal Deposit Insurance Corporation, in its capacity as receiver, will retain its character as an executive administrative agency of the Federal Government.

## B

### *Shareholders' Stock Assessment Liability*

The Act of June 16, 1933, as amended by the Act of August 23, 1935,<sup>81</sup> exempts stockholders from liability on shares of stock issued subsequent to June 16, 1933, and provides further that stockholders' liability on shares of stock in a bank transacting business on July 1, 1937, shall then cease if notice of prospective termination of such liability is published as provided by the law. No relief is afforded stockholders who, prior to June 16, 1933, became owners of shares in a bank which shall have been closed prior to July 1, 1937.

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<sup>77</sup> Breckenridge, *The Banking Act of 1935*, 22 Am. Bar Assn. Jour. 93, 95 (Feb., 1936).

<sup>78</sup> 12 U. S. C. A. Supp. 1935, Sec. 264L(4).

<sup>79</sup> *Ex Parte* Chetwood, 165 U. S. 443, 17 S. Ct. 385, 41 L. Ed. 782; *Auten v. U. S. Nat. Bank*, 178 U. S. 125, 19 S. Ct. 628, 43 L. Ed. 920; *Port Newark Nat. Bank v. Waldron*, 46 F. (2d) 296; *Liberty Nat. Bank v. McIntosh*, 16 F. (2d) 906, *pet. cert. dismissed*, 273 U. S. 769, 783, 43 S. Ct. 571, 71 L. Ed. 890; *Steele v. Randall*, 19 F. (2d) 40.

<sup>80</sup> *Lehman v. Spurway*, 58 F. (2d) 227 (1932), *cert. den.* 287 U. S. 621, 53 S. Ct. 20, 77 L. Ed. 539; *Hulse v. Argetsinger*, 18 F. (2d) 944 (1927); *Wittnebel v. Loughman*, 9 F. Supp. 465 (1935), *aff'd*, 80 F. (2d) 222 (1935), *Wilson v. Awalt*, 2 F. Supp. 465 (1933).

<sup>81</sup> 12 U. S. C. A. Supp. 1935, Sec. 64(a), 49 Stat. 708.

This change in the law obviates, for practical purposes, the necessity of reviewing the many interesting cases involving stock assessment suits.

## C

*Effect of Insolvency on Status of Association—Applicability of State Laws—Bank Collection Code—Liens—Preference Claims*

It is definitely settled that the insolvency of a national bank and the appointment of a receiver to wind up its affairs does not work a dissolution of the corporation, nor affect suits pending against it, nor prevent it suing or being sued.<sup>82</sup>

Since the National Bank Act created a complete system for the winding up of such associations, the Federal law from the moment of suspension becomes the law governing the administration of closed national banks to the exclusion of the law of any state.<sup>83</sup> No state, by way of complement to the Act, may prescribe additional or auxiliary provisions affecting the administration of such banks.<sup>84</sup> Hence, a state law attempting to create a lien<sup>85</sup> or preference under the Uniform Bank Collection Code<sup>86</sup> has no application to an insolvent national bank. Likewise, it is beyond the poyer of a state probate court to try to circumvent the Federal law by declaring a preference with respect to a ward's funds in disregard of the requirement that the necessary elements of

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<sup>82</sup> *City of Marion v. Sneed*, *supra* n. 17 (1935), *Earle v. Pennsylvania*, 178 U. S. 449, 20 S. Ct. 915, 44 L. Ed. 1146, *Chemical Nat. Bank v. Hartford Deposit Co.*, 161 U. S. 1, 16 S. Ct. 439, 40 L. Ed. 595, *Rosenblatt v. Johnston*, 104 U. S. 462, 463, 20 L. Ed. 832; *Bethel Bank v. Pahquioque*, 14 Wall. 383, 20 L. Ed. 840; *Bailen v. Deitrick*, 84 F (2d) 375 (1936), *Wittnebel v. Loughman*, *supra* n. 80; *Bereth v. Sparks*, 51 F (2d) 441, and cases cited in 12 U. S. C. A. Sec. 192 n. 21.

<sup>83</sup> *First Nat. Bank v. Missouri*, 263 U. S. 640; *Easton v. Iowa*, 188 U. S. 220; *Davis v. Elmira*, 161 U. S. 265, 16 S. Ct. 502, 40 L. Ed. 700; *Cook County Nat. Bank v. U. S.*, 107 U. S. 445, 2 S. Ct. 561, 27 L. Ed. 537, *Farmers Bank v. Dearing*, 91 U. S. 29; *First Nat. Bank v. Selden*, 120 Fed. 212.

<sup>84</sup> *Prigg v. Pennsylvania*, 41 U. S. 536, *Calcasieu Nat. Bank v. Calcasieu Bank*, 83 F (2d) 742 (1936).

<sup>85</sup> *Spradlin v. Royal Man'fg. Co.*, 73 F (2d) 776.

<sup>86</sup> *Old Lehigh v. Meeker*, 294 U. S. 227, 55 S. Ct. 392, 79 L. Ed. 876 (1935), *Jennings v. U. S. F & G. Co.*, 294 U. S. 216, 55 S. Ct. 394, 79 L. Ed. 869, 99 A. L. R. 1248 (1935).

augmentation and identification of the trust *res* be established.<sup>87</sup>

Liens arising by state law prior to suspension, such as an attorney's retaining lien, are not invalidated by the appointment of a receiver because he is chargeable with the assets as he finds them and takes them subject to valid liens,<sup>88</sup> but such liens can not be created subsequent to suspension, before a receiver is appointed,<sup>89</sup> nor at any time after suspension.<sup>90</sup>

The *ratable distribution* provision<sup>91</sup> prevents allowance of preferences on any claim except for monies to reimburse the United States for advances to redeem the circulating notes of the bank,<sup>92</sup> and for assets which are traced and identified as belonging to another. Deposits by a trustee in bankruptcy in a closed bank are not subject to summary order of the Bankruptcy Court, since they are only general claims.<sup>93</sup> Likewise, deposits by receivers of state banks,<sup>94</sup> clerks of state courts,<sup>95</sup> receivers in equity,<sup>96</sup> deposits by order of court,<sup>97</sup> and deposits of funds held in escrow<sup>98</sup> have all been held to be no more than general claims.

## D

### *Claims for Rent—Provability of Claim for Damages for Anticipatory Breach*

Although the Supreme Court has recognized the right to prove a claim for an existing demand at the moment of in-

<sup>87</sup> *In re* West Side-Atlas Nat. Bank (O'Connell v. Mitchell), 78 F (2d) 395.

<sup>88</sup> *Earle v. Pennsylvania*, 178 U. S. 449, 20 S. Ct. 915, 44 L. Ed. 1146, *Scott v. Armstrong*, 146 U. S. 499, 13 S. Ct. 148, 36 L. Ed. 1059; *Webster v. Sweat*, 65 F (2d) 109 (1933).

<sup>89</sup> *Steele v. Randall*, 19 F. (2d) 40.

<sup>90</sup> *Cooper v. McNair*, 49 F (2d) 778 (attorney fees).

<sup>91</sup> R. S. Sec. 5236; 12 U. S. C. A. Sec. 194.

<sup>92</sup> *Davis v. Elmira*, *supra* n. 2; *Cook County Nat. Bank v. U. S.*, *supra* n. 83, *First Nat. Bank v. Selden*, 120 Fed. 212.

<sup>93</sup> *First Nat. Bank v. Selden*, *supra* n. 83; *First Nat. Bank v. Selden*, 120 Fed. 212. <sup>93</sup> *First Nat. Bank v. Selden*, *supra* n. 83; *First Nat. Bank v. Selden*, 120 Fed. 212. <sup>93</sup> *First Nat. Bank v. Selden*, *supra* n. 83; *First Nat. Bank v. Selden*, 120 Fed. 212. <sup>93</sup> *First Nat. Bank v. Selden*, *supra* n. 83; *First Nat. Bank v. Selden*, 120 Fed. 212.

<sup>94</sup> *Griffin v. Royal*, 70 F (2d) 103 (1934), *Isaacs v. Stock*, 66 F (2d) 928.

<sup>95</sup> *Eckerson v. Utter*, 78 F. (2d) 307 (1935).

<sup>96</sup> *Bridge v. First Nat. Bank*, 5 F Supp. 442 (1933).

<sup>97</sup> *Keyes v. Paducah*, 61 F (2d) 611, 86 A. L. R. 203 (1932).

<sup>98</sup> *Atlantic Gypsum Co. v. Federal Nat. Bank*, 76 F (2d) 59 (1935).

solvency, based upon a breach of a covenant to pay rent,<sup>99</sup> and has recognized the rule that the intervention of bankruptcy constitutes a disablement constituting an anticipatory breach of a contract relating to personalty, giving rise to a provable claim,<sup>100</sup> yet, it seems settled, now, that there is such a difference between contracts relating to personalty and contracts involving lands that default prior to suspension is a necessary prerequisite to establishing a claim against an insolvent national bank for breach of a lease contract.<sup>101</sup>

Where there is no default prior to suspension the receiver may repudiate the lease without incurring liability to his trust, especially where the lease does not provide for payment of a sum certain in case of its termination before the date fixed therein.<sup>102</sup> A claim is provable for ascertainable damages existing at the moment of insolvency, but not for contingent or speculative damages for anticipatory breach.<sup>103</sup>

## E

### *Preferred Claims on Funds Held by Bank as Constructive Trustee, Trustee Ex Maleficio, or Agent*

Preferred claims, as is indicated above, are quite rare, but many cases have come before the courts in the last few years wherein attempts have been made to establish a constructive trust or a trust *ex maleficio*, and to impress a trust upon the assets of the insolvent bank coming into the hands of the receiver, with the result that the law is now well settled to the extent that before such so-called preferences can be established, it is necessary to show: (1) a trust or agency relationship, (2) an augmentation of assets coming into the receiver's hands, and, (3) identification of the funds or *res* in the re-

<sup>99</sup> Chemical Nat. Bank v. Hartford Deposit Co., *supra* n. 82.

<sup>100</sup> Central Trust Co. v. Chicago Auditorium Assn., 240 U. S. 582.

<sup>101</sup> Wells v. Twenty First St. Ry. Co., 12 F (2d) 237, Fidelity Safe Deposit Co. v. Armstrong, 35 Fed. 567, Kennedy v. Boston Continental, 11 F Supp. 611 (1935), judgment modified and vacated. 84 F (2d) 592 (1936). Docketed U. S. Supreme Court.

<sup>102</sup> First Nat. Bank of Chicago v. First Nat. Bank of Wheaton, 78 F. (2d) 503 (1935), *cert. den.* 296 U. S. 561, 80 L. Ed. 283 (Dec. 17, 1935).

<sup>103</sup> Kennedy v. Boston Continental, *supra* n. 101, modified and vacated. Kennedy v. Boston-Continental, 84 F (2d) 592 (1936), Boston-Continental v. Wendell Phillips, 84 F (2d) 599 (1936).

ceiver's hands.<sup>104</sup> A shifting of credits is not sufficient to establish the augmentation required to be proven,<sup>105</sup> but the Supreme Court, by way of *dictum*, has intimated that it would adhere to the doctrine of "fungible goods" with respect to confused and commingled cash of the wrongdoer to the extent that it will not permit a trust *ex maleficio* to fail because such cash is confounded in a common fund.<sup>106</sup> However, the provisions of the Uniform Bank Collection Code can have no application to insolvent national banks and do not, therefore, excuse the necessity of proving actual augmentation and tracing the identifiable *res*.<sup>107</sup>

## F

### *Transfers in Contemplation of Insolvency—Acts of Insolvency—Knowledge of Transferee*

The National Bank Act forbids transfers after commission of an act of insolvency, in contemplation of insolvency, or with a view to preferring one creditor over another, or transfers to prevent the application of the bank's assets as required by law.<sup>108</sup> This injunction renders void the creation of a lien, whether by state statute or otherwise, which would

<sup>104</sup> Old Lehigh v. Meeker, *supra* n. 86 (1935); Jennings v. U. S. F & G. Co., *supra* n. 86 (1935); Blakey v. Brinson, 286 U. S. 254, 52 S. Ct. 516, 76 L. Ed. 1089, 82 A. L. R. 1288 (1932), Adams v. Champion, 294 U.S. 231, 55 S. Ct. 399, 78 L. Ed. 880 (1935), Kershaw v. Jenkins, 71 F (2d) 647 (1934), Poole v. Elliott, 76 F (2d) 772 (1935), O'Neal v. White, 79 F (2d) 835 (1935), Fulton v. Evans, 79 F (2d) 718 (1935), Stonebraker v. First Nat. Bank, 76 F (2d) 389 (1935), Brownell v. Turman, 75 F (2d) 1913 (1935), Thompson v. School Dist., 67 F. (2d) 284; Swan v. Children's Home Soc., 67 F (2d) 84, *cert. den.* 290 U. S. 704, 54 S. Ct. 372, 78 L. Ed. 605 (1934); Marshburn v. Williams, 15 F (2d) 589; Converse v. Continental, 12 F Supp. 887.

<sup>105</sup> Jennings v. U. S. F & G. Co., *supra* n. 86 (1935), O'Neal v. White, *supra* n. 104 (1935), Lifsey v. Goodyear, 67 F (2d) (1933).

<sup>106</sup> Adams v. Champion, *supra* n. 104 (1935); Jennings v. U. S. F & G. Co., *supra* n. 86 (1935), Blakey v. Brinson, *supra* n. 104 (1932), Schumacher v. Harriett, 52 F. (2d) 821 (1934).

<sup>107</sup> Jennings v. U. S. F. & G. Co., *supra* n. 86 (1935), Old Lehigh v. Meeker, *supra* n. 86 (1935), Calcasieu Nat. Bank v. Calcasieu Bank, 83 F. (2d) 742 (1936).

<sup>108</sup> R. S. Sec. 5242; 12 U. S. C. A., Sec. 91.



in effect prefer one creditor over another, if in violation of the spirit of the Act.<sup>109</sup>

By way of illustration, an "act of insolvency" occurs when a bank fails to meet its obligations in the ordinary course of business,<sup>110</sup> when the board of directors adopts a resolution to suspend operations,<sup>111</sup> when the officers turn over the bank to the Comptroller,<sup>112</sup> or when the bank delivers over its assets to a depositor to prevent a disastrous withdrawal of funds.<sup>113</sup>

The purpose of the Act is to assure a ratable distribution of assets,<sup>114</sup> and a transfer is "in contemplation of insolvency" when the officers, knowing, or chargeable with knowing, its failing condition, permits withdrawals calculated to, or having the effect of, defeating a ratable distribution.<sup>115</sup> It is immaterial whether the transferee has any knowledge of the bank's condition, or innocent of the unlawful effect of the transfer,<sup>116</sup>

<sup>109</sup> *Davis v. Elmira*, *supra* n. 2; *Scott v. Armstrong*, 146 U. S. 499; *National Security Bank v. Butler*, 129 U. S. 223, 9 S. Ct. 281, 32 L. Ed. 682; *Selma v. Colby First Nat. Bank*, 21 Wall. 609, 22 L. Ed. 687, *Bailey v. Mosher*, 63 Fed. 488, *Roberts v. Hill*, 24 Fed. 571, *Pearson v. Durell*, 77 F (2d) 465, *cert. den.* (*Durell v. Pearson*), 296 U. S. 606, 56 S. Ct. 122 (1935).

<sup>110</sup> *Aycock v. Bradbury*, 77 F (2d) 14 (1935), *Roberts v. Hill*, *supra* n. 109.

<sup>111</sup> *Hirning v. Fed. Res. Bank*, 52 F (2d) 382 (1930).

<sup>112</sup> *Smith v. Baldwin*, 69 F (2d) 390 (1934).

<sup>113</sup> *Brill v. McInnes*, 14 F (2d) 306.

<sup>114</sup> *Scott v. Armstrong*, *supra* n. 109; *Selma v. Colby First Nat. Bank*, *supra* n. 109; *Fed. Res. Bank v. Omaha Nat. Bank*, 45 F (2d) 511, *cert. den.* 54 S. Ct. 215 (1934), *Aycock v. Bradbury*, *supra* n. 110 (1935), *Pearson v. Durell*, *supra* n. 109 (1935), *Steele v. Randall*, 19 F (2d) 401; *Hayden v. Thompson*, 71 Fed. 60, 65.

<sup>115</sup> *McDonald v. Chemical Nat. Bank*, 174 U. S. 610, 19 S. Ct. 787, 43 L. Ed. 1106, *National Security Bank v. Butler*, *supra* n. 109; *Mechanics Universal Joint Co. v. Culhane*, 80 F (2d) 147 (1935); *Pearson v. Durell*, *supra* n. 109 (1935), *Nelson v. Lewis*, 73 F (2d) 521 (1934), *Isaacs v. Stock*, 66 F (2d) 928, *American Surety Co. v. Jackson*, 24 F (2d) 768, *Brill v. McInnes*, *supra* n. 113, *Brown v. Stronach*, 7 F (2d) 685, *Ball v. German Bank*, 187 Fed. 750, 753, *cert. den.* 225 U. S. 709, 32 S. Ct. 840, 56 L. Ed. 1267, *Roberts v. Hill*, *supra* n. 109.

<sup>116</sup> *Kullman v. Wooley*, 83 F. (2d) 129 (1936); *Salem Trust Co. v. Federal Nat. Bank*, 78 F (2d) 407 (1935), *Aycock v. Bradbury*, *supra* n. 110 (1935), *First Nat. Bank v. Anderson*, 57 F (2d) 17, *Ball v. German Bank*, *supra* n. 115, But see: *Rucker v. Kokrda*, 68 F (2d) 73 (1933).

and the intent of the officers to give a preference is presumed where they know of the bank's failing condition, or, not knowing, are presumed to know, if, from the circumstances, they would contemplate it.<sup>117</sup> Transactions "in the ordinary course of business", while the bank is technically insolvent but still carrying on as usual in the hope of remaining open, do not come within the inhibitions of the Act and are valid.<sup>118</sup>

## G

*Set-Off: Mutuality as Necessary Basis—Set Off of Deposit of Trustee or Receiver in Bankruptcy Against Dividends Due Bank On Its Claim Against Bankrupt*

The right of set-off is governed by the conditions of things existing at the moment of insolvency and not by circumstances thereafter created.<sup>119</sup> Claims acquired after insolvency, by assignment or otherwise, can not be used for an offset,<sup>120</sup> but the immaturity of a claim need not prevent its being used as the basis of a set-off.<sup>121</sup> Mutuality must exist before claims may be set-off, and this means that the debts or credits must be mutual or reciprocal, existing between the same persons

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<sup>117</sup> *Nelson v. Lewis*, *supra* n. 115 (1934), *Aycock v. Bradbury*, *supra* n. 110 (1935); *Brill v. McInnes*, *supra* n. 113; *Roberts v. Hill*, *supra* n. 109; *Browne v. Stronach*, *supra* n. 115, *First Nat. Bank v. Andresen*, 57 F (2d) 17, *Ball v. German Bank*, *supra* n. 115.

<sup>118</sup> *Easton v. Iowa*, 188 U. S. 220, 23 S. Ct. 288, 47 L. Ed. 452; *McDonald v. Chemical Nat. Bank*, *supra* n. 115. (Transactions held not to be in ordinary course of business: Offering depositor choice of securities in lieu of deposit on imminence of withdrawal,—*Aycock v. Bradbury*, *supra* n. 110; Pledges to secure deposits,—*Parks v. Knapp*, 29 F. (2d) 547 and cases cited *supra* n. 17 & 18, Transfer of assets to a creditor in settlement of deposit liability,—*Ball v. German Bank*, *supra* n. 115, *National Security Bank v. Butler*, *supra* n. 109.)

<sup>119</sup> *Dakin v. Bayly*, 290 U. S. 143, 78 L. Ed. 229, 90 A. L. R. 999 (1933), *Merrill v. Nat. Bank*, 173 U. S. 131, 19 S. Ct. 360, 43 L. Ed. 640; *Yardley v. Philler*, 167 U. S. 344, 17 S. Ct. 835, 42 L. Ed. 192; *U. S. v. Knox*, 111 U. S. 784, 4 S. Ct. 686, 28 L. Ed. 603; *First Nat. Bank v. Malone*, 76 F (2d) 251 (1935), *McCandless v. Dyar*, 34 F. (2d) 989; *Yardley v. Clothier*, 51 Fed. 506, 17 L. R. A. 462; *Hudson v. Thomas*, 6 F Supp. 857.

<sup>120</sup> *Scott v. Armstrong*, *supra* n. 109; *First Nat. Bank v. Malone*, 76 F (2d) 251 (1935).

<sup>121</sup> *Scott v. Armstrong*, *supra* n. 109.

at the same time in the same capacities, as a general rule,<sup>122</sup> but the Act does not require the strict mutuality at law so as to deprive depositors of equitable offsets if sufficient basis exists in equity therefor.<sup>123</sup> Accordingly, an indorser ordinarily can not set off his liability against his deposit claim<sup>124</sup> although the contrary has also been held.<sup>125</sup> Rent falling due after insolvency can not be used to set off against a liability existing at the moment of insolvency;<sup>126</sup> nor can a deposit or other claim against the bank be set off against a stock liability,<sup>127</sup> but the dividends due him on his claim may be set off against his stock liability,<sup>128</sup> even though the debtor had assigned his claim after suspension but before the stock assessment levy was made.<sup>129</sup> In order to prevent injustice, where a secured creditor is also liable as a stockholder, the two claims may be set off in equity.<sup>130</sup>

An interesting question<sup>131</sup> arises where a receiver or trustee in bankruptcy deposits funds of the insolvent's or bankrupt's estate in a bank which is also a creditor of the insolvent or bankrupt, and such bank subsequently closes. The great weight of authority is that the claim of the bank against the

<sup>122</sup> *Wasson v. White*, 12 F (2d) 809; *Poisson v. Williams*, 15 F (2d) 582 (1926), *Richmond v. Litteer*, 1 F (2d) 311, *In re United Grocery Co.*, 253 Fed. 267, *Peurifoy v. Gamble*, 145 S. C. 1, 142 S. E. 788, 71 A. L. R. 783.

<sup>123</sup> *Roelker v. Bromley-Shepard Co.*, 73 F (2d) 618 (1934), *cert. den.* 294 U. S. 713, 55 S. Ct. 509, 79 L. Ed. — (1935), *Gray v. School Dist.*, 67 F (2d) 141, *cert. den.* (*Hustead v. School Dist.*), 291 U. S. 660, 54 S. Ct. 377, 78 L. Ed. 1052 (1935), *Broomfield v. Trinidad*, 36 F (2d) 646, *Hudson v. Thomas*, 6 F (2d) 857.

<sup>124</sup> *Shannon v. Sutherland*, 74 F (2d) 530 (1935); *Bryant v. Williams*, 16 F (2d) 159.

<sup>125</sup> *Williams v. Rose*, 218 Fed. 898, *Yardley v. Clothier*, 51 Fed. 506, 17 L. R. A. 462.

<sup>126</sup> *Standard Oil Co. v. Elliott*, 80 F (2d) 158 (1935).

<sup>127</sup> *Lantry v. Wallace*, 182 U. S. 536, 21 S. Ct. 878, 45 L. Ed. 1218, *Roth v. Baldwin*, 74 F (2d) 1003, *cert. den.* 295 U. S. 737 (1935), *Williams v. Rose*, *supra* n. 125.

<sup>128</sup> *Roth v. Baldwin*, *supra* n. 127.

<sup>129</sup> *King v. Armstrong*, 50 Ohio St. 222, 34 N. E. 163.

<sup>130</sup> *Reconstruction Finance Corp. v. Rawlings*, 76 F (2d) 566 (1935).

<sup>131</sup> *Parker, J. "Bankruptcy and Bank Deposits"*, *Commercial Law Jour.* (Dec., 1934), p. 621 (Address of Hon. John J. Parker, U. S. Cir. Ct. (4th) before conference of Referees in Bankruptcy.)

insolvent or bankrupt can not be set off against the trustee or receiver on the deposit claim.<sup>132</sup> However, there is a conflict of authority, even in the Federal courts, as to the right of the trustee or receiver to set off the *dividends* due the bank against the bank's liability on the deposit—the Supreme Court<sup>133</sup> and one Circuit Court of Appeals<sup>134</sup> in cases involving *state banks*, having followed the rule that such an offset is proper, while another Federal court,<sup>135</sup> in a case involving a controversy between a national bank receiver and a trustee in bankruptcy followed the general rule and denied the offset.

The *Hood* case<sup>136</sup> declares that the *deposit* and the *liability for dividends in bankruptcy* are mutual claims—that the trustee's liability to the bank is not for the face of the claim, but for dividends which may be declared on it; that it is quite equitable that against this liability he be allowed to set off the deposit which was made by him in the same capacity as that in which he is charged with liability for payment of dividends, that the funds in the bank until suspension were subject to summary control of the bankruptcy court; that the bank and other creditors had an equal interest therein; that when the bank closed the bankruptcy court was precluded from summarily recovering the deposit and, therefore, it would be inequitable and unjust to the other creditors of the bankrupt to permit the bank to receive additional funds in the way of dividends from the bankrupt estate until all the other creditors are placed in position to share on an equal basis, and it

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<sup>132</sup> *Peurifoy v. Gamble*, 145 S. C. 1, 142 S. E. 788, 71 A. L. R. 783 and cases there cited. (In 71 A. L. R. at p. 808, the annotator, either erroneously or inadvertently, discusses the *Gardner* case, *ibid.* n. 133, as authority for a set-off of deposit against the claim of the bank against the bankrupt, whereas the case turns on right to set-off *dividends* due the bank on its claim against the bank's deposit liability.)

<sup>133</sup> *Gardner v. Chicago Title & Tr. Co.*, 261 U. S. 453, 43 S. Ct. 424, 67 L. Ed. 741, 29 A. L. R. 622 (1923).

<sup>134</sup> *Hood v. Brownlee*, 62 F (2d) 675, 22 Am. B. R. (N. S.) 441 (1933). See also: *In re Wingert*, 16 F Supp. 873 (Nov. 6, 1936).

<sup>135</sup> *In re United Grocery Co.*, 253 Fed. 267. Cf. *Richmond Ins. Co. v. Litter*, 1 F (2d) 311, and *Wasson v. White*, 12 F (2d) 809 (involving receivers of national banks). But see: *In re Wingert*, 16 F Supp. 873 (Nov. 6, 1936).

<sup>136</sup> *Supra* n. 134.

is concluded that to permit the bank to collect its dividends while indebted to the trustee for funds in which the other creditors have an equal right would accord the bank an unfair advantage.

On the other hand, it is argued that the ratable distribution mandate of the Act guarantees to all creditors of the bank the same treatment, without preference, and that when the bank closed, the trustee became a general creditor, entitled to no more rights than any other general creditor; that the claim of the bank is an asset out of which ratable dividends should be paid all creditors of the bank; that nothing subsequent to insolvency could enlarge or diminish the right of such creditors to those ratable dividends; that at the moment of insolvency there could be nothing to set off against the deposit liability except the liability of the trustee to pay dividends, which is speculative and unascertainable, and could only be determined by conditions arising subsequent to insolvency;<sup>136½</sup> that to accord the trustee the right to set off would prevent the bank's receiver and the bank's creditors from realizing anything on the bank's claim until the trustee was repaid in full; that such procedure would amount to the same thing as a preference and violate the purpose of the Act to guarantee a ratable distribution. Such is the reasoning of the *United Grocery* case,<sup>137</sup> and it is the *only*<sup>137½</sup> case involving a controversy between an insolvent national bank and a trustee in bankruptcy growing out of a dispute over the effect of similar provisions of two codes which, at first blush, appear conflicting in operation.<sup>138</sup> Since the *Hood*<sup>139</sup> and *Gardner*<sup>140</sup>

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<sup>136½</sup> *Peurifoy v. Gamble*, *supra* n. 132 and cases cited 71 A. L. R. 806.

<sup>137</sup> *Supra* n. 135.

<sup>137½</sup> A recent District Court case is to contrary. *In re Wingert*, 16 F Supp. 873 (Nov., 1936).

<sup>138</sup> Cf. R. S. Sec. 5236, 12 U. S. C. A. Sec. 194, and Sec. 68a Bankruptcy Act; 30 Stat. 541, 11 U. S. C. A. Sec. 108. (In *Cumberland Glass Co. v. DeWitt*, 237 U. S. 447, 35 S. Ct. 636, 59 L. Ed. 1042, it was held that Sec. 68a of the Bankruptcy Act is permissive only, not mandatory, and only recognizes the general rule of set-off enabling the courts to invoke the principle to mutual credits.)

<sup>139</sup> *Supra* n. 134.

<sup>140</sup> *Supra* n. 133.

cases were not concerned with the ratable distribution mandate of the National Bank Act, those cases are not exactly controlling, and may very well be distinguished from the *United Grocery* case,<sup>141</sup> which, on the precise question involved, correctly denied the offset claimed.

Let us suppose that a receiver of a state bank deposited funds in a national bank which was a creditor of the insolvent state bank, and assuming that later on the national bank suspended, could it logically be contended that the receiver of the state bank, as a general creditor, has any greater rights than any other general creditors? The state bank receiver would come within the general rule denying him any right to retain and apply dividends, and it would seem that a trustee in bankruptcy stands in an analogous position without greater favor or equities.

It is submitted, as the most equitable solution, and one which may be adopted without violating the ratable distribution requirements, that an offset be allowed on the following basis: (1) determine what proportion the bank's claim bears to the total of all claims of creditors against the bankrupt estate, and from this computation reckon the amount of the beneficial interest of the bank itself in the deposit of the trustee, and set off that beneficial interest in the deposit against its deposit liability; (2) if the bank, at suspension, is entitled to dividends already declared but not delivered over to it by the trustee, those dividends should be set off against the deposit liability because they would be mutual demands; (3) all further dividends declared by the bankrupt estate upon the net balance of the bank's claim should be withheld by the trustee and set off against the deposit until same is fully satisfied; (4) in the meantime, any dividends paid on the deposit should be delivered to the trustee for distribution to the other creditors of the bankrupt's estate, without the bank participating therein; and (5) after the deposit liability is fully discharged, the bank would participate ratably on the balance of its claim in the remaining general assets of the estate. Under this plan the bank would get the

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<sup>141</sup> *Supra* n. 135.

benefit of an equitable offset of its beneficial interest in the deposit, but would not receive more than its share because the dividends on the deposit would be transferred to a special fund by the trustee, for the exclusive distribution of dividends to the other creditors. In this manner the bank would not receive a double benefit, or advantage in the deposit, nor would the other creditors of the bankrupt receive an advantage over the bank in the general assets of the bankrupt estate. Therefore, it appears that full force and effect is given to the equities of all parties, and the ratable distribution rights of the respective claimants are preserved inviolate.

The Banking Act of 1935, as we have already shown, subrogates the Federal Deposit Insurance Corporation to the right of the depositor to the extent of his insured deposit, upon payment by the Corporation of the insured portion of the deposit.<sup>142</sup> Moreover, the Act provides that the Corporation "may withhold payment of *such portion of the insured deposit* of any depositor in a closed bank as may be required to provide for the payment of any liability of such depositor as a stockholder of the closed bank, or of any liability of such depositor to the closed bank, or its receiver, *which is not offset against a claim* due from such bank, pending the determination and payment of such liability by such depositor or any other person liable therefor."<sup>143</sup> (Italics mine). If a depositor has a deposit exceeding the insured amount, and is indebted to the bank for less than the insured amount, there may be some question whether the *insured portion*, i. e., the first \$5,000, shall be used to accomplish the offset, leaving the depositor a general claim for the uninsured balance, or whether the phrase, "such portion of the insured deposit . . . which is not offset against a claim . . .", has reference to the *whole* deposit, entitling the depositor to use the uninsured portion first toward effecting the offset, then so much of the insured part as is necessary, and leaving to him the remaining portion fully insured.

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<sup>142</sup> 12 U. S. C. A. Supp. 1935, Sec. 264L(7).

<sup>143</sup> 12 U. S. C. A. Supp. 1935, Sec. 264M(4).

No doubt this provision was incorporated in the Act in recognition of the right to set off, and to protect the Federal Deposit Insurance Corporation. At the same time, the general purpose of the Act to provide insurance protection to the depositor must be given effect. It seems likely, then, that the language employed will be given a construction which will afford the Corporation the right to enter on its records, in the receivership, an offset of the excess over \$5,000 plus any amount of the first \$5,000 required, to accomplish the offset, and, since it would then owe nothing on the part offset, it could withhold payment of the insured balance until the offset so made is made conclusive by consent or otherwise. If this were not the rule, the Corporation could use all or as much of the first \$5,000 necessary to offset against the depositor's liability, and make him take a common claim for the balance of his deposit, if his deposit and liability each exceeds \$5,000. The general purpose of the Act does not admit of the adoption of any such fantastic construction because in such a situation a depositor would not receive the benefit of any insurance.

It may be, since deposits can not be offset against stock liability, or indirect liabilities, or other liabilities lacking the required mutuality to warrant an offset, that the payment of any portion of the insured deposit (first \$5,000) which is not required to offset against his direct or mutual liabilities, may be withheld until the debtor discharges his other liabilities. If this construction is adopted, it would neither alter the established rule as to the required basis for an offset, nor deprive the depositor of his insurance; but, if it is contemplated that by *withholding* the practical effect of an offset may be accomplished, then a revolutionary innovation has been introduced in the law of offsets.



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