RECENT CASES

Banks and Banking—Statutory Liability of Stockholders of Holding Company— [Federal and Michigan].—A holding company acquired a majority of the stock of seven banks by exchanging its own stock for that of these banks. On the insolvency of one of these subsidiaries and of the parent company, the plaintiff, receiver of the insolvent subsidiary, brought this suit against the stockholders of the parent corporation as the beneficial owners of the stock of the insolvent bank, to recover the statutory double liability thereon, *held*, complaint dismissed. In the absence of averments of fact that Bancorporation was without substantial assets other than bank stock, its corporate entity could not be disregarded so as to charge its stockholders with the liability of the corporation *Pearson v. All Borg.*[1] Where a securities corporation acquired bank stock in the course of its general business, a similar finding of immunity of the stockholders was predicated on the absence of fraudulent intent to evade the liability *Burrows v. Emery.*[2] So also, no liability attached to stockholders of an insolvent holding company owning double liability bank stock where such stockholders had been assured that the company would invest in industrials alone *Nettles v. Rhett.*[3]

The situation presented by these three cases is one in which the courts must choose between the strong statutory policy of protecting bank depositors expressed in the double liability provisions which existed until recently under the national banking law[4] and in all but ten states,[5] and the concept of corporate entity[6] which operates to limit stockholders' liability. The tendency in the application of the statutes has been to extend liability[7] by disregarding the forms of transactions so as to hold the real owner of bank stock.[8] In the simple case, where a corporation controlled by the owner of bank stock has taken title to stock previously held by him in his individual capacity, the courts have had little difficulty in disregarding the corporate entity because of the intentional fraud on the depositors,[9] and this device to avoid liability

[1] 23 F. Supp. 837 (Ill. 1938). [2] 280 N.W. 120 (Mich. 1938).

[3] 24 F. Supp. 304 (S.C. 1938). This decision is interesting in view of a previous holding in the same situation that the liability of preferred stockholders was not affected by a showing that they had never owned bank stock but had purchased holding company stock for cash, and that they had no control of the company. Nettles v. Rhett, 94 F. (2d) 42 (C.C.A. 4th 1938).

[4] 38 Stat. 273 (1913), 12 U.S.C.A. § 64 (1936).

[5] 80 U. of Pa. L. Rev. 1133, note 1 (1932).

[6] For a discussion of the validity of this concept see Latty, Subsidiaries and Affiliated Corporations, c. 2 (1936).

[7] Michie, Banks and Banking, c. 15, §§ 72–102 (1932).

[8] Pauly v. State Loan and Trust Co., 165 U.S. 606, 619 (1896).

[9] Corker v. Soper, 53 F. (2d) 190 (C.C.A. 5th 1931) *cert. denied*, Corker v. Howard, 285 U.S. 540 (1931); Harris Investment Co. v. Hood, 123 Fla. 598, 167 So. 25 (1936); Brusselback v. Cago Corp., 85 F. (2d) 20 (C.C.A. 2d 1936) *cert. denied*, 299 U.S. 586 (1936); Durrance v. Collier, 81 F. (2d) 4 (C.C.A. 5th 1936).

has been no more successful than the older one of registering the stock in another's name.[10]

Litigation concerning the failure of the Detroit Bankers Company and its operating banks presents the more difficult problem arising where the holding company was organized for the legitimate purpose of unifying the operation of a group of banks. In finding that the company was liable on the failure of a bank whose stock was held in trust for a wholly owned subsidiary of the company, the court based its decision on the "beneficial owner" theory.[11] On failure of the company, both the state and federal courts in finding the stockholders liable,[12] relied on a provision in the stock certificate, held to be a contract, that the stockholders would be liable for any losses sustained by the company through the failure of the operating banks, although the federal court intimated that in view of the statutory policy the same result would be reached even in the absence of a contract.[13] That a contract, though material to liability is not prerequisite, at least in the federal courts, where the holding company was dealing primarily in bank stock and had no other substantial assets, is shown by the *Banco-Kentucky* cases.[14] The stockholders of a corporation owning trustees' participation certificates containing a contract similar to the above were held liable as the real owners of the bank stock and the absence of such a contract in the stock certificates of the holding company was held not controlling.[15] That liability arises in such circumstances, without a contract and without fraudulent intent to evade the statute is shown by *Nettles v. Rhett*[16] where the decisions of the lower court[17] for the stockholders, based on these grounds was reversed.

Although there is language in the cases that wherever a corporation owns double liability bank stock, its stockholders will be liable thereon,[18] such a broad view of liability has been questioned[19] and is not supported by the cases. Particularly where the purpose in setting up the holding company is other than to evade liability, the principal cases show that stockholders are not held liable where there were substantial

[10] Case v. Small, 10 Fed. 722 (C.C. La. 1881); Ohio Valley Nat'l Bank v. Hulitt, 204 U.S. 162 (1906).

[11] Fors v. Farrell, 271 Mich. 358, 260 N.W. 886 (1935) noted 20 Minn. L. Rev. 217 (1936).

[12] Simons v. Groesbeck, 268 Mich. 495, 256 N.W. 496 (1934); Barbour v. Thomas, 86 F. (2d) 510 (C.C.A. 6th 1936) *cert. denied*, 300 U.S. 670 (1936). See also the opinions of the lower court, 7 F. Supp. 271 (Mich. 1933) noted 2 Univ. Chi. L. Rev. 484 (1935) and 33 Mich. L. Rev. 273 (1934).

[13] Barbour v. Thomas, 86 F. (2d) 510, 518 (C.C.A. 6th 1936).

[14] Laurent v. Anderson, 70 F. (2d) 819 (C.C.A. 6th 1934); BancoKentucky's Receiver v. Louisville Trust Co.'s Receiver, 263 Ky. 155, 92 S.W. (2d) 19 (1936); Anderson v. Atkinson, 22 F. Supp. 853 (Ill. 1938); Anderson v. Abbott, 23 F. Supp. 265 (Ky. 1938).

[15] Anderson v. Abbott, 23 F. Supp. 265 (Ky. 1938).

[16] 94 F. (2d) 42 (C.C.A. 4th 1938) noted 33 Ill. L. Rev. 104 (1938). See also Metropolitan Holding Co. v. Snyder, 79 F. (2d) 263, 103 A.L.R. 912 (C.C.A. 8th 1935); Hansen v. Agnew 80 P. (2d) 845 (Wash. 1938).

[17] 20 F. Supp. 48 (S.C. 1937). *Cf.* the approved quotation from a case involving a different point in Burrows v. Emery, 280 N.W. 120, 124 (Mich. 1938).

[18] Nettles v. Rhett, 94 F. (2d) 42, 47 (C.C.A. 4th 1938) quoted with approval in Hansen v. Agnew, 80 P. (2d) 845, 852 (Wash. 1938).

[19] Nettles v. Sottile, 184 S.C. 1, 33, 191 S.E. 796, 809 (1937).

assets in addition to bank stock or a substantial business exclusive of dealings in such stock. Despite the existence of language to the contrary,[20] such cases are not to be explained by the absence of a fraudulent intent.[21] It is suggested that where the purpose of the holding company was primarily to profit from the *banking* business of its subsidiaries, the policy of the statute that those who profit from banking shall assume an additional liability justifies the "piercing of the corporate veil" even where the corporation had substantial assets in addition to bank stock. Conversely, where there was operated a non-banking business, as in *Burrows v. Emery*,[22] which business only incidentally dealt in bank stock, such considerations of policy do not apply. On the other hand, it may be argued in support of both cases that whatever the purpose of the holding company, the fact that it held substantial assets in addition to bank stock, presumably sufficient to meet the reasonable strains of the business, will protect its stockholders from further liability on ordinary principles. But where the stockholder's defense is that he was assured that only industrial stock would be purchased,[23] it is difficult to see why this should be available as against creditors of the bank, or anyone other than the promoters themselves.[24] Cases denying liability may also be in accord with the tendency to repeal the statutes creating it.[25] The usefulness of this device as a protection to bank depositors has been questioned[26] and in recent years it has generally been superseded by deposit insurance. But any argument in favor of the restriction of liability on analogy with the policy of these statutes must overcome the objection that they contemplate the existence of a different type of protection for creditors.

Contracts—Statute of Frauds and Formalities of Agreement To Arbitrate—[New York].—The petitioner entered into nine oral contracts of sale with the respondent, each exceeding the value of fifty dollars, and confirmed by written standard forms of sales notes, mailed to and retained by the respondent without objection. Each note contained a provision that "any controversy arising under or in relation to the particular contract should be settled by arbitration." The respondent failed to perform three of the contracts. *Held*, the statute of frauds was no bar to a motion to compel arbitration. The existence of a written contract,[1] although not signed by the party to be charged, satisfies the formal requirements of the New York Arbitration Act.[2] *In re Exeter Mfg. Co.*[3]

[20] Burrows v. Emery, 280 N.W. 120, 124 (Mich. 1938).

[21] See note 15 *supra*.

[22] 280 N.W. 120 (Mich. 1938).

[23] Nettles v. Rhett, 24 F. Supp. 304 (S.C. 1938).

[24] This case may be explained as a result of the state statute which made the purchase of bank stock by a corporation illegal.

[25] Double liability of bank stockholders has been recently abolished or modified as to national banks, 48 Stat. 189 (1933), 12 U.S.C.A. 64a (1936) and as to state banks in a majority of states. But an attempt to repeal the double liability provisions in Illinois by a constitutional amendment submitted to the voters failed in the November, 1938, election.

[26] See the statement in Nettles v. Rhett, 20 F. Supp. 48, 52 (S.C. 1937).

[1] The question of whether a written contract was actually formed by the respondent's retention of the sales notes without objection is referred to the lower court.

[2] Gilbert-Bliss, Civil Practice Act of New York §§ 1448, 1449 (1938).

[3] 5 N.Y.S. (2d) 438 (1938).