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Banks and Banking-Deposits After Insolvency

RECENT CASE NOTES

BANKS AND BANKING—DEPOSITS AFTER INSOLVENCY—T deposited money in bank thirty minutes before closing time. The next day was a legal holiday, and on the following day, the bank was closed by the state bank commissioner. T sues to have the deposit declared a preferred claim. *Held*, T must come in with the general creditors because there was no allegation of fraud nor of insolvency of bank at time of deposit, presented by the pleadings. *Barger v. Stultz*, Appellate Court of Indiana, Sept. 4, 1930, 172 N. E. 549.

The relation of banker and depositor, in general, is that of debtor and creditor with no preference being given to depositors over general creditors. But most courts will give preference to the claim of one who deposits money in a bank, known by its officers to be insolvent. The grounds for this are that since the deposit was induced by the fraudulent representation of solvency thru continuing business, a constructive trust arises. *Pennington v. Third Nat. Bank of Columbus, Ga.*, 77 S. E. 455, 104 Va. 674, 45 L. R. A. (N. S.) 319. *Furber v. Dane*, 204 Mass. 412, 90 N. E. 859, 27 L. R. A. (N. S.) 808. *Barnard v. Black*, Ind. App. 1930, 169 N. E. 872.

In order to establish a preferred claim it is necessary to prove, first the actual insolvency of the bank and, second, knowledge of such insolvency on the part of the bank officers. *Barger v. Stultz, supra.* The establishing of these facts presents a difficult problem for the courts. Some decisions hold that the mere fact that the bank is in difficulties is not enough to make its receiving of deposits fraudulent, if its officers believe the bank has a chance to recover. *Dunlap v. Seattle Nat. Bank*, 161 Pac. 364. *Brennan v. Tillinghast*, 201 Fed. 609, 120 C. C. A. 37. Other cases say insolvency is inability to pay debts in the ordinary course of business as persons carrying on banking usually do. *Steele v. Allen*, 240 Mass. 394, 134 N. E. 401, 20 A. L. R. 203. A middle ground is that a bank is insolvent when all of its assets are insufficient to meet its liabilities. *Youmans v. State*, 7 Ga. App. 101, 66 S. E. 383. Indiana has, apparently, never passed upon the point. There is a decided split of authority as to whether or not knowledge of bank officials necessary to impute fraud to the bank may be inferred from the actual fact of insolvency. The weight of authority seems to be that the depositor must prove the officials had actual knowledge of the insolvency at the time the deposit was received. *Furber v. Dane, supra; Fidelity and Deposit Co. v. Kelso State Bank*, 287 Fed. 828; *Metropolitan State Bank v. Lloyd*, 90 N. Y. 630. Some courts will infer knowledge of banker from the surrounding circumstances, *White v. Poole*, 272 S. W. 1021; especially in the case of a private bank. *In Re Silver*, 208 Fed. 797. And where there was a statute similar to Burns 1926 sec. 2479 making a receiving officer criminally liable for banks receiving deposits while insolvent, and making failure of a bank within 60 days (Indiana says 30) after receiving deposits, *prima facie* evidence of the insolvency, the depositor was allowed a preferred claim even though his complaint did not allege fraud. *Hughes v. Martin*, 81 Okla. 89, 196 Pac. 951; *Meadowcraft v. People*, 163 Ill. 56, 45 N. E. 303, 35 L. R. A. 176. Knowledge is usually inferred where the insolvency is caused by

criminal acts of a bank official, *Orme v. Baker*, 74 Ohio St. 337, 78 N. E. 439, 113 A. S. R. 968; *Somerville v. Beal*, 49 Fed. 790. But not where the defaulter is a minor officer, *Perth Amboy Gas-Light Co. v. Middlesex County Bank*, 60 N. J. E. 84, 45 Atl. 708. *State v. Cadwaller*, 154 Ind. 607, 57 N. E. 512, citing *Meadowcraft v. People, supra*, held that a banker is presumed to know of the insolvency if by the exercise of reasonable diligence he could have ascertained it. But this was a criminal trial under Burns 1926 sec. 2479. A more recent civil case, *Barnard v. Black, supra*, seems to require actual knowledge of bank officers.

Another question in connection with holding a deposit after insolvency as a preferred claim is to determine how far the deposit may be traced into the general assets of the bank. What appears to be a majority of the cases which treat the deposit as a constructive trust follow the analogy of the old requirement of maintaining the identity of the trust *res*, and refuse to give a preferred claim to the depositor if the deposit has been mingled with the general funds of the bank. *Pennington v. Third Nat. Bank, supra; Sadler v. Belcher*, 2 Moody & R. 489; *Furber v. Steppens*, 55 Fed. 17; *Atkinson v. Rochester Printing Co.*, 114 N. Y. 168. Others say the depositor must show that the identical money deposited had not been paid out by the bank, *Re North River Bank*, 60 Hun. 91. Still others will give the depositor a preferred claim only on proof that the identical money deposited remains in the mass of the bank's funds in the receiver's hands. *Lake Erie & Western R. R. v. Indianapolis Nat. Bank*, 65 Fed. 690. And some will even allow depositors a preference out of all of the banks assets. *St. Louis Brewery Association v. Austin*, 100 Ala. 313; *Brennan v. Tillinghast, supra*. Indiana holds with this latter doctrine even tho the courts admit it to be the minority rule, and allow recovery even tho the deposit has been used to pay debts or to buy property for the bank, so long as the assets are greater than the deposit. *Shopert v. Indiana Nat. Bank*, 41 Ind. App. 474, 83 N. E. 515. *Reserve Loan Insurance Co. v. Dulin*, (Ind. App.) 135 N. E. 590; *State v. Farmers & Merchants Bank*, 71 Ind. App. 216, 124 N. E. 501; *Winstandley v. Second National Bank of Louisville*, 41 N. E. 957; *Barnard v. Black, supra*. The Indiana rule is in accord with the modern tendency to disregard the old requirement of "earmarked money" as a trust *res* and hold that if the money can be followed into the deposit, there is sufficient identification. *Perry on Trusts* (Seventh Ed.) Vol. II, p. 1405.

A final moot point is raised by the attempt to hold bank officers personally liable for loss of deposits received by the bank after insolvency. Most courts that have passed on the subject allow recovery against the official, *Tate v. Bates*, 118 N. C. 287, 24 S. E. 482; *Miller v. Harvard*, 95 Tenn. 407, 32 S. W. 305, at least to the difference between the deposit and the depositor's share of the bank's assets. *Boker v. Ashe*, 80 Tex. 356, 16 S. W. 36.

Again, a majority of the cases require affirmative proof that the officer had actual knowledge of the insolvency. *Duffy v. Byrne*, 7 Mo. App. 417; *St. Louis & S. F. R. R. v. Johnson*, 133 U. S. 566. But a strong minority will admit constructive notice of the insolvency. *Delano v. Case*, 121 Ill. 247, 12 N. E. 676. And where depositor has relied on a personal statement of the officer as to bank's solvency, officer was held liable without further proof of knowledge of insolvency. 117 N. C. 330, 23 S. E. 461.

The question has never arisen in Indiana but the courts would probably follow the rule of *Bernard v. Black, supra,* in requiring actual notice, altho states having a criminal statute similar to Indiana's have held constructive notice sufficient. *Hughes v. Mortin,* (Okla.) 196 Pac. 951; *State v. Perry,* 194 La. 1065, 90 So. 406.

J. S. G.