BRANCH BANKING: The making of loans, taking notes by another corporation, as agent for the bank, from the borrowers and made directly to a bank, some notes made to the other corporation and delivered to the bank without the endorsement of the other corporation, and servicing of all such notes, in a city other than the home city of the bank and in a building other than the banking house of the bank in its home city, constitute branch banking on the part of the bank.

June 15, 1950

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6/15/50

Honorable Harry G. Shaffner
Commissioner of Finance
Department of Business and Administration
Jefferson City, Missouri

Dear Commissioner Shaffner:

Your letter requesting the opinion of this Department on whether the proceedings and acts of a bank chartered by the laws of Missouri as described in the letter constitute branch banking, has been received. Your letter states:

> "Parties owning control in a state chartered bank have formed a safe deposit company which is understood to have been incorporated by the Secretary of State of Missouri. This company makes loans at an office located some thirty miles from the bank, in other words, out of the banking quarters.
>
> "Persons borrowing money at the office of the safe deposit company sign notes which are payable to the safe deposit company. Advances to the borrower are drawn against funds of the lender on deposit at the bank.
>
> "Such loans then are turned to the bank, some of which are endorsed, others not endorsed. The safe deposit company keeps a dual set of books, in which case they make collection on those loans sold and remit to the bank in the amount collected.
>
> "We submit a copy of an agreement furnished by the bank and the safe deposit corporation in conjunction with the establishing of

> and the servicing of all notes which originate in the safe deposit company. There is also submitted a copy of the remarks made by the examiner who examined the bank in question so that you may get his viewpoint of such transactions.
>
> "Can any of this procedure be considered branch banking?"

Together with your letter, documents, as informative matter descriptive of the activities of the bank observed and recited by an Examiner of your Division, and Examiners for the Federal Deposit Insurance Corporation, have been transmitted to us for reference and consideration. There is also transmitted with the named documents a copy of the contract, dated August 1, 1949, between the safe deposit corporation and others, on the one part, and the bank referred to in your letter as a State chartered bank, party of the other part, setting forth in detail the rights, privileges and obligations, moving from each to the other, in the carrying on of the business activities which constitute the basis of your request for our opinion whether such activities and proceedings constitute branch banking. The copy of the contract which you furnished is returned herewith.

Your letter advises that the safe deposit corporation makes loans at an office some thirty (30) miles from the bank.

Your letter advises that:

> "Persons borrowing money at the office of the safe deposit company sign notes which are payable to the safe deposit company. Advances to the borrower are drawn against funds of the lender on deposit at the bank.
>
> "Such loans then are turned to the bank, some of which are endorsed, others not endorsed. The safe deposit company keeps a dual set of books, in which case they make collection on those loans sold and remit to the bank in the amount collected."

The contract between the safe deposit corporation and others, on the one part, and the bank on the other part,

provides that the parties agree that the bank shall continue the purchase of notes from the first parties as it has in the past been doing, and that the bank shall be given protection against losses which might occur by reason of serious criticism of the transaction between the parties by bank examiners that would result in the discontinuance of such purchases by a fund called the "Safe Deposit Company CONTINGENT FUND", said fund to be derived from all discount received, or which would be received by the safe deposit corporation or its agent, a credit company, on notes which have been, or will be, after the date of said contract, purchased by said bank from the first parties, or previously acquired by such agent whose contingent funds were transferred by them to the safe deposit corporation when such individuals became officers of said safe deposit corporation. The contract provides that said contingent fund shall be set aside by the bank on the books of the bank and become the property of and payable to the safe deposit corporation only when and to the extent that the balance in said fund exceeds the total of the then determined delinquent loans and 10% of the unpaid balances on all non-delinquent loans acquired by said bank from the sources hereinbefore mentioned, either before or after the date of the contract. It is further provided in said contract that losses on notes (from any cause whatsoever) and write-downs required by bank examiners on notes and any delinquent notes protected hereunder, shall be chargeable to said fund at the sole discretion of any executive officer of said bank, and such officer, or officers, shall be the sole judge of the proper time and amount of such charges. Said contract further states that it is understood that the bank shall receive a discount for its own income on notes so acquired; such discount to be fixed by mutual agreement as to each note at the time of its acquisition by said bank, and the entries made thereupon on the books of said bank shall be irrefutable evidence of the discount agreed upon.

The contract concludes by providing that if the safe deposit corporation shall, at any time, suffer a loss on a note re-purchased from the bank, the safe deposit corporation shall be reimbursed for such loss by the bank only out of the safe deposit corporation Contingent Fund, and only to the extent that said fund is not thereby reduced to an amount less than the balance of said fund sixty (60) days previous to the date of the charge.

We have noted above that losses or notes from any cause whatever, write-downs, required by bank examiners on such notes, and such other notes as become delinquent shall, under the contract, be chargeable to said fund at the sole discretion of any executive officer of said bank. (Underscoring ours.) These advantages and preferences moving to the bank without any corresponding obligation upon its part to allow the use of the Contingent Fund, which is created out of the principal, if not the only, income the safe deposit corporation has, for recoupment for such losses, leaves, as we view it, the safe deposit corporation entirely without right or remedy to subject its Contingent Fund to the discharge of its losses. This, and the further requirement of the contract that write-down notes required by bank examiners and delinquent notes protected by said fund shall be chargeable to said fund at the sole discretion of any executive officer of the bank, tend very strongly to indicate that the contract in these provisions lacks mutuality because the force and effect of such terms of the contract depend entirely on the will of the bank. If there is no mutuality between the parties, with respect to these vital elements of this contract, it would be, for the want of mutuality, a unilateral contract in favor of the bank, and, therefore, void as to both parties.

"* * * There must be mutuality of agreement to give a valid contract. A written instrument which undertakes to create liability as to one party, without liability or obligation upon the other party thereto, is void as to both.* * * (Hudson et al. vs. Browning, 174 S.W. (Mo. Sup.) 393, l.c. 396.)

These observations and authorities are here made and applied in view of the trend of the statements of fact in the documents before us, to indicate that the safe deposit corporation is merely the agent and servant of the bank, and that its acts and conduct in making loans are, in reality, the acts and conduct of the bank itself.

Referring again to the memo of October 6, 1949, in which there are recited facts developed by an examination by the Federal Deposit Insurance Corporation of the affairs of the bank and the safe deposit corporation, it is revealed therein that the said safe deposit corporation was chartered in 1946 with a capital of Five Thousand ($5,000.00) Dollars

for the purpose of conducting a safe deposit business; that on December 31, 1948, the capital stock, then owned in its entirety by the bank, was sold at its book value of Five Thousand ($5,000.00) Dollars; that the majority directors and the majority stockholders of the bank are the majority directors and stockholders, respectively, of the safe deposit corporation.

It is further stated in said October 6, 1949, memo that the said safe deposit corporation was then, October 6, 1949, indebted to the bank in the sum of Forty-Nine Thousand ($49,000.00) Dollars; that the safe deposit corporation has amended its charter and now has the power to make loans; that a portion of the loans originating through the said safe deposit corporation are endorsed without recourse by the corporation (presumably to the bank); and that some of the notes carried in the bank's assets were then, (October 6, 1949) made payable to the safe deposit corporation and not endorsed by it; that all delinquent obligations (notes) are removed from the bank's assets when arrearages occur.

The memo further states that the bank follows the practice of accepting notes, by way of discount, which are payable to the safe deposit corporation and not endorsed by the safe deposit corporation.

The said memorandum of October 6, 1949, written by the examiner for the F.D.I.C. disclosing that the bank accepts discounts from the safe deposit corporation in the form of notes or otherwise, is very persuasive evidence that the bank presently would be exercising no independent judgment or discretion, with respect to the performance of their bounden duty to their stockholders, and the public, but, on the contrary, show that such practices are the result of an understood plan that the safe deposit corporation is merely the agent of the bank in providing such discounts for the bank, since the directors of the safe deposit corporation, as the seller of the discounted paper, are the same persons, who are directors of the bank, which is the buyer of such paper. In other words, the directors of the bank through themselves as directors of the safe deposit corporation are dealing with themselves as a bank in such transactions. This, we believe, inasmuch as such transactions are initiated and the loans and

discounts being made in another city, fifty miles distant from the banking house of the bank, constitutes branch banking by the bank itself through the safe deposit corporation acting as its agent.

Both letter memos of October 6, and November 1, 1949, assert that the said safe deposit corporation at Kansas City, Missouri, in making some of the loans noted, requires the notes to be made payable to the bank.

It is not, as we view the problem, a question whether the acts performed by the safe deposit corporation for the bank, such as taking notes from borrowers of money from the safe deposit corporation, payable directly to the bank, taking notes for such loans payable to the safe deposit corporation and delivered to the bank without endorsement by the safe deposit corporation, and the servicing of all notes which originate in the safe deposit corporation, whether payable to the safe deposit corporation or payable directly to the bank, are sound or unsound, safe or unsafe practices or, moreover, whether such acts in and of themselves may be considered branch banking, although such proceedings may well constitute acts of banking, but the vital inquiry here is, under the facts disclosed, as we view them, whether the bank using the safe deposit corporation as a mere pretense and screen to conceal its own acts as a bank, is itself carrying on a definite banking business outside of its own banking house. Sub-section 1 of Section 7949, R.S. Mo. 1939, defining the rights and powers of incorporated banks in this State reads as follows:

> "To conduct the business of receiving money on deposit and allowing interest thereon not exceeding the legal rate or without allowing interest thereon, and of buying and selling exchange, gold, silver, coin of all kinds, uncurrent money, of loaning money upon real estate or personal property, and upon collateral or personal security at a rate of interest not exceeding that allowed by law, and also of buying, investing in, selling and discounting negotiable and non-negotiable paper of all kinds, including bonds, as well as all kinds of commercial paper; and for all

> loans and discounts made, such corporation may receive and retain in advance the interest; Provided, however, that no bank shall maintain in this state a branch bank, or receive deposits or pay checks except in its own banking house."

Sub-section 5 of said Section 7949, empowering banking corporations to purchase real estate, and among the reasons for such provisions, one apparently was for the purpose of requiring them to have definitely located banking houses, provides that they may exercise the following powers:

> "To purchase, hold or convey real property for the following purposes:
>
> "(a) A plot whereon there is or may be erected a building or buildings suitable for the convenient transaction of its business from portions of which not required for its own use a revenue may be derived."

The United States Supreme Court in the case of ex parte Schollenberger, 96 U.S. Rep. 369, construed a statute relating to where a corporation could be served with process. In the opinion, l.c. 377, the Court had this to say:

> "A corporation cannot change its residence or its citizenship. It can have its legal home only at the place where it is located by or under the authority of its charter. * * * ."

Our Supreme Court in the case of State ex rel. Barrett vs. First National Bank of St. Louis, 297 Mo. Rep. 397, was considering a case respecting a national bank maintaining a branch bank in this State under the National Bank Act. In determining the case, and in holding that a bank may only maintain and operate one banking house, the Court, l.c. 406, said:

> "This location (of the principal office) having been established, it is within the contemplation of the statute that the power of the bank is to be there exercised. Otherwise the words 'an office or banking house'

> ceased to be specific and instead of being singular in number may be construed as plural, and thus permit the establishment of banks in as many places within the county, city or town as the judgment of the directors may prompt. Such a construction finds no resting place in reason. If followed it would, instead of centralizing and rendering more stable the powers of a bank enable it, by multiplying its place of business, to subdivide and at the same time extend its powers in such manner as to stifle competition. . . . ". (Words in parenthesis ours.)

The memoranda of the result of the examinations by the Examiners of the Federal Deposit Insurance Corporation reveals that some notes are taken by the safe deposit corporation at Kansas City, made payable directly to the bank, and in other instances, notes upon loans taken by the safe deposit corporation are turned over to the bank without the endorsement of the safe deposit corporation. The contract between the bank and the safe deposit corporation and the individuals who are named as its agents, gives the right to both the bank and the safe deposit corporation to discount notes, and especially gives the bank the right to discount notes made payable to the safe deposit corporation. These are all, we think, acts carrying on the business of banking. "Banking" is defined in 9 C.J.S., page 30, Section 1, as follows:

> "Banking is the business or employment of a bank or banker, and as defined by law and custom consists of receiving deposits payable on demand, discounting commercial paper, making loans of money on collateral security, issuing notes payable on demand and intended to circulate as money, collecting notes or drafts deposited, buying and selling bills of exchange, negotiating loans, and dealing in negotiable securities issued by the national or state government, or by municipal or other corporations. It is said, however, that any person engaged in the business carried on by banks of deposit, of discount, or of circulation is doing a banking business, although but one of these functions is exercised. * * * ."

These acts, whether performed by the safe deposit corporation as the agent of the bank, or by the bank itself, at Kansas City, Missouri, would constitute branch banking. It is true that there are two corporations, the bank and the safe deposit corporation, Kansas City, Missouri. The bank itself in the beginning carried on in its own banking house the safe deposit business, purchased by the safe deposit corporation and since operated by the safe deposit corporation upon its incorporation. The bank sold this business, or pretended to sell it, to the safe deposit corporation. The majority stockholders of the bank became the majority stockholders of the safe deposit corporation upon its said incorporation. The directors of the bank became the directors of the safe deposit corporation. This means that the stockholders in both corporations and the directorate of both corporations were identical. The safe deposit corporation, according to the memo of the examiner, in October, 1949, owed the bank $49,000.00. When a loan is negotiated by the safe deposit corporation it pays to the borrower the amount of his loan by check on the account of the safe deposit corporation to the bank. It would appear to be conclusive, we think, that should the safe deposit corporation suffer a loss from the non-payment of any note held by it or taken by it and held by the bank, involving the depletion of its account in the bank, such losses would likewise be the losses of the bank. It appears that the bank shared in a part, if not all, of the profits of the safe deposit corporation, and that all or nearly all the acts of business carried on at Kansas City, Missouri, were incidents of banking and acts that the bank is chartered under said Section 7949 to do, and which it must do under the statutes in its banking house. These facts and conditions surrounding these two corporations and identified with the acts of both in carrying on the business of lending money, discounting notes and servicing loans made by the safe deposit corporation in Jackson County, Missouri, demonstrate that the bank is the dominant power, if not the entire power, in carrying on such business. The community of interest between both corporations in the business carried on in Kansas City, Missouri, reflecting as they do that the safe deposit corporation took its initial business by purchase from the bank and continues its present corporate existence, for the purpose of negotiating the loans herein discussed, because of the favors and credit granted it by the bank, which has the power to deny further credit to the safe deposit corporation and has the further power to cast upon the safe deposit corporation the onus of the liability for losses

growing out of any of the notes negotiated by the safe deposit corporation and owned by the bank whether delinquent or not, as is provided in their said contract, and the ownership of the majority stock in the safe deposit corporation being the majority ownership of stock in the bank, all indicate that the bank has been at all times, and now is in control of and carrying on, through the safe deposit corporation, merely as its pretended agent, branch banking away from and outside of its home banking house. It is an often-expressed and well-established rule of law that whoever, whether a corporation or individuals, owns a majority of the shares of the capital stock of another corporation, controls it. (State ex inf. vs. Standard Oil Co., 218 Mo. 1, l.c. 327, citing and quoting People ex rel. v. Chicago Gas Trust Co., 130 Ill., l.c. 292).

39 C.J. 35, Section 4, defines the relationship of master and servant as follows:

> "The relation of master and servant exists whenever the employer retains the right to direct the manner in which the business shall be done, as well as the result to be accomplished, or, in other words, not only what shall be done, but how it shall be done. * * * ."

We believe that the facts here indicate that there are not two independent corporations capable of contracting and dealing each with the other at arms length, each having and exercising its own will in their contractual relationship in carrying on this business, but that the relationship of master and servant existed and still exists between these two named corporations, the bank being the master and in control of this business, and that the safe deposit corporation is the servant, subject in most, if not all, of its acts to the will of the bank in the business being carried on at Kansas City, Missouri. This is branch banking by the bank.

CONCLUSION.

It is, therefore, the opinion of this Department that, considering the above recited proceedings, described in the reports of the examinations of the affairs of the bank in question by the Federal Deposit Insurance Corporation, and

Honorable Harry G. Shaffner

transmitted by you to this Department, such as taking notes from borrowers of money from the agent-corporation, payable to the bank, taking notes for loans payable to the agent-corporation and delivered to the bank without endorsement by the agent-corporation, and the servicing of all notes which are negotiated by the agent-corporation, whether payable directly to the bank or to the agent-corporation and then transferred to the bank, being carried on by the safe deposit corporation, the agent-corporation, for the said bank at Kansas City, Missouri, a city other than the home city of the bank, and in consideration of the above cited and quoted authorities, such proceedings constitute branch banking.

Respectfully submitted,

GEORGE W. CROWLEY
Assistant Attorney General

APPROVED:

J. E. TAYLOR
Attorney General

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