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Review of Pennsylvania Legislation 1939 - Banking and Finance
Termination of Liability of Shareholders of Banks

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I. BANKING AND FINANCE\(^1\)

a. Termination of Liability of Shareholders of Banks

The Act of June 24, 1939,\(^{1a}\) amends Section 614 of Article VI of the Banking Code of May 15, 1933,\(^2\) as amended by the Act of April 24, 1935.\(^8\)

Section 614 of the Banking Code of 1933 provided that the liability of shareholders in banking institutions should be—

"As heretofore provided by law until termination in accordance with the provisions of this section. As to any deposit made, or claim arising, after the effective date of this act, shareholders now subject to statutory liability shall be liable to the extent of the percentage of the par value of their stock by which the surplus of the bank, the bank and trust company, or the trust company falls short of one hundred per centum of its capital. If, at the effective date of this act, the surplus of any such bank, bank and trust company, or trust company is, or at any time thereafter becomes, equal to the aggregate par value of its capital, the liability of shareholders for deposits and other claims against such bank, bank and trust company, or trust company shall cease and determine. Shareholders of banks, bank and trust companies, or trust companies, incorporated under this act, shall not be subject to any liability to the depositors or other creditors thereof."

The Act of 1935 amended this section by providing that the holders of preferred stock should not be individually responsible for any debts, contracts, or engagements of banking institutions, and should not be liable for assessments to restore impairments in the capital of such institutions. The liability of common stockholders was continued as set forth in the Banking Code, but it was provided that in order that the liability of such shareholders should cease the "unimpaired" surplus of the institution should equal the aggregate par value of the common capital of the institution.

The 1939 amendment adds the following provision:

"The liability of common shareholders for deposits and other claims against such bank, bank and trust company, or trust company shall cease and determine on July 1, 1941, or on any later date fixed for such termination, if such bank, bank and trust company on July 1, 1941, or on any later date fixed for such termination, exercises any of the powers conferred upon it by its articles of incorporation, provided that notice of such termination of liability shall have been given

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\(^{1}\)See also "Fiduciaries and Decedents' Estates," infra.
\(^{1a}\)P. L. 736, 7 PURD. STATS. (Pa.) § 819-614.
\(^2\)P. L. 624.
\(^3\)P. L. 56.
six months prior thereto, by advertisement in a manner similar to that prescribed by this act for the advertisement of intention to file articles of incorporation. Shareholders of banks, bank and trust companies, or trust companies, incorporated under this act, shall not be subject to any liability to the depositors or other creditors thereof."

The fifth section of the Act of May 13, 1876, provided in part as follows: "The shareholders of any corporation formed under this act, shall be individually responsible, equally and ratably, but not one for the other, for all contracts, debts, and engagements of such corporation to the amount of their stock therein, at the par value thereof, in addition to the par value of such shares."

The constitutionality of this provision was questioned in Gordon, Secretary of Banking v. Wendoroth, et al, wherein it was held that, since the principal incident of a corporation is the limited liability of stockholders, a statute imposing double liability should clearly indicate in its title the imposition of such liability. The Act of 1876 was accordingly held to be unconstitutional, on the ground that its title does not sufficiently give notice of the imposition of double liability upon the stockholders of insolvent banks. It was also intimated that it might be unconstitutional for the further reason that it might be deemed special class legislation, in view of the fact that such double liability is not imposed on stockholders of trust companies doing a banking business.

In the case above cited Judge McCann states: "It could hardly be argued that this title would be sufficient in the case of any other corporate group, because the body of this act, wherein double liability is fixed, is entirely at variance with the popular conception of a corporation. That this is the viewpoint of both the legal profession and the laymen is evidenced by the fact that the great majority of people who purchased bank stock never knew there was any claim of double liability, and it is not surprising that this question has not reached the appellate courts for the reason that there have been very few cases of bank insolvency in which this question could have been raised prior to the depression which occasioned the failure of many banks. That it is economically undesirable is evidenced by the fact that the legislatures, both National and State, under the new banking laws, have eliminated entirely the question of double liability."

It should be noted that the above statement is too broad, for it is apparent that the above quoted statutory provisions fall far short of entirely eliminating the question of double liability.

4 P. L. 161, 7 Purd. Stats. (Pa.) § 78.
In *Gordon, Secretary of Banking v. Winneberger*, it was held that the Act of 1876 did not apply to trust companies incorporated under the General Corporation Act of April 29, 1874, but the question of the constitutionality of the provision for double liability of stockholders in the Act of 1876 was not passed upon.

The constitutionality of the provision was attacked on the ground of insufficient notice in the title in several prior lower court cases. In *Jones' Estate*, the Orphans' Court of Lackawanna County held the title of the act sufficient. The court ordered a sum sufficient to meet the possible liability of the deceased stockholder set aside "to await further proceedings." It was also contended that the provision was unconstitutional for the further reason that it makes an arbitrary and unreasonable classification of financial institutions, since double liability does not attach to stockholders of trust companies. This objection was also rejected.

These questions are more fully discussed in *Gordon, Secretary of Banking, v. Dodge*. Judge Lark of Northumberland County held the title of the Act of 1876 sufficient, since the act was "substantially a reenactment of prior general legislation on the subject." He compared the provision in question to that making stockholders of certain companies individually liable to laborers for work done for the corporation, and such provision has been held constitutional though the Act of 1874 did not disclose such liability in its title.

In a later decision in the same case it was held that a stockholder's liability cannot be increased because some stockholders are insolvent and their shares of the funds needed to pay the debts of the bank cannot be collected.

The purpose of the Act of 1939 would appear to be to provide a method by which it can finally be settled as to whether the individual liability of the stockholders of a particular bank has "ceased and determined." A bank statement may show a surplus "equal to the aggregate par value of its common capital" but it may later be contended that the book value of its assets was in excess of their fair value and that the bank's stated surplus was therefore "impaired." Under this test it could not be positively stated that individual liability had ceased as to any particular bank. Now, after July 1, 1941, if six months prior thereto or any later date fixed by the bank, notice of termination of such liability is properly advertised, and the bank continues to operate thereafter, individual liability of common shareholders shall "cease and determine." Those having claims against banks, who have relied on the liability of their stockholders to assessment, are thus put on notice that they should collect their claims before July 1, 1941, if they have any doubt as to the continued solvency of the debtor bank.

In *Gordon v. Biesinger*, it was held that an action of assumpsit provides an

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6310 Pa. 362, 165 Atl. 408 (1933).
7P. L. 73, 15 PURD. STATS. (Pa.) 1.
11335 Pa. 1, 6 A. (2d) 425 (1939).
adequate remedy for the imposing of double liability on stockholders under the Act of 1876, and that the mere plurality of defendants does not require the assumption of jurisdiction by a court of equity. This case also holds that the secretary of banking, as receiver of a closed bank, now has the power to enforce double liability by assessment made by him, without recourse to any court for a decree authorizing such assessment.

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b. Pennsylvania Securities Act

The protection of investors has long occupied the legislative mind. Statutes, including those popularly known as "Blue Sky Laws," have been adopted to prevent the unwitting public from transforming good money into securities of questionable value. In Pennsylvania, the first such statute, enacted in 1923, was repealed and supplied by the Act of 1927, which was in turn replaced by the Pennsylvania Securities Act of 1939. The new Act substantially codifies the earlier ones, but makes certain additions and changes. Like its predecessors, it is based on the police power of the State and should withstand attacks on constitutional grounds.

The principal purpose of the Act is to protect the public from frauds, and to effectuate this, it provides a system for the registration of those who deal in or sell securities. It sets forth definitions, exemptions, penalties for violations, and the powers and duties of the Pennsylvania Securities Commission. Instead of requiring the registration of securities, it regulates their sale by the registration of dealers and salesmen. Instead of passing on the price or merits of a securities issue or on the expediency of particular plans of financing, it contemplates investigations to determine whether the securities are being offered to the public honestly and in good faith, without an intent to deceive or defraud.

"Security" is defined by Section 2 (a) in sufficiently broad and general terms to embrace, in addition to stocks and bonds, virtually all types of formal obligations, including, for example, certificates of deposit. The definition of a "sale for value" contained in Section 2 (b), which is derived principally from the Fed-

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1Act of June 14, 1923, P. L. 779.
2Act of April 13, 1927, P. L. 273, 70 PURD. STATS. § 1, et seq., as amended.
3Act of June 24, 1939, P. L. 748, 70 PURD. STATS. § 31, et seq.
5The 1923 Act was administered by the Commissioner of Banking, but Section 30 of the Act of 1927 created the Commission in substitution.