



STATE OF KANSAS

OFFICE OF THE ATTORNEY GENERAL

2ND FLOOR, KANSAS JUDICIAL CENTER, TOPEKA 66612

ROBERT T. STEPHAN  
ATTORNEY GENERAL

July 24, 1981

MAIN PHONE: (913) 296-2215  
CONSUMER PROTECTION: 296-3751  
ANTITRUST: 296-5299

ATTORNEY GENERAL OPINION NO. 81-177

Mr. Charles Rooney, Jr.  
State Banking Department  
Suite 600  
818 Kansas Avenue  
Topeka, Kansas 66612

Re: Banks and Banking -- State Banking Code --  
"Banking Business" Defined

Synopsis: Where a company that is regularly engaged in a wholesale business accepts money on deposit from its employees, such company is engaged in a banking business, as provided in K.S.A. 9-702. Accordingly, such company is subject to the requirements of the state banking code. Cited herein: K.S.A. 9-702.

\* \* \*

Dear Mr. Rooney:

As General Counsel for the State Bank Commissioner, you have requested our opinion as to whether a company situated in Kansas is engaged in the banking business without having complied with the requisites therefor prescribed in the state banking code. You indicate that your request is prompted by an inquiry from such company's attorney, and you have included a copy of the attorney's letter with your request.

The company's attorney indicates that his client is a "large company, engaging in the wholesale business," and he describes the situation giving rise to his inquiry, as follows:

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"A short time ago our client instituted a practice of borrowing money from its employees. The arrangement is a satisfactory one for both the employees and the company, since, the employees may obtain a higher rate of return than at a local financial institution and the company is able to obtain funds at lower interest rates. At the beginning, the transaction was handled by loan agreement allowing for pay back upon demand. For convenience, the company subsequently added a check-off policy, so that the employees could loan money to the company through a deduction from their check. The loans are all still demand loans. The rates of interest on the loans fluctuate and when the rates change the employees are notified."

As recognized by the company's attorney, a determination of whether the company is engaged in the banking business requires an interpretation of K.S.A. 9-702, which provides in pertinent part:

"Any individual, firm or corporation, except a national bank, who shall receive money on deposit, whether on certificates or subject to check, . . . shall be considered as doing a banking business, and shall be amenable to all the provisions of this act . . . ."

From the foregoing, it is apparent that a resolution of your inquiry depends on whether the company is receiving money on deposit within the meaning of K.S.A. 9-702. Since the company contends it is a borrower of moneys from its employees, rather than a depository for such moneys, it is necessary at the outset to distinguish between a "loan" and a "deposit." Before discussing this distinction, however, several prefatory observations are appropriate.

First, we are aware of no relevant Kansas case law to aid our determination, and a consideration of your request has necessitated resort to general authorities and cases from other jurisdictions. Second, it is apparent that a conclusion as to whether the company in question is unlawfully engaging in the banking business is a factual determination. However, the company's attorney has provided a rather summary statement of the facts for our review.

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Therefore, in light of these limitations, it is not possible here to provide you with a definitive opinion. Although our response will discuss what we perceive to be the relevant principles of law and apply them to the facts as presented, we suggest that you satisfy yourself as to the existence or absence of any additional pertinent facts before reaching a final conclusion as to the status of this company under our banking laws. With this caveat in mind, we shall consider first whether the moneys received by the company appear to be loans or deposits.

A definitional distinction between a "loan" and a "deposit" is difficult, at best. Although "loans and deposits are essentially dissimilar," the distinctions are technical and not always easily discernible. Zollner, 7 Banks and Banking §4823 (1936). "All attempted definitions recognize the close relation between the two and the difficulty of laying down a specific rule of distinction applicable to all cases." Commercial Banking & Trust Co. v. Doddridge County Bank, 119 W.Va. 449, 194 S.E. 619 (1937). In Elston, Prince, & McDade v. First State Bank of Plain Dealing, 196 La. App. 305, 140 So. 510 (1932), the court took judicial notice that loans and deposits are distinct and dissimilar transactions. 140 So. at 512. The court further stated:

"A loan is defined as a contract by which one delivers a sum of money to another and the latter agrees to return at a future time a sum equivalent to that which he borrowed. It is presumptively made upon interest. The contrary is true of a deposit, in that the depository must deliver the deposit on demand. A deposit is made primarily for the benefit of the depositor, while a loan is made for the benefit of the borrower." Id.

Similarly, in Schumacher v. Eastern Bank and Trust Co., 52 F.2d 925 (4th Cir. 1931), the issue considered was whether the trust company had loaned money to or deposited money in a bank. There, the court stated that, although "the legal effect of a deposit is a loan to the bank, so that the relation of debtor and creditor is created between the bank and the depositor . . . , there is this distinction between a loan and a deposit . . . : A loan is primarily for the benefit of the bank; a deposit is primarily for the benefit of the depositor. . . . A loan arises from the necessities of the borrowing bank; a deposit from the confidence of the depositor in

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its strength. A loan ordinarily is sought by the bank for its own purposes; a deposit is ordinarily made by the depositor for purposes of his own." Id. at 927.

It is clear from these authorities that the respective benefits to be derived by the parties to a transaction are to be considered in distinguishing the transaction as a loan or a deposit. In this instance, though, there would appear to be mutual benefit to the company and its employees. On the one hand, the company is able to obtain money from its employees to meet the company's necessities, apparently at rates of interest lower than the company could obtain from conventional financial institutions. Similarly, the employees benefit by earning interest on the money made available to the company at rates which are greater than could be obtained from financial institutions, and the apparent regularity with which such moneys are made available to the company would indicate the employees' confidence in the safety and strength of these transactions. The requirement that the moneys be repaid on demand also tends to the benefit of the employees.

From these facts, it is difficult to discern which party receives the predominant benefit, and we are unable to conclude as to the nature of the transaction on this basis. Thus, it is appropriate to consider the form of the transaction itself; and in our judgment, such analysis suggests that it is more appropriate to consider these transactions as deposits, rather than loans.

Even though the company's attorney indicates that the employees initially made money available to the company pursuant to "loan agreements," the company now obtains the money through employees' payroll deductions. Such fact is more indicative of a deposit transaction than it is a loan. In our judgment, the apparent frequency and regularity of moneys being placed with the company by its employees are more characteristic of an employees' savings plan than they are of a loan. Such conclusion is enhanced by the absence of a promissory note or other written contract evidencing the loan agreement, although we would assume that the employees have executed some type of authorization for the deduction of specified amounts from their wages.

Even if written "loan agreements" or "promissory notes" were still used to evidence the company's indebtedness to its employees, the name given to the transaction by the parties is not conclusive as to a determination of what the transaction is

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in fact. The substance of the transaction, rather than the way it is denominated, must control any such consideration. See, generally, Schumacher v. Eastern Bank and Trust Co., supra. In this connection it also is interesting to note the concluding provisions of K.S.A. 9-702 which state that "promissory notes issued for money received on deposit shall be held to be certificates of deposit for the purposes of this act." Thus, assuming that these transactions were still evidenced by "loan agreements" or "promissory notes," such instruments would be regarded as certificates of deposit under K.S.A. 9-702, if the transactions evidenced by these instruments are characterized as deposits rather than loans.

It also is pertinent to note that the principal of and interest on the moneys placed with the company are payable to the employees on demand. While such fact is not determinative of the issue, since both loans and deposits may be made "payable on demand," the demand aspect of these transactions is certainly consonant with a conclusion that the transactions provide for the depositing of the employees' money with the company.

Also, we do not think the company's indebtedness to its employees is persuasive to a finding that the employees have loaned money to the company. As indicated by the previously quoted excerpt from Schumacher v. Eastern Bank and Trust Co., supra, whether the employees' money is loaned to or deposited with the company, there is a debtor-creditor relationship created. Moreover, under either circumstance, the company has the use of the employees' money, which accomodates one of the company's apparent purposes for entering into the transactions.

Although we recognize the tenuous nature of any generalizations as to the circumstances attending the loaning of money, it is interesting to note that there would appear to be a disparity of bargaining power among the parties to these transactions, with the company assuming the superior position. In fact, the description by the company's attorney of the factual circumstances surrounding these transactions clearly indicates that the arrangement in question was "instituted" by the company and remains under the company's control. For example, from the statement of the company's attorney that the employees are notified of the fluctuation in the interest rate, it may fairly be assumed that the company has established the benchmark for determining the applicable rate. In such event, if it is assumed that the employees' money is loaned to the company, we believe it somewhat unusual that the "borrower" maintains this type of control over the transactions.

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All of these facts regarding the form of the transaction itself tend to support a conclusion that the company is receiving money on deposit. Based on that conclusion, we are of the opinion that the company is engaged in the business of banking within the meaning of K.S.A. 9-702.

In making this determination, we have recognized that the receiving of deposits is ancillary to the company's regular business. However, there is authority that a corporation engaged in another business may nonetheless be considered to be engaged in a banking business. The Wisconsin Supreme Court so held in MacLaren v. State, 141 Wis. 577, 124 N.W. 667 (1910). A department store which received money, issued pass books, paid interest on money deposited and paid principal, with interest thereon, on demand of the depositor was held to be engaged in a banking business, under a provision declaring the receiving of money on deposit as a regular business to be a banking business.

K.S.A. 9-702 which defines the business of banking is similar to the provision in MacLaren, but is much broader. As noted above, to be engaged in the banking business, the corporation in MacLaren had to be receiving money on deposit as a regular business. K.S.A. 9-702 is not similarly limited, which provides additional support to a conclusion that a corporation other than a bank or similar financial institution can be considered to be doing a banking business.

We also note that the transactions in question here are different in form, but not in substance from those in MacLaren. Employees of the subject company are not given pass books as evidence of a deposit; neither are they given promissory notes as evidence of indebtedness. However, like the depositors in MacLaren, the employees are entitled to be paid their principal and interest on demand. Thus, calling one transaction a "demand loan" and the other a "deposit" would not seem warranted where such distinction results in one company being deemed engaged in the business of banking and the other not.

It also could be argued that the department store in MacLaren was accepting money on deposit from the general public and as such may have been engaging in a banking business, while the Kansas company is accepting money only from its employees and, therefore, is not engaged in a banking business. That question was not addressed by the court in MacLaren. Other courts have mentioned the scope from which depositors are

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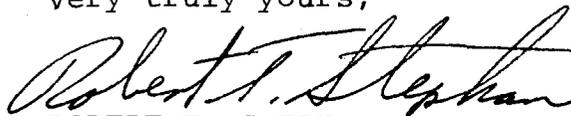
drawn as a factor in determining whether a person or corporation is engaged in banking. See Staunton Industrial Loan Corp. v. Commissioner of Internal Revenue, 120 F. 2d 930 (4th Cir., 1941); Rosenblum v. Anglim, 135 F.2d 512 (9th Cir., 1943); Martin v. St. Aloysius Church, 38 R.I. 339, 95 A. 768 (1915). However, in each of these cases, the operative definition of banking is clearly distinguishable from K.S.A. 9-702. Therefore, a similar result does not necessarily obtain.

We also note that K.S.A. 9-702 does not expressly limit its definition of engaging in the banking business to the receipt of money on deposit from the general public, and we can discern no other evidence of legislative intent that it be so restricted. With this in mind, and in light of the MacLaren decision, we do not believe that restricting the deposits of money to those received from the company's employees operates to avoid the definitional requirements of K.S.A. 9-702. In our judgment, if the company is accepting money on deposit, it is engaging in the banking business, as contemplated by this statute.

We believe this conclusion is consistent with the objectives of the legislature in establishing a scheme for the regulation of individuals, firms or corporations which receive money on deposit. "[I]nasmuch as it is necessary at all to resort to regulation, it must apply to all engaged in the transaction of the same kind of business under substantially similar conditions." MacLaren, supra, 124 N.W. at 669.

In summary, it is our opinion that, based on the facts presented, the company about which you have inquired is engaged in a banking business, as contemplated by K.S.A. 9-702. Even though such company is regularly engaged in a wholesale business, the described transactions between such company and its employees, in our judgment, constitute the company's receipt of money on deposit from its employees, thereby subjecting the company to the requirements of the state banking code. Again, however, we caution that our opinion is predicated on the facts presented with your request, and before any action is taken in reliance upon this opinion, you should satisfy yourself as to the existence or absence of additional facts that would alter the conclusions reached herein.

Very truly yours,



ROBERT T. STEPHAN  
Attorney General of Kansas



W. Robert Alderson  
First Deputy Attorney General