3815.

COUNTY COMMISSIONERS—DISCRETIONARY WHETHER THEY SHOULD EXERCISE TEN DAY ACCELERATION CLAUSE IN NOTES—NOT LIABLE IN ABSENCE OF GROSS ABUSE OF DISCRETION—MAY SET OFF THEIR OBLIGATIONS ON NOTES AND TERM BONDS AGAINST THEIR DEPOSITS WITH BANK—EXCEPTION NOTED.

SYLLABUS:

1. *It is a matter of discretion with the county commissioners as to whether they shall exercise the ten-day acceleration clause provided in the notes, in the exercise of which discretion they are liable only in the case of gross abuse of such discretion.*

2. *The county commissioners may treat their obligations on notes issued for a particular improvement, and sold to a bank, as a set-off against their deposits with said bank, when such bank is the legal holder of such notes when they become due, but they can not use such obligations as a set-off when such bank has sold them to a holder in due course.*

3. *The county commissioners may treat their obligations on term bonds issued for a particular improvement, and sold to a bank which later closed, as a set-off with said bank if such bank is the holder of such bonds when they become due, but the county commissioners can not use such obligations as a set-off as against the bank when such bonds shall have been sold to a holder in due course prior to maturity.*

COLUMBUS, OHIO, December 4, 1931.

HON. R. L. THOMAS, *Prosecuting Attorney, Youngstown, Ohio.*

DEAR SIR:—Your recent request for opinion, reads as follows:

"You are probably aware of the fact that three of the Youngstown Banks failed to open for business October 15, 1931. Since the closing of these banks, several questions have arisen regarding our depository bonds, which we are submitting to you for your opinion.

From one of these banks, Mahoning County had borrowed approximately $187,000.00 on county bearer notes containing a clause that the same might be redeemed upon ten days written notice. The notes, however, on their face are not due until the first of the year. $186,000.00 worth of notes held by the bank were turned over to the City of Youngstown as security to cover deposits made by the city and the city, in turn, after the closing of the bank, sold $150,000.00 worth of county notes to the State Teachers Retirement Fund, which is at present holding them.

The sureties on our depository bonds now raise the question as to whether or not the county, from the sale of bonds, should pay the notes at the present time or wait until the notes become due because of the possibility of the redemption of the notes by the liquidating agents before maturity.

From the foregoing, we would appreciate an opinion from you on the following questions:

1. Should the county exercise the right it has to redeem these

notes on ten days written notice or should the county wait until the notes become due before paying them?

2. May the County Commissioners treat their obligations on notes, issued for a particular improvement and sold to a bank, which later closed, as a set-off against their deposits with said bank?

3. May the County Commissioners treat their obligations on term bonds, issued for a particular improvement and sold to a bank, which later closed, as a set-off against their deposits with said bank?

The above questions, raised by the depository bonding companies must be answered before the bonding companies will reimburse the county for the funds at present in the closed institutions, and have placed Mahoning County in a position where it is unable to pay any of its obligations. For this reason, an early reply by you will be very much appreciated."

You state that Mahoning County issued certain notes in the face value of $187,000.00, payable to bearer, due January 1, 1932, but redeemable upon ten days notice. You further state that $186,000.00 worth of these notes, after having been sold to the bank, were turned over to the city, as security for deposits, and that the city, in turn, sold $150,000.00 worth of these county notes to the State Teachers' Retirement Fund, which is at present holding them.

The facts in this case must be construed in the light of the negotiable instrument law, by reason of the fact that these notes are payable to bearer. Section 8157, of the General Code, defines a holder in due course as follows:

"One is a holder in due course who has taken the instrument under the following conditions:

1. That it is complete and regular upon its face.

2. That he became the holder of it before it was overdue, and without notice that it previously had been dishonored, if such was the fact.

3. That he took it in good faith and for value.

4. That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it."

Section 8162 of the General Code, defines the rights of a holder in due course, as follows:

"A holder in due course holds the instrument free from any defect of title of prior parties, and free from defenses available to prior parties, among themselves, and may enforce payment of the instrument for its full amount against all parties liable thereon."

As to the notes in the principal sum of $150,000.00 sold to the State Teachers' Retirement Fund, said notes having been sold to such fund prior to the date of maturity, we must assume, from the facts stated in your letter, that these notes have not yet been declared due by means of the ten day notice provision stated in your letter. The State Teachers' Retirement Fund is clearly a holder in due course and being such, no right at set-off could be

pleaded as against such notes when they severally become due and payable, this defense being eliminated by virtue of Section 8162 of the General Code. In support of this contention, we call your attention to the case of *Scholl* v. *Sobray et al.,* 17 O. C. C., (N. S.) p. 44, the second branch of the syllabus of which case reads as follows:

> "A claim of a maker of a promissory note against the payee can not be set off against a holder of the note in due course."

While you do not state what became of the $36,000.00 worth of notes which were turned over to the city of Youngstown as security by the bank, if these notes are still held by the city the city would be a holder in due course to the extent of the unpaid deposits belonging to the city, and likewise all defenses of set-off between the county and the bank would be eliminated.

Referring specifically to your first question, as to whether the county commissioners should redeem these notes prior to maturity, you do not state whether or not the funds are now available to redeem these notes. Assuming that they are, it would be more a question of business policy than of law, to be determined by the county commissioners upon an analysis of the funds available and whether the loss of interest from the sinking fund would be equal to, or greater than the interest on the outstanding notes, taking into consideration the other advantages which the county might receive by the retention of the funds. Since there appears to be no provision in the statutes, requiring the county commissioners to anticipate the payment of these notes prior to maturity, this matter would be clearly within their discretion, however, if they should desire to use the notes still held by the bank as a set-off, or in the event that the banking department should pay to the city the remaining funds on deposit it might be of advantage to declare the notes due for the purpose of using them as a set-off, as hereinafter discussed.

In answer to your second question as to whether the county commissioners may treat their obligations on the notes as a set-off against deposits with the bank, Section 11319, General Code, defines "set-off" as follows:

> "A set-off is a cause of action existing in favor of a defendant against a plaintiff between whom a several judgment might be had in the action, and arising on contract or ascertained by the decision of a court. It can be pleaded only in an action founded on contract."
>
> Section 11321 of the General Code, reads as follows:
>
> "When cross-demands have existed between persons under such circumstances that if one had brought an action against the other a counterclaim or set-off could have been set up, neither can be deprived of the benefit thereof by assignment by the other, or by his death. The two demands must be deemed compensated so far as they equal each other."

Section 11241, General Code, in so far as material to the present inquiry, reads in part, as follows:

> "When a party asks that he may recover by virtue of an assignment, the right of set-off, counterclaim, and defense, as allowed by law, shall not be impaired."

Since these notes are not due until the first of the year the bank could not bring action or demand collection until after such date.

In the case of *Armstrong, Receiver* v. *Warner et al.,* 49 O. S., 376, the first paragraph of the syllabus reads as follows

> "When the holder of a claim not yet due, arising upon contract, becomes insolvent and transfers the same before maturity, and the debtor, at the time of the transfer, holds a similar claim then due against the assignor, his right of set-off is preserved against the assignee, when the latter's cause of action arises. And a surety on the obligation so transferred, may enforce the set-off for his own protection, if the principal debtor be insolvent. The rule does not apply where the thing transferred is commercial paper and the assignee becomes the bona fide holder thereof for value."

It is a well settled rule of law that the relation of the bank and its depositors is that of debtor and creditors and while certain protection has by statute been provided for public funds such as bonds securing such deposit, the relation of the bank to the county, city, state or other subdivisions remains that of debtor and creditor, and such depositors have no preference over other general creditors. See In re Liquidation of Osborn Bank, 1 App. Rep., 140; *Cook County National Bank* v. *United States,* 107 U. S., 445; *Fidelity & Casualty Company* v. *Union Savings Bank,* 29 App. Rep., 154.

It is therefore apparent that where the county is indebted to an insolvent bank which has been taken over by the state banking department for liquidation, when such bank is also indebted to the county commissioners by reason of deposits, such indebtedness of the county commissioners can be set off as against the liability of the county commissioners unless prohibited by a positive statute, which provision we do not find.

From your second and third inquiries, it is evident that there exists in your mind some distinction between a note and a bond. A note, as a negotiable instrument, is a definite promise to pay a certain sum of money at a definite or determinable future time. A negotiable bond is likewise a definite promise to pay a certain sum of money at a definite or determinable future time. The ordinary bond usually has attached thereto interest coupons which are likewise negotiable instruments, usually payable to bearer, and usually executed with more formality; however, in so far as we are able to determine, from an examination of decisions, there is no legal distinction between these two forms of negotiable instruments, that is, the liability on each one is the same.

Specifically answering your questions, it is my opinion:

1. It is a matter of discretion with the county commissioners as to whether they shall exercise the ten-day acceleration clause provided in the notes, in the exercise of which discretion they are liable only in the case of gross abuse of such discretion.

2. The county commissioners may treat their obligations on notes issued for a particular improvement, and sold to a bank, as a set-off against their deposits with said bank, when such bank is the legal holder of such notes when they become due, but they can not use such obligations as a set-off when such bank has sold them to a holder in due course.

3. The county commissioners may treat their obligations on term bonds issued for a particular improvement, and sold to a bank which later closed,

as a set-off with said bank if such bank is the holder of such bonds when they become due, but the county commissioners can not use such obligations as a set-off as against the bank when such bonds shall have been sold to a holder in due course prior to maturity.

Respectfully,
GILBERT BETTMAN,
Attorney General.

3816.

APPROVAL, NOTES OF CITY OF LIMA, ALLEN COUNTY, OHIO—$25,000.00.

COLUMBUS, OHIO, December 4, 1931.

Retirement Board, State Teachers Retirement System, Columbus, Ohio.

3817.

APPROVAL, NOTES OF CITY OF LIMA, ALLEN COUNTY, OHIO—$10,000.00.

COLUMBUS, OHIO, December 4, 1931.

Retirement Board, State Teachers Retirement System, Columbus, Ohio.

3818.

APPROVAL, NOTES OF CITY OF LIMA, ALLEN COUNTY, OHIO—$500,000.00.

COLUMBUS, OHIO, December 4, 1931.

Retirement Board, State Teachers Retirement System, Columbus, Ohio.