Republic of Palau v. Bank of Micronesia, 7 ROP Intrm. 275 (Tr. Div. 1999)

BANK OF PALAU,
Plaintiff,

vs.

BANK OF MICRONESIA CORP., et al.
Defendants.

MOYLAN'S INSURANCE UNDERWRITERS (PALAU), INC.,
Plaintiff,

v.

BANK OF MICRONESIA CORPORATION, et. al.
Defendants.

ISAO SINGEO
Plaintiff,

v.

BANK OF MICRONESIA CORPORATION, et. al.
Defendants.

NGCHESAR STATE GOV., Rep. by Governor Duane Hideo,
Plaintiff,

v.

BANK OF MICRONESIA, et. al.,
Defendants.

CIVIL ACTION NOS. 98-121, 98-206, 98 207, & 98-124 (Consolidated)

Supreme Court, Trial Division
Republic of Palau

Issued: February 8, 1999

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BEFORE: R. BARRIE MICHELSEN, Associate Justice.

INTRODUCTION

Ngchesar State, as a depositor of the Bank of Micronesia ("the Bank"), and Moylan's Insurance Underwriters (Palau), Inc. ("Moylan's"), in its capacity as lessor of the property used by the Bank, seek priority when the Bank's assets are distributed. Ngchesar State argues it has a common law priority because of its status as a state. It seeks a ruling that it receives all of its deposits before any other depositors are paid. Moylan's requests that rentals accruing after the Receiver was appointed be deemed a priority administrative expense, and that the reasonable rental amount be determined to be $1,760 per month.

⊥276 FACTS

The facts regarding the Ngchesar State claim may be stated simply. The State alleges it had $127,000 in State funds on deposit when the Bank failed in March 1998.

Moylan's claim is also straightforward. Moylan's and the Bank executed a written lease in September, 1992. The term of the Lease was for a period of ten years, with a Bank option to extend the term for an additional term of five years on the same terms and conditions.

The Bank first defaulted on rent in January, 1998. Moylan's took no action when that rent was not paid. On or about March 23, 1998, the Bank closed for business and has not reopened. Nonetheless, Moylan's still took no action pursuant to the lease. Subsequently, the Government of the Republic of Palau filed an action for injunctive relief against the Bank. The Court appointed a receiver by June 19, 1998.

Moylan's then filed an action to both evict the Bank from the premises on June 24, 1998 and to recover past rent. That action was stayed by the Court, and the case has been consolidated as part of the receivership.

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THE NATURE OF AN EQUITY RECEIVERSHIP

Article X, Section 5 of the Palau Constitution states in part: "The judicial power [of the Palau Supreme Court] shall extend to all matters in law and equity." The Appellate Division has said "This provision extends jurisdiction over any and all matters which traditionally require judicial resolution." *Becheserrak v. ROP*, 5 ROP Intrm. 63, 66 (1995).

Consequently, this Court "is a court of general equitable jurisdiction, and as such, has power to appoint receivers and make such orders in the receivership proceedings as the exigencies of the case may require." *Bassett v. Merchant's Trust Co.* , 161 A. 789 (Corm. 1932), reprinted in 82 A.L.R. 1223, 1225 (1933).

In exercising such jurisdiction, "it is a recognized principle of law that the [trial] court has broad powers and wide discretion to determine the appropriate relief in an equity receivership." *SEC v. Lincoln Thrift Ass'n* , 577 F.2d 600, 606 (9th Cir. 1978): *See also* , 13 Moore's Federal Practice 3rd ed., ¶ 66.07 [2](Court has "remarkably broad discretion" when supervising receivership).

CLAIM OF NGCHESAR

Ngchesar State claims a priority in the distribution of the assets of the Bank, based upon the common-law doctrine that the sovereign may assert a priority with respect to the assets of an insolvent debtor as against unsecured general creditors. *See* 42 Am Jur 2d *Insolvency* § 79 (1969).[1]

Ngchesar State relies on 1 PNC § 303 which provides that the "rules of common- ⊥277- law . . . as generally understood and applied in the United States, shall be the rules of decision in the courts of the Republic in applicable cases." However, the rule that Ngchesar State seeks to apply here is not "generally understood and applied in the United States," and therefore cannot constitute s "rule of decision" in this Court.

A quotation from the Virginia Supreme Court aptly sums up this area of American common law:

> In so far as the rule of English common law may be deemed to give the king a preference in the case of debts due him which have arisen from commercial or business transactions, it is so mixed up with the prerogative right of the king, which has no counterpart in our system of government, that it should got be deemed to have been adopted by the adoption by Virginia of the common law of

[1] Ngchesar State does not explain in what sense it is sovereign. The state government was created by the Palau Constitution. The Palau government is not a federation of states that have chosen to join a union. Rather, the vote on the Constitution was by direct vote. *Gibbons v. Salii*, 1 ROP Intrm. 333 (1986) (relating circumstances of enactment of Constitution). By comparison, the Constitution of the Federated States of Micronesia was ratified on a district-by-district basis. FSM Const. art. I, § 1. *See also* U.S. Const. art. VII (decision regarding ratification of the Constitution to be made by the States individually).

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England. The following cases from other jurisdictions support this view: *Fidelity & Deposit Co. v. Brucker* (ind. Sup.) 183 N. E. 668, ante, 166; *Maryland Casualty Co. v. Rainwater, Bank Comm.*, 173 Ark. 103, 291 S. W. 1003, 51 A.L.R. 1332; *North Carolina Corp. Comm. v. Citizens' Bank & Trust Col.* , 193 N. C. 513, 137 S. E. 587, 51 A.L.R. 1350; *Fidelity & Casualty Co. v. Union Sav. Bank Co.*, 119 Ohio St. 124, 162 N. E. 420; *State v. Carlyon* , 166 Wash. 498, 7 P. (2d) 572; *Lake Worth Inlet Dist. v. First Amer. B. & T. Co.* , 97 Fla. 174, 120 So. 316; *Denny, Banking Com'r v. Thompson* , 236 Ky. 714, 33 S. W. (2d) 670, 673, 674; *Campion v. Village of Graceville*, 181 Minn. 446, 232 N. W. 917; *People v. Home State Bank*, 338 Ill. 179, 170 N. E. 205.

This conclusion efficiently disposes of the appellant's claim to a preference; but there are several other contentions of the appellant to which we shall briefly address our consideration.

In our rather extensive examination of the English precedents and authorities we have found no authority which even intimates that at the time of the American Revolution any political subdivision of the kingdom or body politic was regarded as being entitled under the common law of England to have its debts preferred. *United States Fidelity & Guaranty Co. v. Carter* , 170 S. E. 764 (Va. 1933), reprinted in 90 A.L.R. 191, 206 (1934).

Because there is no one accepted common law rule affording preferences to state governments in insolvency proceedings in the United States, and because the Restatement of Laws does not address the issue, this court is not bound by the original English common law rule. Rather, it feels free to conclude, as did the Colorado Supreme Court, that "the better rule seems to be that in the absence of statute or a showing of facts sufficient to create a trust, a claim for public money has no preference over the claims of the ⊥278 general creditors of a bank, but stands on the same footing with them." *Board of County Com'rs v. McFerson* , 9 P.2d 614, 615 (Col. 1932).

The general principle of equity is that the remaining assets of an insolvent bank are to be distributed pro rata among its general creditors. *See* 11 Am Jur 2d *Banks and Financial Institutions* § 1142 (1997). It is not unfair to apply that rule in this case. As the Attorney General has noted in his brief:

Unlike the pre-depression era cases it cites, Ngchesar State in this case had the option of depositing its funds in an FDIC -insured bank. Ngchesar State currently has funds in FDIC- insured banks, and in fact, had deposited funds in FDIC-insured institutions before it decided to use BOM, and before BOM became insolvent. *See* Public Auditor's Audit Reports of Ngchesar State Government for Years Ended September 30, 1994 and 1993, at p. 9 (stating that the State's cash was maintained in an FDIC-insured bank); and Audit Reports for Years Ended September 30, 1996 and 1995, at 8-9 (stating that the State's cash was maintained in three banks, two of which are FDIC-insured). For some reason -perhaps to get

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a higher interest rate -- the State knowingly risked substantial funds in the uninsured BOM. [Footnote included in text].

For these reasons, the request of Ngchesar State for a preference is denied.

CLAIM OF MOYLAN'S

Moylan's moves the Court for an order requiring that rentals for the commercial space subject to the Lease be established as a priority administrative expense over the claims of other general unsecured creditors of the Bank.

This request will be granted from June 24, 1998, the date Moylan's instituted suit. However, as a matter of equity, Moylan's costs will be paid last among administrative expenses. Moylan's is not without blame for its current predicament. It quietly allowed a bank to fall months in arrears without taking any action that would have warned the public of the bank's financial distress, and cut its own financial exposure. Fair rental for the premises will be deemed $1,760 per month, computed on a per diem basis from June 24, 1998 to the date the premises was vacated by the receiver.