STATE OF MAINE.

REPORT

OF THE

ATTORNEY - GENERAL

FOR THE TWO YEARS ENDING

NOVEMBER 30, 1904.

AUGUSTA
KENNEBEC JOURNAL PRINT
1905

they can enter legally upon the duties required of them by the agreement.

Second: That the application and agreement therewith do not infringe upon the insurance laws of this State relating to rebates.

October 2, 1903.

NEW ENGLAND REAL ESTATE AND TITLE COMPANY.

The methods employed by said company in carrying on its business are repugnant to the law relating to Loan and Building Associations. The purposes set forth in the charter of said company do not permit the corporation to carry on the business indicated by its contracts.

Hon. F. E. Timberlake, State Bank Examiner, Augusta, Me.:

Dear Sir:—In answer to your letter under date of September 22, 1903, calling my attention to the business which the New England Real Estate and Title Company, located at Bangor, is doing, and asking my opinion as to whether or not the business as carried on by said company conflicts with the law relating to loan and building associations of this State and the requirements of said law, I submit the following opinion:

The New England Real Estate and Title Company was organized under the general laws of this State in April, 1903, and by its purposes set forth, purports to carry on a real estate business. The purposes as set out in the certificate of said company are within the laws of the State. The real question is whether or not said company in carrying on its business is exceeding its authority and rights under its certificate of organization, and conflicting with the law relating to loan and building associations.

To fully decide this question it is important, first, to review briefly the kind of business which said corporation is doing. From the certificate of incorporation nothing can be gathered as to what kind of business the company is doing, but by its circular and contract we find that it is doing business on the installment plan and collecting moneys for the purpose of securing homes for its patrons. It issues contracts for the deposit of money in installments by the covenantee.

(1) This contract, under the first paragraph, provides that the covenantee shall pay the sum of $4 for every $1,000 of the contract on the execution of the same, which said sum of $4 is paid to the use of the company. The contratee is to pay a further sum of $1 per month for commissions and for services to be rendered during the life of the contract, by the company. The covenantee pays the further sum of $2 per month on each $1,000 of the contract until the property agreed upon by the covenantee and the company shall be bought for the covenantee. After the purchase of the property desired by the covenantee, then a sum of $8 per month on each $1,000 is to be paid by the covenantee to the company until the total amount of payments shall be equal to the cost or purchase price of the property bought. When the property is purchased the company receives title to the same and on full payment being made for it by the covenantee, the company then executes a sufficient deed to the covenantee or his heirs, executors or assigns.

Under this paragraph the covenantee first pays $4 on the signing of the contract, and thereafterwards, so long as the contract continues, $1 per month for commissions and services to the company. He is also bound to pay $2 per month to be applied to the purchase price of the property when it shall be secured for him. This glaring inadequacy of the charges for services and commissions might well startle one as a business proposition. The covenantee is required to pay $12 per year for the right to deposit without interest $24 per year until the contract matures, and at least $96 per year after maturity, assuming that the contract is for $1,000.

(2) Under the second paragraph of the contract, among other things it is provided that if the title and price of the property to be bought is found to be satisfactory to both parties; that is, to the company and the covenantee, then the company shall buy such property at such price and upon such terms as it may agree upon with the owner, provided that the total cost shall not exceed the face value of the contract.

As pointed out in this paragraph, the property to be purchased is to be purchased on such terms as may be agreed upon between the company and the owner of the property. This provision cuts out the covenantee, who is interested because his money is at stake, from the exercise of his judgment as to the amount

to be paid for the property. The company may purchase a piece of property below the face of the contract and turn it over at a price equivalent to the face of the contract. This on its face is pernicious and opens a broad door for fraud.

(3) Under paragraph three the contract provides that if the company shall fail through its own fault to purchase said property within sixteen months, the covenantee shall have the option to revoke his contract and thereupon shall receive from the company the amount paid in by him on the contract, and surrender the contract. And, further, in case the company fails to purchase such property for thirty-two months after the sixteen months aforesaid, then the covenantee shall receive, as liquidated damages, an amount equal to all the sums paid by him to the company, together with three per cent compound interest thereon computed from each semi-annual accumulation thereof, from the time such payments commenced to the expiration of the thirty-two months aforesaid; provided, however, that the covenantee shall continue to perform on his part all the conditions of the contract.

Hence, if the company shall fail to purchase the property desired by the covenantee within sixteen months from the date of the contract, then the covenantee has the power to revoke the contract and to receive from the company the amount paid in on the contract. The company may refuse to carry out the contract and in such case the covenantee may receive back what he has paid in, but without interest. This is plainly a hardship on the covenantee. And, further, if the company refuses for thirty-two months after the expiration of the sixteen months to carry out the contract, then the covenantee may recover liquidated damages equal to the entire sum paid in by him, together with three per cent interest, compounded, provided, however, that the covenantee shall continue to perform his part of the contract; that is, the company may refuse to perform its part of the contract, but the covenantee, to recover back anything of the sum which he has paid in, must continue to perform his part of the contract and in the end receive what he has paid in with three per cent compound interest. Even if there were no dangers surrounding such contract, yet the covenantee would get only his money back with three per cent interest, being less than that which the banks pay, and having no security whatever during

the four years that his money will ever be paid. Besides, the company can cut off all interest by payment of the amount paid in any day before the close of the thirty-two months.

(4) Paragraph four of the contract provides that if the covenantee shall fail to make the payments as aforesaid, before the maturity of his contract, then the company shall have the option to declare the contract void and all the previous payments forfeited, time being the essence thereof. This provision is somewhat modified in case of sickness, loss of employment or other misfortune, when the company will give the covenantee three months additional time, or such time as may seem prudent to the company, in which to pay up arrearages. Said paragraph further provides that in case the covenantee fails to make the required payments after maturity, that is, after the purchase of the property by the company, which is designated as the time of maturity, then such failure shall operate as an assignment of the covenantee's equitable rights in such property, and shall pass to and vest in the company all of his equitable rights in such property without further process. This provision is modified by giving the covenantee the right to assign his equitable interest, but with the consent of the company only.

The provisions of this paragraph are thoroughly detrimental to the covenantee, because if he fails to continue his payments then the company has the power to declare the contract void and all payments made thereon forfeited. To be sure this is modified in case of sickness, etc., but why should the covenantee forfeit everything which he has paid to the company in case he fails to keep up his payments, particularly when the company has received the initial fee of $4 and also excessive monthly payments for commissions and services? The unfortunate covenantee under this provision has little protection if he fails to meet the regular monthly payments. After maturity the provision is still stronger against the covenantee, if possible, for if he fails to meet his payments then such failure operates as an assignment of all his equitable rights and vests his equitable title in the company without further process. To be sure this provision is qualified somewhat by giving the covenantee the right to assign his contract with the written consent of the company, but what does this right amount to when taken in connection with paragraph "five" which provides as follows: "But no assignment

of this contract shall be valid if made while payments are due and unpaid"? I can hardly conceive of a more ingenious method to secure the property of others without adequate compensation than is set forth in these paragraphs.

(5) Paragraph six provides that the title to all property bought under said contract shall be taken in the name of the company, but that the equitable ownership thereof shall be in the holders of the unmatured contracts pending payment of the same by the covenantee in possession. There is also the further provision that the lien herein created by the holders of unmatured contracts on all such real estate shall be dissolved upon the failure to perform the contract by the holder thereof or his successor. What, then, becomes of the property? It is released from all lien claims and as the company holds the title, it becomes absolutely the property of the company.

At no time, as appears from this paragraph, does the covenantee hold any record interest or title in the property whatsoever until the contract is completed. And besides, provision is made that all of the covenantees shall have a lien claim upon all property so bought by the company. In other words, although a covenantee may have nearly paid for his property, yet until payment is completely made and the title has been passed over to him from the company, all the other covenantees have a claim upon it, and in case of the insolvency of the corporation the covenantee who has nearly paid for his house and premises will be required to divide the same with all of the covenantees in possession, according to their interest.

(6) Paragraph nine provides that the covenantee shall keep his life insured in a sum equal to the face of his contract, and in case of his failure so to do he thereby forfeits the contract and all sums paid thereon.

The covenantee may have nearly paid for his property and yet under this provision, if he allows his life insurance to lapse, all the moneys paid in on the contract are forfeited.

Following the contract form appears an explanation thereof, one paragraph of which is important, relating to the purchase of property, wherein it provides that "such purchase to be made at such time after the contract is dated as the covenantee's turn shall be reached in the order of his contract. Meantime from the beginning of the contract the covenantee agrees to make

certain payments to the company to secure its services in his behalf."

These various provisions have been selected from the contract and the explanatory addition to show the method of the New England Real Estate and Title Company in pursuing its business. The provisions are so thoroughly hostile to the interest of the covenantee that little or no protection is left him. Taking them all together they amount to little less than the taking of the covenantee by the throat and requiring him to forfeit his property in case he is not able to keep up the payments or seeks to release himself from his contract.

Having considered the provisions of the contract under which the New England Real Estate and Title Company is doing business, the question naturally arises, do they or any of them conflict with the law of this State relating to loan and building associations?

Section 1 of chapter 79, Public Laws of 1891, reads as follows: "Except as hereinafter provided, no person, association or corporation shall carry on the business of accumulating the savings of its members and loaning to them such accumulations in the manner of loan and building associations within this State unless incorporated under the laws thereof for such purpose."

The gist of this section is the accumulation of the savings and the loaning to its members such accumulations in the manner of loan and building associations within this State.

First. No question can be raised but that the New England Real Estate and Title Company is accumulating the savings of its members, for it specifically provides therefor in the payment of $2 per month until the contract matures and $8 per month thereafterwards. This point does not require further consideration.

Second. Does the New England Real Estate and Title Company loan such accumulations to its members or are its methods of operating equivalent to a loan of its accumulations to its members?

Evidently the authors of the contract have sought to escape this provision. At least the wording of the contract would seem to indicate that particular care had been taken to escape it if possible. While on its face the contract does not purport to make loans direct to its members, nevertheless the whole method

is equivalent to a loan. In the ordinary loan and building association a member mortgages his property to the association and the association furnishes him with cash. The title to the property is in the loan and building association and the equitable record title in the mortgagor, and eventually, to protect his equity, the mortgagor must pay the mortgage.

The New England Real Estate and Title Company in a sense turns the thing about. The title to the property purchased is taken by the company and it advances the purchase price to the seller, and, as set out in the contract, the covenantee holds the equitable ownership but no record title. The payment by the company of the purchase price of the property to the seller, and the holding of the covenantee under his contract to pay the same to the company, is equivalent to a loan to the covenantee direct. So that the situation as to the covenantee and the company is quite similar to that between the loan and building association and the party who mortgages his property, except that in the last case the mortgagor has a record title although only equitable, while in the case of the covenantee with the New England Real Estate and Title Company he has apparently no record title whatever but simply pays in his money to the corporation without security until he has paid for his property.

There is no question, then, but that under these two provisions of the contract of the New England Real Estate and Title Company said company is endeavoring in a roundabout way in some respects to carry on the business of accumulating the savings of its members and loaning them such accumulations in the manner of loan and building associations.

Third. If an association desires to accumulate the savings of its members and to loan to them such accumulations in the manner of loan and building associations, then it must become incorporated under the laws of this State for such purpose, and the words "incorporated under the laws of this State" as used here mean incorporation under chapter 47, Revised Statutes, and public laws additional thereto and amendatory thereof.

Fourth. The New England Real Estate and Title Company does not fall within the exceptions stated. These so-styled home buying associations regardless of the actual name under which they operate, have become numerous and their methods of operating are not new to this State. We find the same points raised

in this case to have been raised in other states and to have been adjudicated upon. The methods are very similar, the difference, if any, being as to details. The central point with all is the accumulation of the savings or funds of its members and the purported use of it to purchase or secure homes for them. If companies doing business according to the methods of the New England Real Estate and Title Company are successful and do not meet very shortly with disaster, then it is for one reason only, viz.: that so many members drop out and forfeit their hard earned money to the company that the few who remain are able to profit thereby. In other words, it is a business which flourishes mainly on the misfortunes of others.

The proposition as set out in its explanatory note, that each member shall take his turn according to the order of his contract for the purchase of a home when sufficient funds accumulate in the company for that purpose, is simply preposterous when a large number have become parties to the company's contract. The man signing the one hundredth contract cannot obtain a home for many years, and during the waiting period he must continue to deposit his hard-earned money without interest and without any protection or security whatever further than the word of the company, at the same time paying excessive rates for the privilege of depositing his money with the company.

This very question has been discussed in Shaw v. Interstate Savings Loan and Trust Company, 8 Ohio, also in Nebraska v. Nebraska Home Company. And as a matter of fact the very points involved in this case have been decided in very many states as insecure and dangerous to the depositors.

In U. S. v. McDonald, 59 Fed. Rep. 563, Judge Grosscup said in relation to one of these companies: "This is plunder of the public. It is said that this has been fairly done. * * * Two elements are essential to an investment—profit and security. What equality of profit do these companies offer? What security do they offer to the holders of unmatured contracts who are required to make a deposit each month? * * * The naked promise of an unincorporated and non-capitalized company do not constitute securities." The same is true whether the association is incorporated or not in this State, unless incorporated under chapter 47 of the Revised Statutes.

In U. S. v. Fulkerson, 74 Fed. Rep., 629, the court says in relation to such companies: "An act or contract though not originating in an evil design, yet tending to deceive and mislead, or violate private confidence, is a constructive fraud, equally reprehensible with actual fraud and prohibited by law."

In Shaw v. Interstate Savings Loan and Trust Company, 8 Ohio, the court says: "Experience has demonstrated one inevitable result to all such enterprises, viz., that there comes a time that the influx of credulous people to these societies ceases, and as the money paid out to the lucky members has been wholly and grossly out of proportion to their contributions or investments, or to the mutual earnings of such contributions and investments, these societies necessarily collapse leaving the unlucky members to bear the losses * * *."

All such contracts are unlawful because of the discrimination which results between the various contractees who deposit their money with the company. Only a few, comparatively, can protect themselves, and this must be done invariably to the loss of the other contractees.

My decision in the matter, therefore, must be that said New England Real Estate and Title Company is carrying on a business contrary to the provisions of section 1 of chapter 79 of the Public Laws of 1891 in that it is not properly incorporated for that purpose, and that the purposes set out in the charter of organization of said company do not permit it to carry on such a business as indicated by its contracts.

October 17, 1903.