

IN THE  
**Supreme Court of Tennessee,**  
AT NASHVILLE

*In re:* SENTINEL TRUST COMPANY

) Supreme Court No.  
) M2005-00031-SC-R11-CV  
)  
)  
) Court of Appeals No.  
) M2005-00031-COA-R3-CV  
)  
)  
) Lewis Equity No. 4781  
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**APPELLANTS' APPLICATION  
FOR PERMISSION TO APPEAL**

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The above-named Appellants in the Court of Appeals (herein, "Sentinel," the individual appellants being the members of Sentinel's board of directors), respectfully make application to the Court, under Rule 11, T.R.App.P., for permission to appeal the judgment of the Court of Appeals affirming the final judgment approving the transfer of Sentinel Company's performing trust accounts to SunTrust Bank.

**Note:** For the reader's convenience, parts of this Application are verbatim copies from the Application in the appeal arising from proceedings upon *certiorari*, No. M2005-01073-SC-R11-CV and original paragraphs herein are begun in bold type and full capital letters.

**I—THE JUDGMENT OF THE COURT OF APPEALS**

The opinion and judgment of the Court of Appeals were rendered December 29, 2005, and no petition for rehearing was filed. A copy of the judgment is appended hereto.

## II—QUESTIONS PRESENTED FOR REVIEW

1. Whether the courts below erred in refusing to apply the law of statutory construction to determine if the face of a Tennessee Banking Act section empowering the Commissioner of Financial Institutions to seize a “state bank,” under restricted circumstances, empowers him as well to seize a “state trust company,” under claim that it is insolvent when (i) no language within the Act literally authorizes the seizure of a state trust company under *any* circumstances, (ii) the Act expressly defines both types of institutions by mutually-exclusive definitions, (iii) the Act provides completely different remedies for the insolvency of a bank and the insolvency of a trust company, and (iv) it is impossible that the circumstances that empower the commissioner to seize a state bank without prior due-process hearing *could ever occur* with regard to a non-bank state trust company.

2. **UNDER A STATUTE** that empowers the Commissioner of Financial Institutions to seize a “state bank,” under restricted circumstances, and does not requires any litigation, but vests the local trial court with authority only to give specific approval or disapproval to listed decisions previously made by the Commissioner, whether all decisions of the trial court,<sup>1</sup> before its entry of final judgment, were invalid under Tennessee law holding that when any statute gives a trial court jurisdiction to make only limited decisions, any decision not within those limits is void for lack of subject-matter jurisdiction, as the rule was expressed and applied in *Brown v. Brown*, 198 Tenn. 600; 281 S.W.2d 492 (1955) and in *City of Bluff City v. Morrell*, 764 S.W.2d 200 (Tenn., 1988).

3. **UNDER THE CIRCUMSTANCES** that the sole basis of a trial court’s alleged jurisdiction was the statutory power of the Commissioner of Financial Institutions to seize a “state bank” when it has become insolvent, and the Commissioner, upon his own claim of authority, seized a “state trust

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<sup>1</sup>As not being among the listed approval/disapproval orders such a local Court is authorized to make by the Tennessee Banking Act in bank-seizure cases, including such as approving the payment of receivership administration costs, and approving disbursements to bond holders.

company” that in fact was not insolvent, and in recognition of the legal principles that a trustee’s insolvency does not empower a court involved in its liquidation, whether a state court or a federal bankruptcy court, to deal with or use the monies an insolvent trustee holds in trust, *Caplin, Trustee, v. Marine Midland Grace Trust Co.*, 406 U.S. 416, 92 S.Ct. 1678, 32 L.Ed.2d 195 (1972), and *Wagner, Trustee v. Citizens’ Bank & Trust Co.*, 122 Tenn. 164, 122 S.W. 245 (1909), made a specific rule by enactment that “*Trust property is not subject to the personal obligations of the trustee, even if the trustee becomes insolvent or bankrupt . . .*” Tennessee Uniform Trust Code, Public Acts of 2004, Chapter 537, Section 46, whether, after the Commissioner has unsuccessfully solicited bids for the business of all of Sentinel Trust Company’s trust accounts, the trial court is empowered to approve the Commissioner’s agreement to make a gratuitous transfer to a non-bidding bank, by “cherry-picking” a selection of Sentinel’s valuable trust accounts to a non-bidding bank, and not transferring three remaining trust accounts in default and undergoing liquidation.

4. Whether the courts below erred in failing to hold particular parts of the Tennessee Banking Act, as amended, unconstitutional on its face as attempting to vest in an executive officer, the Commissioner of Financial Institutions, certain powers which may be vested only in the judiciary, including the judicial power to appoint receivers, the judicial power to remove corporate directors, and the judicial power to bring about the dissolution of a corporation for insolvency, as well as the legislative power to make provisions of the Tennessee Banking Act applicable or inapplicable to non-banking corporations, at his pleasure.

### **III—THE RELEVANT FACTS**

**THIS CASE INVOLVES ACTIONS** by the Tennessee Commissioner of Financial Institutions in seizing—and thereafter proceeding with attempted administration and liquidation of a non-depository Tennessee Trust Company—claiming to act solely under the authority of a statute authorizing him, under stated conditions, to seize a “state bank” with no statutory language

purporting to authorize him to seize a “state trust company,” such as the leading appellant herein, Sentinel Trust Company.

Because of differences in the risks of the banking business and the trust company business, every bank is always subject to the risk of sudden insolvency which can result in a “run” on the bank, in which case the bank’s future receipt of income to cover checks will end —except for the inadequate amounts that will trickle in during liquidation of its loans—leaving its unsecured “depositors” the biggest losers except, in modern times, to the limited extent that they are protected by Federal Deposit Insurance. On the other hand, if a trust company becomes short of cash, this will cause no such emergency, because the trust company will continue to receive each year the large sums the indenture-settlors are obligated to pay, and a trust company can safely operate a trust business *without any assets* as long as its (or its owner’s) credit will enable it to borrow operating expenses from its owners or banks.

The legal setting of this dispute is that from the beginning, the Commissioner and his predecessor office, originally within the former Department of Insurance and Banking, had no authority over trust companies, but only banks. In 1980, a Banking Act (T.C.A. Title 45, Chapters 1 and 2) amendment first gave the Department regulatory authority over some trust companies,<sup>2</sup> but only those formed thereafter with the required Commissioner-approved charter. Then in 1999, all previously-grandfathered trust companies (including Sentinel) were first subjected to Departmental authority. The amendatory act, *inter alia*, subjected *all* trust companies to both chapters of the Banking Act and to the Commissioner’s regulatory authority, it contained some provisions<sup>3</sup> applicable only to banks, others applicable only to trust companies, and six sections applicable equally to trust companies and to banks *with fiduciary powers*. It also empowered the Commissioner to exercise *one* of his bank-control powers (but not the bank-seizure powers) over newly-regulated

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<sup>2</sup>And provided some rules regarding their operation.

<sup>3</sup>The pre-1999 amended Banking Act also contained some provisions in each of these three categories.

trust companies for only a limited 3-year period, which expired June 30, 2002, before the Commissioner seized Sentinel.

**IN BRIEF SUMMARY**, provisions of the law authorizing the Commissioner to seize a “state bank” authorized the Commissioner, by his own authority, to seize the bank to prevent “serious losses to its *depositors*,” it empowers him to operate the bank and to appoint a receiver to operate or liquidate it, empowers him to borrow needed moneys for such operation from a Federal Reserve Bank, empowers him to use the “state bank’s” own assets and the moneys borrowed from the Federal Reserve Bank to pay his employees and all expenses of operation, and gives him first priority on the bank’s assets, after liquidation, to pay all his fees, expenses and Federal Reserve Bank loan repayment above those paid from the bank’s own assets for these purposes.

**AFTER THE COMMISSIONER** shall have selected a local circuit or chancery court, the chosen court is empowered to approve a list of his decisions, including such actions as paying bank debts or settling claims against the bank for amounts above \$500.00, approving his final settlement, and reviewing appeals from the commissioner’s decisions to disallow creditors’ claims against the bank’s assets. The statute contains no provision empowering the local court to approve or disapprove payments to his employees, lawyers, and other administrative expenses, or payments to trust beneficiaries or other actions required to administer any funds the “state bank” may have held in trust if the bank had been granted the power to perform fiduciary functions.

**WITH THE RECORD** in the local court not including the Commissioner’s administrative record, the only relevant record evidence consists of filings by Sentinel and its directors, including a copy of its sworn Petition for *Certiorari* with supporting affidavits and exhibits and original affidavits filed in opposition to the Commissioner’s motion to approve transfer of all of Sentinel’s profitable trust accounts, which were excuted by Sentinel’s controlling stockholder Danny Bates, and by its expert witness, a C.P.A. who is president of the Tennessee Association of Certified Public Accountants.

**SENTINEL'S DIFFICULTIES** grew out of over 60 of its bond-issuers operating health-care businesses becoming insolvent and defaulting on their bond-payment obligations beginning 1998-1999.

During the period of 1998 until just before Sentinel's seizure in 2004, Sentinel credited each of the defaulted trust accounts with its monthly pro-rata share of interest earnings on a pooled fund<sup>4</sup> each month, but under Sentinel's schedule of fees and charges, each overdraft of each bond-issuer in default (effectively the same as a loan by the pooled fund) incurred liability to the fund for interest at the rate of 1½% a month, compounded monthly, pending Sentinel's liquidation of that issuer's assets. Sentinel had no interest in nor expectation of income from such interest-earning. The interest-compounding at this high rate would be a multiple of the moneys "borrowed" from the pooled fund.<sup>5</sup> Each such accrual of entitlement to daily interest received from SunTrust Bank and charging of interest on overdrafts was at all times automatically computed each month on Sentinel's computer accounting systems by whether the account had a positive or negative balance.

*Additional relevant facts* established by affidavits in the record include the following:

- During the period from the commencement of the health-care bond issuers' insolvency until Sentinel's 2004 Seizure by the Commissioner, Sentinel successfully completed 50 of the 63 issuers' collateral liquidations, in many of which the accounts-receivable (overdrafts plus compounded interest) exceeded \$1 million. In each of the 50, there was a full recovery of the total receivables, including interest, all of which was deposited into the pooled trust account, with the remaining balance pro-rated among bond-holders.
- It was proven by affidavit of the President of the Tennessee Association of Certified Public

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<sup>4</sup>All payments Sentinel received throughout every year from bond-issuers under their indenture obligations was deposited in this single checking account at SunTrust Bank in Nashville, from which Sentinel semi-annually disbursed required distributions to its bondholders.

<sup>5</sup>This caused the interest debts of many bond-issuer's to mount to between double and quadruple the money "borrowed," depending upon the number of months until payment.

Accountants, having both long experience and an impressive record of service to the judiciary that, considering the documentation before the Commissioner at the time of seizure, there was no way Sentinel could be determined to be insolvent before seizure; that it would not be possible to determine whether Sentinel would end up prosperous or insolvent until its completion of all liquidations; that the effect of the interest-compounding on indebtedness originating in overdrafts was to multiply the total receivable, as summarized above; that Sentinel's controlling-owner Bates was correct in the methodology of his determination that the amount of moneys actually used in liquidation work was less than half the total owed by all defaulted bond-issuers; that his methodology was correct in showing that the Commissioner's receiver's post-seizure collections through liquidation was sufficient to overcome any deficiency in the pooled trust fund; and Mr. Bates' testimony on the method of recording interest credits and compound-interest charges in Sentinel's pooled trust funds and the fact that it was faithfully followed, could absolutely be either confirmed or refuted by brief examination of Sentinel's computer records in the Commissioner's exclusive control, by any person having competent knowledge of such computer systems.

- At the time of its seizure, Sentinel had over about \$2 million in assets, had the credit to borrow large sums of money (including a Nashville bank's written commitment to lend Sentinel \$1 million on conditions acceptable to Sentinel, but whose amount the Commissioner deemed inadequate to delay seizure and liquidation), and had millions dollars worth of future profits on its books subject only to its continued competent performance of its trustee obligations.
- **THE COMMISSIONER PRESENTED** to the Court an application to transfer its performing bond issues (not in default) to a bank, essentially for no consideration other than monies that could be derived from the bond funds, which resulted in a final judgment of approval. During this period of administration, the Commissioner's receiver liquidated the collateral of all defaulted bond issues but three for amounts totaling in the millions of dollars

and sufficient to overcome negatives in the pooled bond fund if the Commissioner had applied Sentinel's regular schedule of fees and charges by paying the required amounts into the pooled bond fund at SunTrust Bank in Nashville.

#### IV—REASONS SUPPORTING THIS COURT'S REVIEW

1. The Attorney-General throughout insisted that actual statutory phrase "state bank" should be read as "state bank or state trust company" on the basis of one isolated phrase<sup>6</sup> of the statute, and this insistence was accepted and followed by the Court below, despite this Court's determination<sup>7</sup> that reasoning from a single isolated provision of a statute is not an application of the law of statutory construction.

2. **WITH THERE BEING** no litigation filed in the court below, the Court refused to accept and follow, as binding Tennessee law, the rule that its special jurisdiction (if any) was limited to the bank-seizure statute's listed decisions by the Commissioner that the Court was empowered to approve or disapprove, and that decisions not included in such statutory authorization were beyond its subject-matter jurisdiction under *City of Bluff City v. Morrell*, 764 S.W.2d 200 (Tenn., 1988) and *Brown v. Brown*, 198 Tenn. 600, 281 S.W.2d 492 (1955).

These specific reasons, along with the stated questions offered for review and the accurate factual summary clearly show the factors that meet the requirements for supreme judicial review: The needs to secure uniformity of decision, for settlement of important questions of law and

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<sup>6</sup> Providing that the said chapters "apply to the operation and regulation of state trust companies." Chapter 112, Public Acts of 1999, § 4, codified in T.C.A. § 45-1-124(b).

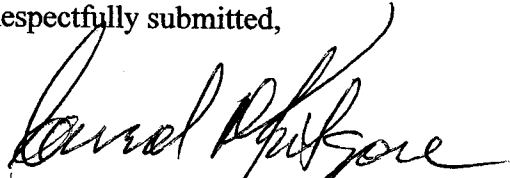
<sup>7</sup>Such determination was made by this Court's statement: "It is not in accord with **any rule of statutory construction** to lift one sentence out from the statute and construe it alone, without reference to the balance of the statute, . . ." in *Cummings v. Sharp*, 173 Tenn. 637, 643-644, 122 S.W.2d 423, 425, as quoted and followed in *Rose v. Blewett*, 202 Tenn. 153, 163; 303 S.W.2d 709, 713 (1957).

questions of public interest, and the need for the exercise of this Court's supervisory authority.

It would be tragic—and should be impossible—for any Tennessee citizen, individual or corporate, to advisedly conclude that Tennessee had seized its property and destroyed its valuable business, genuinely believing that no law authorized such action, and that the action violated constitutional prohibitions, only to find Tennessee's entire judicial system effectively closed to its detailed attempts to prove the truth of these beliefs through much research, much study, and much labor, all at great expense to the citizen.

ACCORDINGLY, Appellants respectfully pray for permission to appeal to this Court.

Respectfully submitted,



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#### **Certificate of Service**

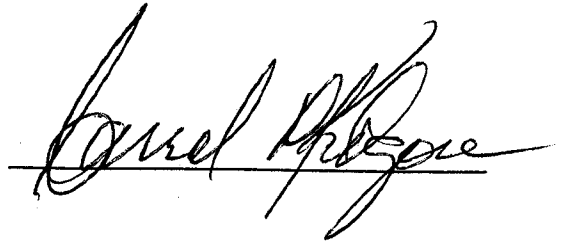
It is hereby certified that copies of the foregoing application have been mailed by First Class Mail, postage prepaid, to:

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this February 24, 2006.

A handwritten signature in black ink, appearing to read "Donald Schwendimann", written over a horizontal line.

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**APPENDIX**

**Copy, Opinion of the Court of Appeals**