2-1-1935

Bankruptcy -- Jurisdiction of Court Under 1933 Amendments

D. W. Markham

Follow this and additional works at: http://scholarship.law.unc.edu/nclr

Part of the Law Commons

Recommended Citation
D. W. Markham, Bankruptcy -- Jurisdiction of Court Under 1933 Amendments, 13 N.C. L. Rev. 204 (1935).
Available at: http://scholarship.law.unc.edu/nclr/vol13/iss2/5

This Note is brought to you for free and open access by Carolina Law Scholarship Repository. It has been accepted for inclusion in North Carolina Law Review by an authorized editor of Carolina Law Scholarship Repository. For more information, please contact law_repository@unc.edu.
between the estates of the partners. By analogy the estate by the entirety should go first to pay the joint creditors. In some jurisdictions where the estate by the entirety is not recognized in personalty received from sale of realty held by entireties, it is suggested that the surplus should be divided between the estates of the spouses for payment of the individual debts. The surplus, however, in other jurisdictions would still be held by the entireties. In these jurisdictions the trustee of the estate of the individual spouse would not be vested with any part of the surplus since a judgment creditor of the individual spouse could not reach it, and the trustee has no more right than such creditor. The suggested distribution would protect joint creditors who make loans believing they will be satisfied out of the estate by the entirety and would allow the surplus to be used, when the law permits, in payment of the debts of the individual spouses.

ROBERT BOOTH.

Bankruptcy—Jurisdiction of Court Under 1933 Amendments.

A decision which will prove to be of unusual interest to the profession, and of far-reaching importance, is that of the Circuit Court of Appeals in In re Chicago, Rock Island & Pacific Railway Company.

The railway company filed its petition in the Northern District of Illinois for reorganization under the new Section 77 of the Bankruptcy Act. More than four months prior to the filing of the petition, the railway company had borrowed an aggregate of more than $17,000,000 from the Reconstruction Finance Corporation, two New York banks, two Illi-
nois banks, and a Missouri bank. As collateral for these loans, $54,000,-
000 in securities, consisting largely of otherwise unissued bonds of the
railway company itself and of its subsidiaries, were pledged under an
agreement which gave the creditors a power of sale, conditioned upon
the happening of certain contingencies relating to the debtor's financial
status. Upon petition of the railway company, the District Court issued
an order enjoining these creditors from exercising the power of sale,
or from otherwise converting or disposing of the pledged collateral.
All of the creditors had filed special appearances to contest the Court's
jurisdiction over them and over the pledged securities.

On appeal, the Circuit Court of Appeals (per Evans, J.) affirmed
the order, relying solely, as to the jurisdictional question, upon that por-
tion of paragraph (a) of Section 77 which reads: "... If the petition
is so approved, the court in which such order approving the petition
is entered shall, during the pendency of the proceedings under this sec-
tion and for the purposes thereof, have exclusive jurisdiction of the
debtor and its property wherever located..." This language, accord-
ing to the opinion, "extended the court's jurisdiction over the debtor's
property so as to include the entire United States." That being so, the
pledged collateral was held to be "property" within the meaning of the
Section, and the jurisdictional issue was disposed of by saying, "In
short, the jurisdiction of the court, so far as the property was concerned,
included the territory wherein all of appellees' bonds were located."

Italics ours. The importance of this decision is increased by the fact that
the quoted language of §77 is also to be found substantially in §§74 (for the
relief of agricultural debtors) (11 U. S. C. A. §203n) and 77B (on corporate re-

No attempt is made in this note to deal with that aspect of the problem.
However, see Guaranty Trust Co. v. Galveston City R. Co., 87 Fed. 813, 815 (C. C.
A. 5th, 1898), where Court said: "They are evidence of debt, not assets of the
appellee." Compare Mississippi Valley Trust Co. v. Railway Steel Spring Co., 258
Fed. 346 (C. C. A. 8th, 1919).

The Court then proceeded to hold that the District Court not only had the
power to enjoin the sale of pledged securities, but might do so in a summary
proceeding, relying again upon §77 and giving it a "liberal construction... con-
sonant with the purposes of this remedial legislation."

These two problems are not within the scope of this note. However, the
decision, on both points, seems to be against the weight of judicial opinion prior
to the enactment of §77.

On the first point, see, in general, accord: Mississippi Valley Trust Co. v.
McCarter, 94 U.S. 734, 24 L. ed. 136 (1876); Hiscock v. Varick Bank, 206 U.S.
28, 27 Sup. Ct. 681, 51 L. ed. 945 (1907); In re Hudson River Nav. Corp., 57 F.
(2d) 175 (C. C. A. 2d, 1932); In re Browne, 104 Fed. 762 (E. D. Pa. 1900). Also
Remington, Bankruptcy (4th ed. 1934) §§923, 2510; 2 Collier, Bankruptcy
(13th. ed. 1923) 1550-53; Note (1924) 28 A. L. R. 409; Hatch, A Form of De-
pression Finance—Corporations Pledging Their Own Bonds (1934) 47 Harv.
L. Rev. 1093.

On the second point, see, in general, In re Silver, 2 F. Supp. 628 (S.D. Fla.
1933); Remington, Bankruptcy (4th, ed. 1934) §2350; 1 Collier, Bankruptcy
(13th, ed. 1923) 771-89.
The decision is in striking contrast with one of the same Court (Evans, J. again writing the opinion), decided only two years before. In that case, two of the Insull holding companies, both of which were Illinois corporations, had pledged the stocks of certain other Illinois corporations with New York banks to secure loans from the latter. Both holding companies went into receivership, and, on petition of the receivers, the District Court for the Northern District of Illinois enjoined the creditor banks from exercising the power of sale given in the pledge agreement, and from otherwise converting or disposing of the pledged securities. The banks appeared specially, and moved to vacate the restraining orders on the ground that the Court was without jurisdiction over either the banks or the pledged property. On appeal, the Circuit Court of Appeals ordered the injunctions vacated, holding that the Court had no jurisdiction over the parties, and that "the absence of possession, or any right to possession by the receivers, and the location of the pledged securities with the pledgees in New York" were "decisive of the question." In the course of his opinions in the Fentress case, Judge Evans remarked that "the jurisdiction of a court in bankruptcy in such matters is as extensive as that of a court of equity which appoints a receiver."

Was the jurisdiction of the court sitting in bankruptcy any more extensive than when sitting in an equity receivership, prior to the amendment? The Court's reliance upon the quoted language of the amendment in disposing of the jurisdictional question would indicate that it was not. Section 2 of the Bankruptcy Act expressly limited the jurisdiction of the court to the territorial limits of the district, and the process of a bankruptcy court could not validly issue outside those boundaries. However, upon the filing of the petition, the property of the bankrupt, wherever situated in the United States, was brought in custodia legis, and the court in which the petition was filed obtained "plenary jurisdiction in bankruptcy, coextensive with the United States,  

12 Acme Harvester Co. v. Beekman Lumber Co., 222 U.S. 300, 32 Sup. Ct. 96, 56 L. ed. 208 (1911)  
to order and control the disposition of the bankrupt's estate" and "to
determine all liens thereon and all interests affecting it." This jurisdic-
tion did not attach, however, when the bankruptcy court had neither
actual nor constructive possession of the property. Thus, an explana-
tion may be found for the fact that in the Fentress case, the decision
on the jurisdictional question rested jointly upon the absence of pos-
session, or right to possession, in the receivers, and the situs of the
pledged collateral outside the territorial limits of the district, while, in
the principal case, no mention is made of the Court's possession or right
to possession, but the pledged property is held to be within the newly
enlarged territorial jurisdiction of the Court; and that enlargement of
territorial jurisdiction is found in the amendment giving the court "ex-
clusive jurisdiction of the debtor and its property wherever located."

Was that portion of Section 77 intended to enlarge the territorial
jurisdiction of the bankruptcy court, so as to make it coextensive with
the United States, in proceedings under the amendment? The Court
believed that the amendment "was intended to and did wisely exclude
ancillary receivership proceedings in bankruptcy cases wherein railroad
corporations were the bankrupts." The belief in that purpose points
strongly to the interpretation which the Court adopted. However,
there are at least three considerations that militate against the conclusion
of the Court.

In the first place, the word "jurisdiction" has been subjected to such
indiscriminate use and has been permitted to assume so many connota-
tions that its use in the amendment furnishes no very valuable clue


In re Hudson River Nav. Corp., 57 F. (2d) 175 (C. C. A. 2d, 1932); In re Silver, 2 F. Supp. 628 (S.D. Fla. 1933); see In re Peacock, 178 Fed. 851, 856 (C.C. E.D. N.C. 1910); In re Dayton Coal & Iron Co., 291 Fed. 390, 396 (E.D. Tenn. 1922); In re Smith, 3 F. (2d) 40, 42 (S.D. Tex. 1924); 1 Collier, Bank-
ruptcy (13th, ed. 1923) 781-82.

The right to possession could have been no greater in one case than in the other. In re Hudson River Nav. Corp., 57 F. (2d) 175 (C. C. A. 2d, 1932). See In re Landquist, 70 F. (2d) 929, 936 (C. C. A. 7th, 1934), where the Court said:

"So far as we know it has always been held that a bankruptcy court has no
jurisdiction whatever over pledged security which has been transferred in good
faith by a debtor to his creditor more than four months prior to the filing of
the bankruptcy petition."

In this connection, see Report Pamphlet No. 1. The Association of the
Bar of the City of New York (1926-7). Annual Report of Special Committee
on Equity Receiverships, pp. 19-31, in which an extension of the doctrine of
§55 of the Judicial Code (11 U. S. C. A. §117) was advocated. See also, 56 A.
B. A. Rev. 406-9 (1931); and Swaine, Corporate Reorganization—An Amendment
to the Bankruptcy Act—A Symposium (1933) 19 Va. L. Rev. 317.

As was said by Professor Lloyd, in referring to the use of the word "lien,
"It is proof of the poverty of the legal imagination that in so many instances
to the Congressional intent. This is strikingly impressed upon one who reads the decisions of the bankruptcy courts and attempts to assign some meaning to the word wherever used. On at least one occasion, the Circuit Court of Appeals referred to the powers of the bankruptcy court, long prior to the enactment of the Section 77, in language practically identical with that of the amendment upon which the Court relied in the principal case—and at a time when the territorial jurisdiction of the bankruptcy courts was expressly limited, and the limitation recognized. Is language to be given one meaning when used by the courts, and another when used by Congress in a piece of rush legislation?

Secondly, paragraph (n) of Section 77 provides, in part, that “in proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court... shall be the same as if a voluntary petition for adjudication had been filed...” Is it clear that, if this paragraph is read with paragraph (a), Congress referred to territorial jurisdiction in paragraph (a), and to something else in paragraph (n)?

Thirdly, insofar as there is any value in speculating on the question of Congressional intent, it might be added that the relative obscurity of the provision relied upon by the Court leads one to the conclusion that no very revolutionary change was intended thereby. If Congress had intended to enlarge the territorial jurisdiction of bankruptcy courts in certain cases from the limits of the district to include the entire United States, is it not reasonable to presume that such an intention would have been phrased more unmistakably and placed a bit more conspicuously in the amendment?

It is submitted that, in view of the foregoing considerations, the Court’s decision on this point is at least dubious, the Court, perhaps, terms definitely applied to particular purposes are forcibly appropriated to other uses.” (Lloyd, Mortgages—The Genesis of the Lien Theory (1922) 32 Yale L. J. 233, 245).

In In re Granite City Bank, 137 Fed. 818, 822 (C. C. A. 8th, 1905, the Court said: “Under the scheme of the bankrupt act, the District Court of the domicile of the bankrupt takes exclusive jurisdiction of the bankrupt and his property, wherever situated, to administer it and distribute the proceeds pari passu among the creditors.” (Italics ours.)

Other illustrations of such language are to be found in In re Dempster, 172 Fed. 353, 355 (C. C. A. 8th, 1909); Staunton v. Wooden, 179 Fed. 61, 63 (C. C. A. 9th, 1910); and a particularly interesting example in Orinoco Iron Co. v. Metzel, 230 Fed. 40, 46 (C. C. A. 6th, 1916).

Note 11 supra. Italics ours.

It is not to be understood that this note takes a position critical of the policy which apparently impelled the Court to the general result reached in the case and prompted it to hurdle the jurisdictional problem in order to reach that result. The note, rather, raises the question whether or not the language of the amendment (upon which the Court was forced to, and did, rely) justified the hurdle which the Court made.
assuming the equitable viewpoint in "regarding as done that which ought to be done."

D. W. Markham.

Banks and Banking—Insolvency—Recovery of Funds Held by Insolvent Bank as Trustee Ex Maleficio.

The trust department of the C. Bank had approximately two hundred small trust accounts, whose uninvested funds had been included in a general deposit maintained by it in the commercial department. To facilitate investment the trust department consolidated these small accounts into what it termed a "Mortgage Pool Account," with itself as trustee, and each estate was credited with a participation certificate to the extent of its contribution. A consolidated account totaling $155,940 was thereby built up out of which the bank purchased from its own departments, affiliated investment companies, and elsewhere securities aggregating $151,867.34, leaving a cash credit in the pool account of $4,072.66. Subsequently the bank closed its doors, and the plaintiffs were appointed to succeed it as trustees for the "Mortgage Pool Account." In this action it was alleged and to some extent proved that the securities sold to the pool account then had a market value of $60,746.93 less than the sums actually paid therefor. On this basis plaintiffs sought to impress the bank's cash in the hands of the Commissioner of Banks with a constructive trust in favor of the estates represented by them. Held, that the judgment of nonsuit be affirmed.1

It is well settled that a fiduciary may be declared a trustee ex maleficio of any profits which he may have acquired through his dealings with the funds committed to his care,2 and, since creditors are not bona fide purchasers, the rule is applicable to the receiver3 of an insolvent trustee. Such a proceeding, however, is not, as is so often stated, one to establish a preference, but, rather, an action brought to restore to the cestui that which equity considers his own.4 Success will depend upon the proof of two facts: (a) that the alleged trustee, whether express or ex delicto, has at the outset acquired something of value the beneficial ownership of which remains, either by express or implied provisions of the parties, or in the contemplation of law, in another; and (b) that

1 Cocke v. Hood, 207 N. C. 14, 175 S. E. 841 (1934).
3 The same principles would, of course, be applicable to an assignee for benefit of creditors or trustee in bankruptcy.