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Article 4

Bankruptcy - Reorganizations - Equity Receiverships

Oliver H. Bassuener

RECENT DECISIONS

BANKRUPTCY—REORGANIZATIONS—EQUITY RECEIVERSHIPS.—Three creditors, with claims in excess of $1,000, filed a petition against the debtor hotel corporation, requesting reorganization under Section 77B of the Bankruptcy Act. The hotel properties of the debtor corporation were under the control of a receiver appointed to collect rents and profits in a suit begun by a mortgagee to foreclose. The petitioning creditors set out the appointment of the receiver in the foreclosure suit as a pending equity receivership sufficient to support the petition for reorganization. The bankruptcy court dismissed the petition. *In re 2168 Broadway Corporation.* 11 F. Supp. 404 (S.D. N.Y. 1935). The decision was affirmed by decree of the circuit court of appeals. *In re 2168 Broadway Corporation,* 78 F. (2d) 678 (C.C.A. 2nd, 1935). On *certiorari* to the Supreme Court, *held,* decree affirmed; submitting to the foreclosure receivership was not an act of bankruptcy and it was not sufficient under the statute as an equity receivership. *Duparquet Huot & Moneuse Co.* v. *Evans,* 56 Sup. Ct. 412, 80 L.ed. 413 (1936).

Section 77B was enacted to eliminate practical difficulties of administration, with the possible attendant unfair practices, growing out of the older equity reorganization proceedings. See Sabel, *The Corporate Reorganizations Act* (1934) 19 MINN. L. REV. 34. The receivers appointed in a consent proceeding might be favorable to particular groups of creditors and stockholders. Other creditors might be lulled into inactivity and lose their opportunities to file involuntary petitions in bankruptcy. Resort to the bankruptcy court left no opportunity for participation by stockholders. The bankruptcy courts hesitated to enforce early sales and distributions of assets. *Cf. Harkin* v. *Brundage,* 276 U.S. 36, 48 Sup. Ct. 268, 72 L.ed. 457 (1928); *May Hosiery Mills* v. *District Court,* 64 F. (2d) 450, 452 (C.C.A. 9th, 1932); Friendly, *The Corporate Reorganizations Act,* (1934) 48 HARV. L. REV. 39. Section 77B literally specifies that the existence of a pending equity receivership or the committing of an act of bankruptcy within the previous four months shall be required to support the jurisdiction of the bankruptcy court on an involuntary petition in a reorganization proceeding. Section 77B (a), 48 Stat. 913 (1933), 11 U.S.C.A. § 207 (a) (1935). By text definition the phrase "equity receivership" may be taken to include all proceedings in which a receiver is appointed by an equity court for any purpose. 1 CLARK, RECEIVERS, (2d ed. 1929) § 12; Note (1935) 19 MARQ. L. REV. 190. There has been some opinion among the lower federal courts that "equity receivership" in Section 77B includes receivers appointed to collect rents and profits in a foreclosure suit. *In re Surf Bldg. Corporation,* 11 F. Supp. 295 (E.D. Ill. 1934) in which the foreclosure receivership covered most of the debtor's assets; *In re Granada Hotel Corporation,* 78 F. (2d) 409 (C.C.A. 7th, 1935), reversed on *certiorari* in the Supreme Court, *Tuttle* v. *Harris,* 56 Sup. Ct. 416, 80 L.ed. 417 (1936), decided with the principal case.

Taking into consideration the experiences in reorganization before the enactment of Section 77B and the experiences of the bankruptcy courts in working out liquidation where various kinds of receivers had been appointed, the solution of the court in the principal case is plausible. In a foreclosure receivership reorganization is not the primary end sought. See *Sullivan* v. *Rosson,* 223 N.Y. 217, 119 N.E. 405, 4 A.L.R. 1400 (1918); *cf. In re Draco Realty Corp.,* 11 F. Supp. 405 (S.D. N.Y. 1935). Section 3 (a) of the Bankruptcy Act [30 Stat. 546 (1898), 32 Stat. 797 (1903), 44 Stat. 662 (1926), 11 U.S.C.A. § 21 (1926) (1935)], in declaring the appointment of a receiver for the debtor's property to be an act of bankruptcy, has been interpreted as excluding foreclosure receiverships from

the act of bankruptcy category. *Standard Accident Insurance Co.* v. *E. T. Sheftall & Co.*, 53 F. (2d) 40 (C.C.A. 5th, 1931). And while a trustee in bankruptcy supersedes receivers who have been appointed to conserve or to liquidate assets of a corporation, it has been suggested that even a trustee in bankruptcy could not interfere with a receiver put into possession at the request of a mortgagee in a foreclosure suit. Compare the two cases, *Gross* v. *Irving Trust Co.*, 289 U.S. 342, 53 Sup. Ct. 605, 77 L.ed. 1243 (1933) and *Stratton* v. *New*, 283 U.S. 318, 322, 327, 51 Sup. Ct. 465, 75 L.ed. 1060 (1931).

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BILLS AND NOTES—ACCOMMODATION CO-MAKERS—SUBROGATION.—The plaintiff's husband owed the bank $62,500. The debt was secured by the pledge of collaterals. To procure an extension of time, and to cover depreciation in the value of the pledged collaterals, the debtor executed and delivered to the bank his note for $15,000, secured by a mortgage on certain of his real estate. The plaintiff signed the note as a co-maker. She joined in the execution of the mortgage. Eventually the plaintiff paid the $15,000 note. Her husband died. The bank filed a claim against the estate for the balance of the indebtedness. The plaintiff demanded that the mortgage be assigned to her. When the bank refused to make the assignment, the plaintiff began this suit for subrogation. The bank contended that the sale of collateral left a substantial part of the total indebtedness unpaid, and the bank demanded that the court declare the premises to be a part of the decedent's estate, free from the lien of the mortgage and subject to the claims of the decedent's creditors. The trial judge gave relief to the plaintiff. On appeal, *held,* judgment reversed; the note was paid and the mortgage satisfied and the bank was entitled to judgment as requested. *Strelitz* v. *First Wisconsin Nat. Bank* (Wis. 1936) 264 N.W. 649 (three justices dissenting).

The language of the majority opinion is general and cryptic. The court speaks of the wife's being a party primarily responsible and as such not entitled to subrogation. Without some qualification by way of reference to the specific facts in the case that proposition is unsound. There is nothing in the Negotiable Instruments Law to justify it. By the terms of that act an accommodation co-maker is a party primarily responsible on the instrument. WIS. STAT. (1935) § 116.01. After the enactment of the Negotiable Instruments Law it has been held in some jurisdictions that extension of time by the holder to the principal debtor is no defense to the accommodation co-maker [*Union Trust Co.* v. McGinty, 212 Mass. 205, 98 N.E. 697 (1912); *Cellers* v. *Meachem*, 49 Or. 186, 89 Pac. 426 (1907)]; that tender at maturity to the holder thereof by an accommodation co-maker, a party primarily responsible, does not discharge the instrument [*Jameson* v. *Citizens Nat. Bank*, 130 Md. 75, 99 Atl. 994 (1917)]; that release of security by the creditor does not discharge the accommodation co-maker [*Merchants' Nat. Bank* v. *Smith*, 59 Mont. 280, 196 Pac. 523 (1921)]. These decisions do lay down propositions which supersede the traditional rules of suretyship, the common law rules. *Cf.* Note (1935) 19 MARQ. L. REV. 122. It is absurd, however, to generalize from them, and to suppose that since the enactment of the Negotiable Instruments Law these courts pretend to decide that the law of suretyship no longer applies in the field of bills and notes. See *Mueller* v. *Jagerson Fuel Co.*, 203 Wis. 453, 456, 233 N.W. 633, 72 A.L.R. 1059 (1931). The Wisconsin court has suggested that it will follow what has probably become the dominant view, that "extension of time" is no longer available as a defense to a party primarily responsible on a negotiable note, primarily responsible as the principal debtor or the accommodation party. *Rosendale State Bank* v. *Holland,*