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Article 11

Trust Receipts: Conditional Sales Contracts: Estoppel

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The court in the instant case placed a reasonable construction on the surety contract. But in refusing the defendant's contention, no longer of importance in view of the construction given the contract, by holding that he was estopped to assert such a defense, the court erred; for the reasoning imputed strength to the defense when in reality there was none; and the doctrine of estoppel was applied without considering the defendant's dual capacity.

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TRUST RECEIPTS—CONDITIONAL SALES CONTRACTS—ESTOPPEL.—Defendant, a finance corporation, in dealing with A, an automobile dealer, received from the manufacturer bills of sale. Defendant would then forward the bill of lading, together with a sight draft for 10 per cent of the purchase price, a note for the remainder and a trust receipt to a bank in A's community. The A company then would pay the draft and execute the note and trust receipt, and upon paying freight take possession of the cars. The trust receipts contained the usual provisions as to holding in trust, etc., A further agreeing not to sell, incumber, or otherwise dispose of the cars until all the payments were completed. Plaintiff company was engaged in buying chattel mortgages and conditional sales agreements. A represented to plaintiff that a car had been sold to one X, on a conditional sales agreement and offered plaintiff the contract. Plaintiff investigated the credit of X, found it satisfactory, bought the contract and recorded it. This conduct was pursued a second and third time with Y and Z, as supposed buyers. In fact X, Y, and Z never purchased the cars, their names being inserted on the respective contracts by A. The automobiles never left the possession of A, and were taken into possession of the defendant upon default of A on the notes in September, 1931. Action by plaintiff to recover the cars. Judgment for plaintiff, and motion for new trial denied; appeal. *Held,* judgment reversed. No one can transfer better title than he has. Plaintiff is not a bona fide purchaser. The rule of estoppel applies only if the party asserting it can show that he was in fact misled to his prejudice. Plaintiff had no knowledge with reference to the cars. *Iowa Guarantee Mortgage Corporation* v. *General Motors Acceptance Corporation,* (S. Dak., 1933) 250 N.W. 669.

Trust receipts have been interpreted by the courts as conditional sales, *New Haven Wire Company Cases,* 57 Conn. 352, 18 Atl. 266 (1899); *Mershon* v. *Moors,* 76 Wis. 502, 45 N.W. 95 (1890); as chattel mortgages, in Kentucky, *In re Draughn & Steele Motor Co.,* 49 F. (2d) 636 (E. D. Ky., 1931); in New Jersey, *Karkuff* v. *Mutual Securities Corp. et al.,* 108 N.J. Eq. 128, 148 Atl. 159 (1928); and in Texas, *Commercial Credit Co.* v. *Schlegel-Storseth Motor Co. et al.,* 23 S.W. (2d) 702 (Tex. Comm. of App., 1930); and as a bailment, in Pennsylvania, *Brown Bros.* v. *Billington,* 163 Pa. 76, 29 Atl. 904 (1894); in Nebraska, *General Motors Acceptance Corp.* v. *Hupfer,* 113 Neb. 228, 202 N.W. 627 (1925); and in California, *Commercial Credit Co.* v. *Peak,* 195 Cal. 27, 231 Pac. 340 (1924). Thus it is seen that the courts are as yet undecided as to its inherent nature, and the variance in the holdings has been to give or deny protection. *In the matter of L. E. Lee, Bankrupt,* 6 Am. Bankruptcy Rep. (N.S.) 437 (Ref. W. D. Wis., 1923).

It is in the nature of a pledge transaction, with delivery to the pledgor for a temporary purpose, *In re Smith-Flynn Commission Co.,* 292 Fed. 465 (C.C.A. 8th, 1923). The bona fide purchaser from the holder of the cars has always been protected by the court under situations similar to the instant case, *Glass* v. *Continental Guaranty Co.,* 81 Fla. 687, 88 So. 876, 25 A.L.R. 312 (1921); *Indiana*

Investment Securities Co. v. *Whisman,* 85 Ind. App. 109, 138 N.E. 512 (1923); *Mississippi Finance Corp.* v. *McGowan,* 108 Kan. 622, 196 Pac. 614 (1921); *Clark* v. *Flynn,* 120 Misc. Rep. 474, 199 N.Y.S. 583 (1923); *Truck, Tractor & Forwarding Co.* v. *Baker,* 281 Pa. 145, 126 Atl. 239 (1924).

The purchase may be outright or by conditional sale in which latter case, being a chose in action, the assignee of the contract takes all the rights of the assignor, *People* v. *Michigan Avenue Trust Company,* 233 Ill. App. 428 (1924); *Smader* v. *Columbia Wisconsin Co.,* 188 Wis. 530, 205 N.W. 816 (1925). Therefore the plaintiff in the instant case, had the transactions been actual, would have clearly been given protection. Query, In view of the fact that the courts have granted so little protection to the holder of the trust receipt, should it make any difference as to whether there was an actual buyer or not? The court, in support of its decision intimates that there is something more that the plaintiff was required to do, than merely to inquire into the credit of the supposed purchaser. Query, To what length must the finance company go in order to secure protection?

Because of the fact that the courts have drawn an analogy between the trust receipt transactions and pledges it might be that a chattel mortgagee subsequent to the trust receipt would be given protection as in the case of a pledge. *E. Bostheim Co.* v. *Schultz,* 46 Cal. App. 24, 188 Pac. 841 (1920). The situation here is analagous to a chattel mortgage transaction if the theory above is to be discarded. Plaintiff, herein, has loaned money on the security of the cars which in fact never left the dealer's hands. The form of the instrument means little to the court, which will look to the nature of the transaction. Thus plaintiff again becomes a subsequent encumbrancer, who is to have priority over the claim of the holder of the trust receipt.

The trust receipt transaction is a convenient commercial security and should be recognized as separate and distinct from other security transactions, and dealt with accordingly. The very purpose of this form of security is to leave the chattel in the hands of the dealer to sell free from any lien which might interfere with a subsequent purchase or encumbrancing. The courts have been extremely reluctant as always to recognize this change in commercial dealings. The farthest the court has gone was in *In re James,* 30 F. (2d) 555 (C.C.A. 2d, 1929) in which relief was granted against a trustee in bankruptcy where the security title came to the holder from the manufacturer directly, and it specifically differentiates this type from that in which the security passes through the intermediate step, i.e., a bank or trust company. In the latter case protection has been denied, *In re Schuttig,* 1 F. (2d) 443 (D.C.N.J., 1924). Even in the former situation relief has been denied, *In the Matter of L. E. Lee, Bankrupt,* supra.

The court in the instant case, in view of the reluctance to grant protection, has made a wide departure, whether advisedly or not. It disposes of the case on the theory that since the purchasers were fictitious, no title was transferred. It fails to discuss the fact that the cars here were in the possession of the dealer for the purpose of sale, and on its face that is what the transaction appeared to be.

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