Bankruptcy: Summary and Plenary Proceedings: Constitutional Law

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RECENT DECISIONS

BANKRUPTCY—SUMMARY AND PLENARY PROCEEDINGS.—CONSTITUTIONAL LAW.—The railway company, and nine wholly owned subsidiaries, alleging inability to meet accruing interest and principal charges, petitioned for a reorganization under Section 77 of the Bankruptcy Act. 11 U.S.C.A. 205 (July 1, 1898, c. 541, § 73, as added March 3, 1933, c. 204, s. 1, 47 Stat. 1467). The appellants, five banks and the Reconstruction Finance Corporation, held 54 million dollars of the debtor's own bonds as collateral to secure loans amounting to nearly 18 million dollars. From a summary order restraining them from selling or otherwise disposing of their security, the pledgees appeal. Held, decree affirmed. The restraining order was a valid exercise of authority necessarily conferred to make the amendment effective. In re Chicago, R. I. & P. Ry. Co., 72 F. (2d) 443 (C.C.A., 7th, 1934).

The appellants contended that the court had no power to make this restraining order in a summary proceeding. Prior to the amending of the Bankruptcy Act summary proceedings have been limited to orders restoring property of the bankrupt to the trustee from persons who claim no adverse title to it; to situations where the property is within the actual or constructive possession of the court. In re Prokop, 65 F. (2d) 628 (C.C.A., 7th, 1933), Note 8 L.R.A. (N.S.) 1232. So where a trustee sought to recover stock pledged by the debtor with a bank, the interest of the bank, an adverse claimant, could only be challenged in a plenary suit. In re Bacon, 210 Fed. 129, (C.C.A. 2d., 1913); 3 R.C.L. 182. Louisville Trust Co. v. Coningor, 184 U.S. 18, 22 Sup. Ct. 293, 46 L.Ed. 413 (1901); cf. Taylor v. Sternberg, 71 F. (2d) 157 (C.C.A. 8th, 1934). Bankruptcy courts had no jurisdiction to enjoin the disposition of the security by the pledgee. Hiscock v. Varick Bank of N. Y., 206 U.S. 28, 27 Sup. Ct. 681, 51 L.Ed. 945 (1906) (life insurance policy sold); In re Hudson River Navigation Co., 57 F. (2d) 175 (C.C.A., 2d, 1932) (pledged notes and shares of another corporation were disposed of). But where the security pledged is a mortgage leave of the bankruptcy court is necessary to a foreclosure. Isaacs v. Hobbs Tie & Timber Co., 282 U.S. 734, 51 Sup. Ct. 270, 75 L.Ed. 645 (1930). (For an extended discussion of the effect of the pledgor's bankruptcy on the rights of the pledgee see, McGinnis, The Sale of Collateral Security by the Pledgee Thereof after the Intervention of the Bankruptcy of the Pledgor, 9 Ind. Law Rev. 195; Hatch, A Form of Depression Finance: Corporations Pledging Their Own Bonds, 47 Harv. Law Rev. 1093.) In the instant case the court pointed out that to permit 54 million dollars of bonds, obligations of the debtor, to remain beyond its control would hamper or make impossible the consummation of a fair plan of reorganization; whereupon it determined that this power to restrain was necessarily incident to those expressly granted. e.g. The appellants might buy in all the collateral with a face value of 54 million dollars to discharge their claim of 18 million dollars, giving them eventually in the reorganization planning a claim for a 54 million dollar "position" in place of their 18 million dollar "position." Quaere, Would the court have the power to grant such an order were the collateral securities other than an obligation of the debtor. It is not necessary for the purpose of effecting reorganization that the court have before it securities other than those representing obligations of the debtor, the value of such securities being the pertinent inquiry.

Concerning the constitutionality of Section 77, much has been written. Spaeth, The Reorganization Amendments to the Bankruptcy Act, 8 Temple Law Quart. 447; Billig, Corporate Reorganizations: Some Recent Developments, 18 Minn.
Law Rev. 14; Stebbins, *Constitutionality of the Recent Amendments to the Bankruptcy Law*, 17 Marq. Law. Rev. 163; Sargent and Zelkowich, *The Problem of Reorganizing “Solvent” Corporations*, 29 Ill. Law Rev. 137. Those holding against its constitutionality contend that the constitutional grant “on the subject of bankruptcies,” (U.S. Const., Art. 1, Sect. 8), does not give the authority to effectuate a plan of reorganization. However the Supreme Court of the United States has never attempted to make an inclusive definition of “the subject of bankruptcies” as pointed out by Judge Sparks in *In re Landquist (In re Parmenter)*, 70 F. (2d) 929 (C.C.A., 7th, 1934). Those upholding the validity of the amendments see little difference between a scaling down of secured claims, and a compelling of unsecured non-assenting creditors to accept less than their contract claims in a composition proceeding. Composition proceedings are valid. *In re Reiman*, 20 Fed. 490, (D.C.S.D., N.Y., 1874); *In re Landquist*, supra.

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**Conditional Sale Agreements—Assignments—Automobile Registration.**

An automobile dealer purported to sell a car to one of his salesmen. Payment of the stipulated purchase price was secured by a conditional sale agreement. The car was left in the dealer’s garage. The dealer assigned the contract to the defendant who filed it with the register of deeds in the county where the salesman resided. That was not the county where the dealer’s garage was located. The dealer sold the car in the regular course of business to another purchaser on another conditional sale contract which the dealer assigned to the plaintiff. This contract was filed in the proper district. The defendant eventually seized the car claiming as an assignee of the vendor. Thereupon the plaintiff also claiming as an assignee of the vendor, brought this action for conversion. The trial was by the court and there was a judgment for the plaintiff. *Held*, judgment affirmed, the contract upon which the defendant relied was void, and the defendant had failed to file the contract in the proper district. *Burnett Co. Abstract Co. v. Eau Claire Citizen’s L. & I. Co. Co.*, (Wis., 1934) 255 N.W. 890.

Conceding, as the court does when it suggests the second ground for decision, that the assignment of the first sale agreement was comparable to the giving of a chattel mortgage, the defendant, having failed to comply with the filing statute (Wis. Stat. [1933] § 241.10), could get no protection against a subsequent purchaser or encumbrancer like the plaintiff, the second assignee. *Carpenter v. Forbes*, 211 Wis. 648, 247 N.W. 857 (1933); *Hartford Accident & Indemnity Co. v. Callahan*, 271 Mass. 556, 171 N.E. 820 (1930). On that ground alone the decision could be supported, but the court suggested, too, that the contract upon which the defendant relied was void, because there had been no change of possession after the purported sale. It is submitted here that the mere fact that a salesman had purported to purchase an automobile from his employer on a conditional sale agreement, and that he had permitted the car to remain in the dealer’s garage, would not be conclusive that the sale was void, nor would it follow thereafter that an assignee of the dealer-vendor could get no protection against any third party. Whether the dealer and his salesman have caused the car to be registered in the name of the salesman, the purported vendee, and whether they have caused a certificate of title to be issued to him, ought to be the decisive factors in these cases concerning the amount of protection to be given to an assignee situated like the defendant in the instant case, and that ought to be true whether the deal between the dealer and the salesman was a real transaction.