Case No. 7,076.

IRVING v. HUGHES.

[2 N. B. R. 61 (Quarto, 20);[1] 7 Am. Law Reg. (N. S.) 209; 6 Phila. 451; 24 Leg. Int. 380; 15 Pittsb. Leg. J. 121.]

Circuit Court, E. D. Pennsylvania. Nov. 12, 1867.

INVOLUNTARY BANKRUPTCY—FRAUDULENT PREFERENCE—REMEDY.

1. In a case of involuntary bankruptcy in which the debtor, being insolvent, or having insolvency in contemplation, and intending to give a preference, or to defeat or delay the operation of the bankrupt law [of 1867 (14 Stat. 517)] has, within six months before the commencement of the proceedings in bankruptcy, given to a creditor who had reasonable cause to believe that a fraud on this law was intended, or that the debtor was insolvent, a warrant of attorney under which judgment has been confessed in a state court, and an execution has been levied upon his stock in trade, which has not as yet been sold under it, the present bankrupt law gives to the court of the United States, for the proper judicial district, jurisdiction to prohibit such creditor, by injunction, from proceeding further under such execution.

[Cited in Markson v. Heaney, Case No. 9,098; Re Brinkman, Id. 1,884; Re Mallory, Id. 8,991; Thames v. Miller, Id. 13,860; Re California Pac. R. Co., Id. 2,315; Re Marter. Id. 9,143; Hudson v. Schwab, Id. 6,835.]

2. The district court, instead of issuing such an injunction under the summary jurisdiction in bankruptcy, may refuse to consider the subject unless under a distinct auxiliary proceeding in equity against such a creditor. The bill at the suit of the petitioning or any intervening creditor, may then be prosecuted in the circuit court on behalf of the general body of creditors, until the assignment in bankruptcy, after which the assignee may be substituted or added as a complainant: and if the proceedings in bankruptcy are duly prosecuted, a preliminary injunction issued by the circuit court may, in a proper case, be continued after answer, under such conditions as will preserve the priority of the creditor thus restrained, if the lien of his execution should ultimately be established.

The first section of the act of congress of 2d of March, 1867, establishing a uniform system of bankruptcy, provides that the jurisdiction conferred upon the several district courts of the United States shall extend to the collection of all the assets of the bankrupt; to the ascertainment and liquidation of the liens and other specific claims thereon, to the adjustment of the various priorities and conflicting interests of all parties, &c. The second section enacts that the several circuit courts of the United States for the respective districts shall have a general superintendence and jurisdiction of all cases and questions arising under the act; and, except when special provision is otherwise made, may, upon bill, petition, or other process, of any party aggrieved, hear and determine the case in a court of equity; and shall also have concurrent jurisdiction with the district courts of the same district of all suits at law or in equity brought by the assignee in bankruptcy against any person claiming an adverse interest, or by such person against the assignee, touching any property or rights of property of the bankrupt transferable to or vested in the assignee.

The eighth section enacts that appeals may be taken from the district to the circuit court in all cases in equity. As to involuntary bankruptcy, the thirty-ninth section enacts that any person residing and owing debts, as provided in other parts of the act, who, after the passage of it, shall commit any one of certain acts therein mentioned, shall be deemed to have committed an act of bankruptcy, and, upon petition of a creditor or creditors, in the mode and under the conditions prescribed, may be adjudged a bankrupt, provided the petition is brought within six months after the act of bankruptcy is committed. Among the acts of bankruptcy here specified, are making any assignment, &c, or transfer of the party's estate, property, rights or credits, with intent to delay, defraud or hinder his creditors, and making, when bankrupt or insolvent, or in contemplation of bankruptcy or insolvency, any payment, gift, grant, sale, conveyance or transfer of money or other property, estate rights or credits, or giving any warrant to confess judgment, or procuring or suffering his property to be taken on legal process, with intent to give a preference, or with the intent, by such disposition of his property, to defeat or delay the operation of the act. It is enacted that if such person shall be adjudged a bankrupt, the assignee may recover back the money or other property so paid, conveyed, sold, assigned or transferred, provided the person receiving such payment or conveyance, had reasonable cause to believe that a fraud on the act was intended, or that the debtor was insolvent. The fortieth section enacts that upon the filing of the petition authorized by the next preceding section, the court, if sufficient grounds for it appear to exist, shall, in a prescribed mode, require the debtor to show cause at a time specified "why the prayer of the petition should not be granted, and may also, by its injunction, restrain the debtor and any other person, in the meantime, from making any transfer or disposition of any part of the debtor's property not excepted by this act from the operation thereof, and from interference therewith." The forty-first section enacts that if it appears that the facts set forth in the petition are not true, or that the debtor had paid and satisfied all liens upon his property, in case the existence of such liens were the sole ground of the proceeding, the proceedings shall be dismissed. In several cases of involuntary bankruptcy in this district, the alleged act of bankruptcy has been that under a warrant of attorney, given within six months by the alleged bankrupt, judgment against him had been entered at the suit of a favored creditor in the state court, and an execution levied upon the stock in trade of the defendant,

who (it is alleged) gave the warrant, or procured the levy to be made, when he, with such plaintiff's knowledge, was insolvent, or contemplated insolvency, and that the intent was to give a preference, or to defeat or delay the operation of the bankrupt law; this alternative intent being usually, in the proper language of pleading, alleged conjunctively as a two-fold intent.

In these cases, unless the property levied on has been already sold under the execution, the petitioning creditor, upon obtaining the preliminary order on the debtor to show cause against the adjudication of bankruptcy, has usually asked of the district court an injunction prohibiting the judgment creditor from proceeding further under his execution in the state court. The district court has uniformly refused to grant such a preliminary injunction without a previous citation of the execution creditor; and, upon the return of such citation, has given to him the option of requiring the petitioning creditor to proceed by bill in the circuit court under the auxiliary jurisdiction conferred as above by the bankrupt law. When the urgency has been too great to abide the return of a citation, the district court has required the petitioning creditor to proceed, at all events, in the first instance, by bill in the circuit court. Preliminary injunctions have been granted upon such bills, with saving to the party enjoined of his lien if its priority should afterwards be established either under the proceedings in bankruptcy, or in the suit in equity. The court has remarked that after the appointment of an assignee in bankruptcy, the proceedings in equity could not be continued, except under a supplemental bill at his suit. The execution creditor thus enjoined has, in some cases, moved to dissolve the injunction. In one of these cases an objection to the jurisdiction of the circuit court was that the second section of the act of congress confers jurisdiction upon this court, with an exception of cases for which special provision is otherwise made, and that the case was within the exception because the fortieth section gave a summary jurisdiction to the district court in bankruptcy to restrain, by injunction, the debtor, and any other person, from making any transfer or disposition of the debtor's property and from any interference with it. The answers to this objection were that the summary jurisdiction specially conferred by the fortieth section was not coextensive with the exigency of the case in which an injunction may be necessary; that this summary jurisdiction was, perhaps, limited to cases of restraint of the alleged bankrupt's own agents or other persons in immediate privity or association with him, and that it was, at all events, in terms expressly limited to the interval between the issuing and the return of the order to show cause. It was suggested that formerly, under the bankrupt law of 1841 [5 Stat. 440], a question had arisen whether the prohibition of the act of 2d of March, 1793, section five [1 Stat. 334], to grant an injunction without previous notice, applied to a proceeding in equity in aid of the jurisdiction in bankruptcy, and the enactment now in question resolves this doubt by allowing the injunction, without previous notice, for this interval of time between the issuing and the return of the order to show cause.

The court overruled the objection. In the cases which have been mentioned thus far, the circuit court was held by the district judge sitting alone. The question of jurisdiction was very little contested, the principal discussions being upon the legal and equitable merits of the respective cases.

In the meantime, the district court sitting in bankruptcy had several times refused to interfere, in cases of voluntary bankruptcy, with questions upon the enforcement of prior liens in the state courts by ordinary executions; and some cases in bankruptcy had been decided in the western district of Pennsylvania in which the language used was understood by some persons to imply a doubt of the judicial power of the courts of the United States to enjoin the plaintiff in any judgment in a state court from proceeding under an execution, though the execution itself was a direct violation of the rights of the general creditors under the thirty-ninth section of the present bankrupt law. In these cases, however, the bankruptcy was not involuntary; and there was only one case in which any question as to the right of priority of an execution creditor could be supposed to have in anywise arisen. In the present case in the circuit court, the bill was auxiliary to the jurisdiction in bankruptcy under proceedings against an involuntary bankrupt. The defendant in equity, who was plaintiff in an execution upon a judgment confessed in a court of the state, had been prohibited by a preliminary injunction from proceeding under it. Upon filing his answer, he had moved to dissolve the injunction. The cause came on for argument first, upon the question of jurisdiction, and second, upon merits. The district judge, holding the circuit court, adjourned the argument of the question of jurisdiction until the circuit judge should be present

This question was accordingly argued before the two judges

(GRIER, Circuit Justice, and CADWALADER, District Judge).

For the defendant the decisions in the Western district were cited, and it wasart, by Mr. Longstreth and Mr. Townsend, that the foundation of an argument for the jurisdiction upon the fortieth section of the bankrupt law was defective, because that section applied only to the period anterior to return of the order to show cause.

THE COURT overruled the objection to the jurisdiction, saying: The eases in bankruptcy in the Western district are inapplicable. The language used in them should be

understood according to their subject matter. The case principally relied on was one of voluntary bankruptcy involving a question which the court of the state was considered by the judge fully competent to decide. Here, on the contrary, the question is not fully cognizable under the jurisprudence or legislation of the state. The courts of the state certainly cannot, in all cases, enforce the adversary rights of the general creditors under an involuntary bankruptcy. The jurisdiction of the courts of the United States does not here depend upon the provision of the fortieth section of the present bankrupt law. This provision does, indeed, impliedly recognize the jurisdiction. But the previous enactments of other sections confer it. The provision of the fortieth section applies only to the primary stage of the proceedings. In that stage it dispenses with conditions and formalities which must otherwise have been fulfilled and observed. As against what parties other than the alleged bankrupt it has thus dispensed with them need not be considered, because the present proceedings in this court, if in proper form, cannot be irregular. Under the former English jurisdiction in bankruptcy, the chancellor would refuse to proceed otherwise than upon a bill, where he thought proper thus to afford an opportunity to appeal from his decision. The present bankrupt law of the United States gives to this court, in addition to its revisory jurisdiction, an auxiliary jurisdiction which may sometimes be so exercised as to secure the benefit of an appeal from the district court without the delay and expense. These courts have no supervisory jurisdiction over proceedings of the state courts. In each of the cases [Diggs r. Wolcott] 4 Cranch [8 U. S.] 179, and [Peek v. Jenness] 7 How. [48 U. S.] 612, 625, the court of the state had full cognizance of the subject of controversy, and of all its proper incidents; and in the case in 7 How. [48 U. S.] the subject was not peculiarly cognizable under proceedings in bankruptcy. In such a case to enjoin the plaintiff in the state court would, in effect, have been to enjoin that court, which the act of the 2d of March, 1793, had prohibited. But, in the present case, if the act of 1793 would otherwise have been applicable, the present bankrupt law would exclude its application so far as the present question is concerned. The state court cannot be enjoined; but the litigant in it may be restrained from doing what would frustrate or directly impede the jurisdiction expressly conferred by the bankrupt act.

The jurisdiction having thus been established, the argument of the motion to dissolve the injunction was heard in the circuit court, on bill and answer, by the district judge sitting alone. He refused to dissolve the injunction, but modified it in a manner which does not concern the question of jurisdiction [so as to save the lien of the defendant when the goods should be sold and the money realized].[2] The injunction, thus modified, continues in force. He said, as to the jurisdiction, that although he had exercised it very cautiously, and would continue to do so, he had never doubted its existence, and that he had asked the attendance of the circuit judge merely in order that any doubts of others might be quieted.

[1] {Reprinted from 2 N. B. R. 61 (Quarto, 20), by permission.}

[2] {From 7 Am. Law Reg. (N. S.) 209.}