13FED.CAS.—71

Case No. 7,529.

IN RE JORDON.

[9 N. B. R, (1874) 416.][1]

District Court, E. D. Michigan.

BANKRUPTCY—MORTGAGE—CHANGE OF SECURITY WITHIN FOUR MONTHS—PREFERENCE.

1. A being indebted to B executed to him a mortgage upon his entire stock of goods to secure the payment of the sum due in one year. Two years afterward, the mortgage and interest having increased several hundred dollars, A gave B his note for the amount at thirty days, and executed another mortgage on the stock of goods then on hand, part of which consisted of the old stock and part of the new. This last mortgage was given within four months before the commencement of proceedings in bankruptcy, and the assignee claimed that A was insolvent at the time, took possession of the goods and sold them. B then presented proof of his claim as a secured debt and asks that the same be paid him out of the proceeds of the mortgaged property. The assignee asks that the proof of claim be rejected, and that B's application be denied. *Held,* that upon taking the second mortgage the first ceased to have any validity or effect, and the mortgagee's rights as to lien must stand and be determined solely by the second mortgage: that the second mortgage was a preference to the mortgagee under sections thirty-five and thirty-nine of the bankrupt act [of 1867 (14 Stat. 534, 536)]; that B is absolutely prohibited from proving his debt against the bankrupt's estate.

2. Application of B denied, with costs, including attorney's fee of fifteen dollars.

On the objections of the assignee to the proof of claim offered by George D. Moulton, a creditor, and to the application of the latter to have his claim preferred on account of a lien by way of mortgages. On the 20th of February, 1871, the bankrupt [James Jordon], being a merchant and indebted to Moulton for loans of money in the sum of nine hundred and twenty-five dollars, executed to Moulton a mortgage upon his entire stock of goods then on hand, to secure the payment of said sum, in one year from date, with interest at ten per cent. On the 11th day of February, 1873, there was due and unpaid upon this mortgage, for principal and interest, one thousand one hundred and three dollars and twenty-five cents. On that day the bankrupt gave Moulton a promissory note for that amount due in one month from date with interest at ten per cent, and at the same time executed to Moulton another mortgage on his entire stock of goods then on hand, and store furniture and fixtures; which stock consisted in part of goods on hand when the first mortgage was given, and in part of new goods not covered by the first mortgage. The reason for taking the new mortgage was that the debt had become so much increased by accumulations of unpaid interest, and the stock covered by the first mortgage had become so much diminished by sales by the mortgagor, in the usual course of trade, that the security had become insufficient. The mortgage of February 11th, 1873, was given within four months before the commencement of the proceedings in bankruptcy; and it is claimed by

the assignee that the bankrupt was insolvent at the time, and that the mortgage was given by him with a view to give Moulton a preference over his other creditors, and that the latter had reasonable cause to believe, etc.; and that not having surrendered the advantage gained thereby, Moulton is prohibited from proving his claim or receiving any advantage on account of his said mortgage. The assignee took possession of the stock, sold it, and the proceeds are now in court. Moulton having presented proof of his

claim as a secured debt, setting up both mortgages, asks that the same be paid to him out of the proceeds of the mortgaged property. The assignee asks that the proof of claim be rejected, and that Moulton's application for payment be denied.

LONGYEAR, District Judge. The mortgage of February 11th, 1873, was to secure the same debt secured by, and it covered all the property covered by, the previous mortgage. It was clearly in substitution for the previous mortgage. In Re Wynne {Case No. 18,117}, Chief Justice Chase held, in a case in point, that upon taking the second mortgage the first ceased to have any validity or effect, and that the mortgagee's rights as to lien must stand and be determined solely by the second mortgage. In deciding the question he made use of the following language: "It is doubtless true that a mortgage or other conveyance made as security for a debt evidenced by a note or bond will operate as security for the same continuing debt, though the evidence of it be changed by renewal or otherwise. Winsor v. McLellan {Id. 17,887}. But in this case it is the security itself which has been changed, and not the evidence of the debt. The deed of December 8, 1866, was executed, it seems, in substitution for that of August, which therefore ceased to have any validity or effect." This, I believe, is but a simple declaration of settled law, and announces no new doctrine. It governs this case.

The only question to be determined, therefore, is as to Moulton's rights and disabilities under the mortgage of February 11th, 1873. From the proofs there is no room left in my mind for doubt that the bankrupt was in fact insolvent when this mortgage was given, and, of course, that it was a preference to the mortgagee. I am convinced, also, beyond a reasonable doubt, from Moulton's long and close famliarity with the bankrupt's affairs and business, and from various specific facts and circumstances developed by the proofs, but too numerous to mention in detail in this opinion, that Moulton had not only reasonable but abundant cause to believe the bankrupt insolvent, or at all events in failing circumstances, and that it was such belief, actually entertained by him, that moved him to seek and obtain better security by the taking of the mortgage. This brings the case clearly within sections thirty-six and thirty-nine of the bankrupt act, defining and prohibiting preferences in certain cases. This unlawful preference Moulton has not surrendered to the assignee, but, on the contrary, he is now before the court in the attitude of insisting upon its enforcement. The twenty-third section of the bankrupt act provides that "any person who, after the approval of this act, shall have accepted any preference, having reasonable cause to believe that the same was made or given by the debtor contrary to any provision of this act, shall not prove the debt or claim on account of which the preference was made or given, nor shall he receive any dividend therefrom until he shall first have surrendered to the assignee all property, benefit or advantage received by him under such preference."

By this provision Moulton is absolutely prohibited from proving his debt in this court against the bankrupt estate, beyond the power of the court to grant him any relief whatev-

er from the effects of the prohibition. The claim is for one entire and indivisible debt, and the prohibition applies to every part of it. The debt not being provable no claim could be maintained on account of it to any portion of the assets, by way of lien or otherwise. And this would be equally the case even if the first mortgage could be held to be still in existence. Without proof of the debt no lien can be enforced any more than dividends can be received on account of it. Phelps v. Sellick [Case No. 11,079]. This law may operate harshly in particular instances, but its commands are imperative and the courts have no discretion in the matter. Moulton has, however, only to blame his own anxiety to get the start of the bankrupt's other creditors instead of sharing with them as to any deficiency of the property covered by his former mortgage, according to the spirit, intent and purpose of the bankrupt law. When he took the mortgage of February 11th, 1873, he did so subject to the chances of his mortgagor being thrown into bankruptcy within four months thereafter. Those chances have turned against him, and he must abide the consequences.

It results that Moulton's proof of claim must be rejected, and his application to have his debt or any part thereof paid out of the proceeds of the mortgaged property must be denied; and Moulton must pay the costs of this proceeding, including an attorney's fee of fifteen dollars.

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