29FED.CAS.—18

Case No. 17,194.

WARREN v. DELAWARE, L. & W. RY. CO.

[7 N. B. R. 451;[1] 5 Chi. Leg. News, 205; 4 Leg. Op. 533.]

District Court, N. D. New York. Dec. 23, 1872.

BANKRUPTCY—BILL BY ASSIGNEE TO AVOID FRAUDULENT JUDGMENTS—COSTS.

An assignee in bankruptcy filed a bill in equity against a creditor of the bankrupt for the purpose of obtaining a decree that several judgments in favor of that creditor and against the bankrupt, and the executions issued thereon were fraudulent and void as against the said assignee. *Held,* that under the proofs in the case and the authorities cited, the assignee's right to the decree was undoubted; that the judgments in question were obtained when the bankrupt was insolvent, such creditor having reasonable cause to believe his debtor was insolvent at the time such actions were brought; that the creditor having fought this case to the bitter end to maintain his preference, the assignee must have costs.

In equity.

HALL, District Judge. This is a bill in equity, filed by the plaintiff, as assignee in bankruptcy of the Wadsworth Iron Works, for the purpose of obtaining a decree that several judgments in favor of the defendant, against the bankrupt, and the executions issued thereon are fraudulent and void as against such assignee. The petition in bankruptcy, under which the plaintiff was appointed assignee, was filed against the bankrupt on the 20th day of April, 1871. It appears by the pleadings and proofs that in February, March and April, 1871, the defendant recovered against the bankrupt, by default, five several judgments. In the supreme court of the state of New York, and procured executions to be issued thereon to the sheriff of Erie county by whom such executions were levied upon the personal property of the bankrupt. Such judgments may be, briefly, further described as follows, viz.:

I. A judgment recovered February 18th, 1871, for the sum of eight thousand nine hundred and fifty-one dollars and two cents upon a promissory note of the bankrupt for eight thousand eight hundred and eighty-five dollars and sixty cents, dated October 18th, 1870, and payable in three months after the date thereof.

II. A judgment for four thousand seven hundred and fifty-seven dollars and seventy cents, recovered February 25th, 1871, on the promissory note of the bankrupt for four thousand seven hundred and sixteen dollars and ninety-two cents, dated October 25th, 1870, and payable in three months after the date thereof.

III. A judgment for four thousand seven hundred and sixty dollars and fifty-three cents, recovered March 4th, 1871, on a promissory note of the bankrupt for four thousand seven hundred and sixteen dollars and ninety-two cents, dated November 1st, 1870, and payable in three months after such date.

IV. A judgment for four thousand seven hundred and fifty-nine dollars and fifty-eight cents, recovered March 7th, 1871, on a promissory note of the bankrupt dated November 7th, 1870, and payable three months after such date.

V. A judgment recovered April 1st, 1871, for five thousand nine hundred and forty dollars and thirty-four cents, on a promissory note of the bankrupt, dated December 1, 1870, and payable in three months after date.

It further appears that no defence was interposed in any or either of the suits in which said judgments were so recovered; and upon the proof in the case it is very clear that the Wadsworth Iron Works, the bankrupt and defendant in such suits, for some time prior to January 1st, 1870, and ever after, was, in fact, insolvent and wholly unable to pay all its debts as they fell due in the ordinary course of business; and that the property of such bankrupt was never, after that time, sufficient to pay and discharge all its debts and liabilities upon a final settlement and closing of its business and estate. It also appears that a promissory note of the bankrupt, dated September 11th, 1870, for eight thousand four hundred and eighty-six dollars and ten cents, payable to the defendant three months after its date, and which had been endorsed by the defendant to the National City Bank of New York, was protested for non-payment at its maturity, December 3d, 1870; that the bankrupt was soon after prosecuted thereon by such bank at the request of the financial agents of the defendant; that a judgment was recovered thereon against the bankrupt by default, for the amount thereof, January 3d, 1871; that another note of the bankrupt, dated October 1st, 1870, and given to the defendant for the sum of eight thousand eight hundred and fifty-five dollars and ninety cents, payable three months after date, was also protested for non-payment at its maturity, and that the defendant recovered a judgment by default against the bankrupt for the amount thereof, February 1st, 1871; that the amount of the first of the two judgments last above named was collected by or paid to the sheriff, February 27th, 1861; and that the amount of the second was so paid or collected, March 27th, 1871. It also appears that Mr. Wadsworth, the president and chief manager of the bankrupt corporation, at some time in the fall of 1870, applied to the financial officers of the defendant for an extension of payment on a promissory note of the bankrupt about to fall due, and which had been given to the defendant by the bankrupt; and that in answer to such application he was told that the note had passed out of the hands of the defendant; that shortly before the maturity of the said note falling due December 3d, 1870, he applied for an extension of the payment of such note, and stated that if the payment of that note and the one to become due in January could be extended he would pay the others at maturity; that such application was declined and that thereupon Mr. Wadsworth was very angry.

The bankrupt was a manufacturer and the

seven notes referred to were severally its commercial paper. It is thus apparent that the Wadsworth Iron Works was not only insolvent when each of the notes upon which the judgments in controversy in this suit matured, but that it had committed repeated acts of bankruptcy to the knowledge of the defendant's officers and agents before the first of such judgments was recovered. That the agents and officers of the defendant had not only reasonable but very abundant cause to believe that the Wadsworth Iron Works was then insolvent is beyond doubt; and they certainly knew it was bankrupt, and liable to be proceeded against under the bankrupt act [of 1867 (14 Stat. 517)]. Under such circumstances the judgments in controversy can only be sustained, if they can be sustained at all, upon very clear and satisfactory proofs to repel the legal presumptions of actual or legal intent to give and to obtain a preference in fraud of the provisions, policy and purpose of the bankrupt act. Shawhan v. Wherrit, 7 How. [48 U. S.] 627; In re Bininger [Case No. 1,420]; Bump, Bankr. (5th Ed.) 468–470; In re Bininger [Case No. 1,420].

It was strongly insisted that there was no intention on the part of the bankrupt corporation to give a preference to the defendant, and the testimony of the treasurer and another active officer of the defendant has been taken for the purpose of showing that the omission to pay the notes above referred to, and the suffering of the judgments, executions and levies upon the property of the corporation as heretofore stated, were believed to be, and were, the result of a feeling of spite and vindictiveness on the part of Wadsworth, the principal stockholder and president of the bankrupt corporation, caused by the refusal of the defendant to grant an extension of further time for the payment of the aforesaid notes which fell due December 3d, 1870, and January 4th, 1871. The testimony of Mr. Wadsworth was not taken by either party, and the other evidence in the case is very far from satisfactorily establishing the allegation that he acted under the influence of such feeling, and intended, by refusing to cause the payment of the commercial paper of the corporation, and then suffering judgments, executions, and levies, as hereinbefore set forth, to injure rather than benefit the defendant. It must be presumed that he, as the principal stockholder, chief officer and manager of the corporation, knew, as the vice-president (who was examined) well knew, that the corporation was hopelessly insolvent and wholly unable to pay its debts in full. Knowing this and suffering these judgments to be taken and executions to be issued and levied, one after another, for many weeks, without giving notice to other creditors that they might institute proceedings in bankruptcy, he can not be allowed to say that he did not intend to give a preference to the defendant. He clearly intended to suffer and allow precisely what was done, and, as the necessary and inevitable consequence of its being done was to give such preference, he could not, if he had been examined as a witness, have effectually denied the intention which, under such circumstances, is by law conclusively presumed. In re Bininger [supra], and cases there

cited; Bump, Bankr. (5th Ed.) 49, 472–477, and cases cited; Toof v. Martin [13 Wall. (80 U. S.) 40].

The suffering of the judgments, executions and levies in controversy, was, in effect, a transfer of so much of the bankrupt's property as was necessary to satisfy such executions, while the bankrupt was hopelessly insolvent, and when the defendant had reasonable cause to believe such insolvency existed, and knew that acts of bankruptcy had been committed. The leading case of Toof v. Martin [supra], decided by the supreme court of the United States at the last December term, and which is only an affirmance of doctrines frequently acted upon by judges of the circuit and district courts, is deemed entirely decisive of this case. In that case it was declared by the court that "it is a general principle that every one must be presumed to intend the necessary consequences of his acts. The transfer in any case, by a debtor, of a large portion of his property, while he is insolvent, to one creditor, without making provision for an equal distribution of its proceeds to all his creditors, necessarily operates as a preference to him, and must be taken as conclusive evidence that a preference was intended, unless the debtor can show that he was at the time ignorant of his insolvency, and that his affairs were such that he could reasonably expect to pay all his debts. The burden of proof is upon him in such case, and not upon the assignee or contestant in bankruptcy. * * *" "It is manifest not only that the bankrupts were insolvent when they made the conveyances in controversy, but that the creditors Toof, Phillips & Co., had reasonable cause to believe that they were insolvent. The statute, to defeat the conveyances, does not require that the creditors should have had absolute knowledge on the point, nor even that they should, in fact, have had any belief on the subject. It only requires that they should have had reasonable cause to believe that such was the fact. And reasonable cause they must be considered to have had when such a state of facts was brought to their notice in respect to the affairs and pecuniary condition of the bankrupts as would have led prudent business men to the conclusion that they could not meet their obligations in the ordinary course of their business. * * * It only remains to add that the creditors had also reasonable ground to believe that the conveyances were made in fraud of the provisions of the act. This, indeed, follows necessarily from the facts already stated. The act of congress was designed to secure an equal distribution of the property of an insolvent debtor among his creditors, and any transfer made with a view to secure the property, or any part of it, to any one, and thus prevent

an equal distribution, is a transfer in fraud of the act." See, also, Smith v. Buchanan [Case No. 13,016]; Haskell v. Ingalls [Id. 6,193]; Bump, Bankr. (5th Ed.) 478, 479, and cases cited.

It was very earnestly insisted in behalf of the defendant, that the officers and agents of the defendant actually believed the bankrupt corporation to be entirely solvent, until after the proceedings in bankruptcy were commenced, and that the repeated failures of the bankrupt to pay at maturity, and the long continued suspension of the payment of the commercial paper in which the defendant was so largely interested, and the suffering of judgments, executions and levies to be had thereon, was caused by the unwillingness and not by the inability of the debtor; and that they sought to obtain such judgments without any intent to obtain a preference, and without any suspicion or cause to suppose that a fraud on the bankrupt act was intended. In support of these positions the testimony of two of the defendant's officers and agents was relied on, and one of them, although he knew at the time that an urgent application for an extension upon one or two of the first of the dishonored notes herein referred to was made a short time before the first of said notes became due, and also knew of the repeated failures to pay such notes, and of the legal proceedings thereon promptly commenced upon such refusals to pay, and had been told by the president of the defendant immediately after Mr. Wadsworth first refused to meet his indebtedness to the defendant, that "he (the witness) must get the money out of it as soon as he could," nevertheless testified that up to time of the issuing of the execution on the last judgment against the bankrupt he believed the bankrupt to be responsible and solvent; that he had no information to the contrary, and that when he obtained such judgments and caused executions to be issued, it was not done with any intent to obtain a preference over any other creditor. In charity to the witness it may be presumed that he testified in ignorance of the legal definition of insolvency, and of the natural and legal presumptions arising upon the knowledge and information in his possession, and perhaps confounded the ideas of motive and intent, and believed he was testifying truthfully. But to allow such testimony to control the rights of the general creditors, in cases like the present, would defeat the purposes and policy of the bankrupt act; and if the proper construction and administration of the act requires it, the act is, indeed, but a miserable abortion.

The language of the learned circuit judge who decided the Case of Bininger [Case No. 1,420], applies in its full force to the question of the intentions of the defendant, or the officers of the defendant, in this case. He says: "The debtor," (and of course the creditor, also) "must be taken to know the law, and to know the precise legal effect of his act. He did certainly intend the act and all the legal consequences of the act. "It is easy to confound motive with intent, and that has been done, I think, in the discussion of this case. It was done by the debtor, Clark, in his testimony. No doubt he testified

truthfully, when he said, in substance, that he did not intend to procure the appointment of a receiver with the intent to defeat the operation of the bankrupt law. I have no doubt he means by this, that defeating or delaying the operation of the bankrupt act, was not the motive which induced him to procure such appointment. He did intend to do the very thing which hinders and defeats that act, and in judgment of law, he knew when he did it that it would have that effect. Knowing the effect he must have intended to produce it, when he voluntarily chose to do the act. Whatever his motive was, he acted voluntarily in choosing, and therefore, in intending all the legal results which would flow from his action in the matter."

Upon the proofs in this case, and the authorties cited, it is impossible to doubt the right of the plaintiff to a decree, and the defendant having fought this case to the bitter end to maintain the preference claimed, the plaintiff must have costs.

NOTE. It was not necessary in this case, or in the case of Toof v. Martin {supra} to decide the question whether acts done in contravention of the general purposes and policy of the bankrupt act, and which directly tend to defeat such policy and purpose, by securing a preference of one creditor over other creditors of a known insolvent debtor, can be held invalid and be set aside when the case cannot be brought within any of the express provisions of the act declaring fraudulent and void certain specified acts by which it is attempted to secure such preferences. See Shawhan v. Wherrit, 7 How. {48 U. S.} 627; Bell v. Leggett, 3 Seld. {7 N. Y.} 176, Beattie v. Gardner {Case No. 1,195}, and cases cited.

[1] {Reprinted from 7 N. B. R. 451, by permission.}