

v.7, no 9-51
CROOKS, ASSIGNEE, V. STUART AND OTHERS.

Circuit Court, D. Iowa.

May 18, 1881.

1. CHATTEL MORTGAGE—SUBSEQUENT CREDITORS—IOWA STATUTE.

Under the statute of Iowa, as construed by the highest court of that state, an unrecorded mortgage of chattels, of which the mortgagor retains possession and control, is valid as against creditors who receive notice at any time before obtaining a lien by levy or otherwise.

2. SAME—SAME—COMMON LAW.

At common law a mortgage of chattels which permits the mortgagor to retain possession of the property and deal with it as his own, is void as against a creditor who becomes such without notice of the mortgage.

3. CONSTRUCTION OF STATUTE—CONFLICT OF LAWS.

In the construction of a statute of a state this court is bound by the construction placed upon it by the courts of that state, but the

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doctrine of the supreme court of the United States controls upon any question of general jurisprudence not depending for its support upon any provision of state law.

4. ASSIGNEE IN BANKRUPTCY—FRAUDULENT CONVEYANCES OF BANKRUPT.

The assignee in bankruptcy of the mortgagor has all the rights of creditors to attack conveyances made by the bankrupt in fraud of his creditors.

In Equity.

MCCRARY, C. J. The complainant, as assignee in bankruptcy of A. J. Nutter, bankrupt, and representing the creditors of the bankrupt estate, brings his bill to set aside two certain mortgages executed by the bankrupt upon a stock of merchandise, and to subject the same to the payment of the debts of the estate. The mortgage is assailed upon the ground that the mortgagor retained the possession of the goods mortgaged and used, and disposed of the same as his own; and upon the further ground that the mortgage

was not recorded until after the debts represented by complainant were contracted. One of the mortgages expressly provided that the mortgagor might dispose of the goods in the usual course of business; the other contained no such provision, but it appears that there was in fact no change of possession, and that the mortgagor, after the execution of both mortgages, and with the assent of the mortgagees, retained the possession and continued to carry on the business, buying and selling in the usual course of trade for about one year before the mortgages were recorded, and for a little more than a year before possession was taken under them. The debts represented by the complainant were contracted while the mortgagor was in possession and before the recording of the mortgages, and the creditors had no notice of any encumbrance upon the property.

The statute of Iowa provides as follows:

“No sale or mortgage of personal property, where the vendor or mortgagor retains actual possession thereof, is valid against existing creditors or subsequent purchasers without notice, unless a written instrument conveying the same is executed, acknowledged like conveyances of real estate, and filed for record with the recorder of the county where the holder of the property resides.” Code 1873, § 1923.

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Two questions have been elaborately discussed by counsel, to-wit:

(1) Whether under the statute a mortgage of personal property not recorded is valid as against a subsequent creditor who becomes such without notice of such mortgage. (2) Whether, independently of the statute, a mortgage of personal property, where the mortgagor retains the possession and deals with the property as his own, is valid as against a creditor of the mortgagor who becomes such without notice of the mortgage?

The first of these being a question as to the true construction of a statute of the state of Iowa, we are constrained to follow the decisions of the supreme court of the state, however much we may doubt the soundness of those decisions. Were this an original question we should hold, without hesitation, that the statute was enacted to prevent the perpetration of fraud by the sale or mortgage of personal property without the delivery of the possession, and without notice to persons subsequently dealing with the vendor or mortgagor. Independently of any statutory provision, a manual delivlivery of the mortgaged property to the mortgagee would be necessary to the validity of the instrument. This rule of the common law has its foundation in the doctrine that possession of personal property is *prima facie* evidence of ownership. To allow the owner of such property to transfer the title by a *secret* conveyance, while retaining the possession and assuming to act as the owner, was regarded at common law as permitting a fraud upon all who should deal with him upon the faith of his ownership. His possession and apparent ownership, it was believed, gave him credit, and afforded him the means of defrauding others.

The purpose of the legislature in enacting this statute was not, in our judgment, to set aside this wholesome doctrine and thus enable dishonest persons to commit fraud by means of secret chattel mortgages; it was only to substitute recording for delivery. If thus construed, the statute affords a protection against fraud quite as effectual as that given by the common law; but if we hold that a secret unrecorded sale or mortgage may be enforced as against a creditor who deals with the vendor or mortgagor in ignorance of its existence, unless such creditor shall, by attachment or otherwise, obtain 803 a lien before having notice of the instrument, it seems to us that the door for fraud is left wide open. One who gives credit to a

merchant in the open and exclusive possession of a stock of merchandise, upon which there is no recorded lien, has a right to assume that he is dealing with the owner of such stock, and to rely upon such ownership in extending credit. If he is to be affected by any secret lien upon such stock which may be recorded before he secures a lien by levy or otherwise, it will generally happen that the first notice to him upon which he can make an affidavit for attachment will be the recording of the lien, so that the circumstance that gives him the right cuts off the remedy. If, therefore, we were at liberty to construe the statute for ourselves, we should unhesitatingly hold the mortgages in question in this case to be void under the statute.

But the supreme court of Iowa, whose decisions upon the construction of state statutes are rules of decision in this court, have reached upon this question a different conclusion. By a series of decisions that court has held that an unrecorded mortgage of chattels, where the mortgagor retains possessions, is valid as against creditors who receive notice at any time before obtaining a lien by levy or otherwise. *Hughes v. Cary*, 20 Iowa, 399; *Allen v. McCalla*, 25 Iowa, 465; and other cases cited in note to the case of *Cragin v. Carmichael*, 2 Dill. 519.

The question remains whether these mortgages should be held void independently of the statute, upon the ground that the mortgagor retained the possession of the property, with power to dispose of the same in the usual course of trade. As already stated, the proof shows that the mortgagor remained in possession and continued the business with the assent of the mortgagees.

The case of *Robinson v. Elliott*, 22 Wall. 513, is, we think, conclusive of this controversy. It was there distinctly held that a mortgage of chattels which permitted the mortgagor to remain in possession until default in payment of the debt secured, with power to

sell the goods as theretofore, was fraudulent and void in law, and could not be enforced by a 804 court of equity. Mr. Justice Davis, who delivered the opinion of the court, expressed the opinion that to sustain the validity of such a transaction would be to permit the mortgagors, under cover of the mortgage, to sell the goods as their own and appropriate the proceeds to their own purposes. And he adds that—

“A mortgage which in its very terms contemplates such results, besides being no security to the mortgages, operates in the most effectual manner to ward off other creditors. And where the instrument on its face shows that the legal effect of it is to delay creditors, the law imputes to it a fraudulent purpose.”

This is a doctrine of general jurisprudence not depending for its support upon any provision of the state law; and we are, therefore, bound by the decision of the supreme court of the United States. If there be anything in the decision of the supreme court of Iowa in *Jordan v. Lindrum*, 8 N. W. Rep. 311, inconsistent with the doctrine announced in *Robinson v. Elliott, supra*, we must follow the latter, and not the former. It is suggested that the mortgages in controversy, being good as between the parties, are also good as between the mortgagees and the assignee in bankruptcy of the mortgagor; but the rule is well settled that the assignee represents the rights of creditors, and may attack conveyances made by the bankrupt in fraud of his creditors. The assignee may prosecute any suit to recover assets in the hands of third parties, or to enforce the payment of claims that could have been prosecuted by the creditors themselves had no proceedings in bankruptcy been instituted.

There will be a decree for complainant.

LOVE. D. J.. concurs.

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