Notes

POWER OF BANKRUPTCY RECEIVER TO SUE

IN the case of *Rivoli Drug Co. v. Lynch*,[1] it appeared that two drug stores had used mutual checking accounts and the same delivery facilities, and had represented for credit purposes that they were the same firm. A series of transactions had taken place which involved transfers of large quantities of stock from one store to the other. Subsequently a petition in bankruptcy was filed against the transferor and a receiver appointed. Upon authorization of the bankruptcy court the receiver sought an accounting and appointment of a receiver for the other store, alleging that there was danger of irreparable loss to creditors through dissipation of the assets. Over the objection that a bankruptcy receiver has no power to sue, the relief was granted.

By a strict construction of the Federal Bankruptcy Act the courts have evolved a so-called majority rule whereby the bankruptcy receiver, persistently characterized as the mere custodian of the visible property without title thereto, is denied the power to sue to recover debts or property.[2] The court in the instant case prefers to follow the principle, for which there is considerable support, that the receiver may bring suit, pending the election of a trustee, to prevent dissipation of the estate.[3] In support of these latter decisions and in derogation of the conception of the receiver as a passive custodian, it is observed that the receiver may invoke the summary jurisdiction of the bankruptcy court,[4] which

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[1] 50 F. (2d) 536 (C. C. A. 9th, 1931).

[2] Boonville National Bank v. Blakey, 107 Fed. 891 (C. C. A. 7th, 1901) (suit to avoid a preferential payment); Guaranty Title & Trust Co. v. Pearlman, 144 Fed. 550 (W. D. Pa. 1906) (fraudulent conveyance); Bingaman v. Commonwealth Trust Co., 1 F. (2d) 505 (M. D. Pa. 1924); Hanna, *The Receiver in Bankruptcy* (1930) 3 SO. CALIF. L. REV. 241, 242.

[3] In re Fixen, 96 Fed. 748 (S. D. Cal. 1899); McKenna v. Randle, 5 Alaska 590 (1st Div. Juneau, 1917). In the latter case the court said, on page 592, that it is the "height of absurdity to deny the receiver access to the courts to enable him to perform his duties under his appointment. He may sue out an attachment, or bring an action to prevent the statute of limitations from running, or sue at law to recover any debt or personal property which might be lost, and certainly if the interposition of equity is necessary to enable him to prevent loss or waste of assets, he has a right to bring suit for that purpose." See In re Dempster, 172 Fed. 353, 357 (C. C. A. 8th, 1909). *Cf.* In re Lebrecht, 135 Fed. 878 (W.D. Tex. 1905); West v. Empire Life Ins. Co., 242 Fed. 605, 606 (W. D. Wash., 1917); Ellis v. Feeney & Sheehan Building Co., 187 App. Div. 481, 485, 176 N. Y. Supp. 61, 64 (1st Dep't 1919) (where property has been taken from the receiver, he must retake it or answer in damages for the conversion).

[4] In general, whatever property the bankruptcy court would have summary jurisdiction to order surrendered later to the trustee it will have jurisdiction to order surrendered in the meantime to the receiver. 1 REMINGTON,

extends to all the property of the alleged bankrupt not held adversely under a *bona fide* claim of right.[5] Moreover, the contention that the receiver's powers are confined to the present visible *corpus* is met by the fact that the filing of a petition in bankruptcy is a *caveat* to all the world and in fact an injunction and an attachment in regard to all the property of the alleged bankrupt.[6] Furthermore, to accept the bald statement that the receiver shall never be entitled to sue is to overlook the provision of the Bankruptcy Act which allows the bankruptcy court to issue orders necessary for the protection of the estate.[7] Although such an order is not conclusive that there is a cause of action[8] it is not subject to collateral attack[9] and would therefore be determinative of the power to sue.

It has been urged that the receiver be given by statute a qualified title allowing him to bring suit in all cases except those relating to fraudulent or preferential assignments.[10] One writer would even extend the receiver's power to all cases,[11] despite the fact that the present Act expressly delegates to the trustee the right to sue in the excepted situations.[12] It is arguable that here, as in the ordinary suit, neither rule of court nor statute provides for an emergency situation, and in fact bankruptcy courts have relied upon their own power to allow the receiver summary process against a fraudulent conveyance.[13] Moreover, on the hypothesis that the framers of the Act contemplated a speedy adjudication, it might well be

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BANKRUPTCY (3d ed. 1923) § 452. See In re Harris, 221 U. S. 274, 280, 31 Sup. Ct. 557, 558 (1910).

[5] The test of jurisdiction is the possession of the *res* by the court, either actual or constructive. Examples of constructive possession are: property in the hands of the bankrupt's agent or bailee; property held by one who makes no claim, or merely a colorable claim. GILBERT'S COLLIER ON BANKRUPTCY (2d ed. 1931) § 23 (e) 1–5. Taubel Scott-Kitzmiller Co., Inc. v. Fox, 264 U. S. 426, 432, 44 Sup. Ct. 396, 398 (1924). Note (1925) 5 B. U. L. REV. 42; Note (1930) 5 ALA. L. J. 226. And even adverse claimants may be dealt with summarily when they have consented to the jurisdiction of the court. Bryan v. Bernheimer, 181 U. S. 188, 21 Sup. Ct. 557 (1900) (marshall); *cf.* May v. Henderson, 268 U. S. 111, 115, 45 Sup. Ct. 456, 458 (1925).

[6] See Mueller v. Nugent, 184 U. S. 1, 14, 22 Sup. Ct. 269, 275 (1901); Acme Harvester Co. v. Beekman Lumber Co., 222 U. S. 300, 306, 32 Sup. Ct. 96, 99 (1911).

[7] 30 STAT. 545-6 (1898), 11 U. S. C. § 11, I. 15 (1926). Not only is the receiver a proper person to carry out orders made pursuant to this section, but it is his duty to call to the attention of the court the necessity of such orders. In re Gottlieb & Co., 245 Fed. 139 (D. N. J. 1917).

[8] See Greenhall v. Hurwitz, 80 Misc. 186, 188, 141 N. Y. Supp. 914, 915 (N. Y. City Ct. 1913).

[9] Slaughter v. Louisville & Nashville R. R. Co., 125 Tenn. 292, 143 S. W. 603 (1911).

[10] See Hunt, *Improvement of Bankruptcy Administration,* (1931) 8 A. B. Rev. 57, 59.

[11] 2 CLARK, RECEIVERS, (2d ed. 1929) § 1111.

[12] 36 STAT. 842 (1910), 11 U. S. C. § 96 (1926) (preferential transfers); 32 STAT. 800 (1903), 11 U. S. C. §§ 107, 110 (1926) (fraudulent conveyances).

[13] In re Haupt Bros., 153 Fed. 239 (S. D. N. Y. 1907). The statement of the court at page 240, that this was "confessedly a most drastic remedy" calls attention to the fact that it was necessary to avoid the statute to reach the desired result. *Cf.* In re Knopf, 144 Fed. 245 (D. S. C. 1906).

argued that the designation of the trustee does not indicate an intention to exclude any other officer of the court.[14] In view of the fact that a conveyance cannot be deemed "preferential" until adjudication, it seems reasonable to deny the receiver's power to avoid such a transfer.[15] But there is ample reason to allow him to set aside fraudulent conveyances which are void at all times, for the alternative of a creditor's bill, suggested by courts when faced with urgent situations,[16] offers little in preventing dissipation in view of the probable neglect of creditors to take the initiative. And in the event that there is no adjudication of bankruptcy, a suit of this kind would ultimately prejudice a defendant no more than a similar bill instituted by creditors.

EFFECT OF STIPULATIONS RESTRICTING ASSIGNMENTS OF MONEY CLAIMS

IN an action[1] to enforce a claim for wages, which had been assigned to the plaintiff by an employee without the employer's consent,[2] the latter relied in defense upon terms of the employment contract, known to the assignee,[3] which expressly prohibited such an assignment. Although conceding that the assignment might provide grounds for the employee's discharge, the Illinois Supreme Court refused to uphold the stipulation against assignment on the grounds not only that there was no privity of contract between the assignee and the employer,[4] but also that a debtor cannot restrict the assignability of a money claim "any more than he can forbid the sale or pledge of other chattels."

Numerically at least the weight of judicial opinion frowns upon attempts to restrict the assignability of money claims. As in the principal decision, a number of courts have concurred with the United States

[14] It can be safely asserted that it was not the intent of the framers of the statute to give a trustee greater powers than those of the bankruptcy court. *Cf.* Horner-Gaylord v. Miller & Bennett, 147 Fed. 295 (N. D. W. Va. 1906). The receiver has the same rights against a lien as the trustee. Clark v. Huckaby, 28 F. (2d) 154 (C. C. A. 8th, 1928), *certiorari* denied 278 U. S. 648, 49 Sup. Ct. 83 (1928).

[15] See Note (1918) 5 VA. L. REV. 272. By the terms of the act a preference is "voidable by the trustee."

[16] See Guaranty Title & Trust Co. v. Pearlman, *supra* note 2, at 552; Frost v. Latham & Co., 181 Fed. 866, 868 (C. C. S. D. Ala. 1910); *cf.* In re Schrom, 97 Fed. 760 (N. D. Iowa 1899).

[1] State Street Furniture Company v. Armour & Company, 177 N. E. 702 (June 18, 1931—rehearing denied Oct. 9, 1931).

[2] Consent of the debtor to an assignment of the debt is not a condition precedent to suit by the assignee in Illinois. Knight v. Griffey, 161 Ill. 85, 43 N. E. 727 (1896).

[3] Neither court nor counsel seem to have considered the possibility, that by taking an assignment with knowledge of the terms of the employment contract, and the employee's consequent liability to discharge for breach thereof, the plaintiff induced a breach of the employment contract, sufficient either to deny him recovery against the employer, or to grant the employer a counterclaim for the amount of his damage. The analogy to the yellow dog contract cases seems complete. *Cf.* Hitchman Coal & Coke Company v. Mitchell, 245 U. S. 229, 38 Sup. Ct. 65 (1917).

[4] No previous cases have been found which rely on the absence of privity of contract in this situation.

Supreme Court[5] in analogizing a debt to chattels in the hands of the creditor. Upon such reasoning an undertaking to make a promissory note "non-transferable without the written consent of principal and endorsers," and a bank's regulation making drafts payable only to the original depositor presenting the pass-book, have been held ineffectual as against an assignee of the note in the one case,[6] or the pass-book in the other.[7] Decisions nullifying restrictions upon wage assignments have more frequently been reached by importing mandatory implications into statutes making money claims assignable,[8] or by construing the language of restrictive stipulations as too indefinite,[9] or by interpreting them as contemplating only a complete unconditional assignment where the assignment in suit was one for security.[10]

On the other hand, there is respectable authority for the view that, while the power to assign is an incident to ownership of a money claim, the parties may nevertheless curtail that power by freely contracting with reference to it.[11] Thus, stipulations of non-assignability have been held valid defenses in actions by an assignee of a claim for wages,[12] of time-certificates issued to employees for wages,[13] or of trading-stamps issued by a department store to its customers.[14]

If it be assumed that the stipulation against assignment in employment

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[5] Portugese-American Bank of San Francisco v. Welles, 242 U. S. 7, 37 Sup. Ct. 3 (1916).

[6] Weber v. Rosenheim, 37 Ill. App. 72 (1890); Herrick v. Edwards, 106 Mo. App. 633, 81 S. W. 466 (1904).

[7] Bank of United States v. Public Bank of New York City, 88 Misc. 563, 151 N. Y. Supp. 26 (Sup. Ct. 1915). As to the assignability of claims after loss under insurance policies prohibiting assignments, see cases collected in (1928) 56 A. L. R. 1391.

[8] Bewick Lumber Company v. Hall, 94 Ga. 539, 21 S. E. 154 (1894). But see Larue v. Groezinger, 84 Cal. 281, 283, 24 Pac. 42, 43 (1890). See also Note (1915) 24 YALE L. J. 590.

[9] Wabash R.R. v. Smith, 134 Ill. App. 574 (1907).

[10] Inter-Southern Life Insurance Company v. Humphrey, 122 Miss. 579, 84 So. 625 (1919).

[11] The question is equally unsettled with regard to assignments of bilateral contracts. In construction contracts, a provision against the assignability of "the contract" has been construed to invalidate only an assignment of the contractor's duties, but not of the right to moneys due. Bank of Harlem v. City of Bayonne, 48 N. J. Eq. 246, 21 Atl. 478 (1891). *Contra:* City of Omaha v. Standard Oil Company, 55 Neb. 337, 75 N. W. 859 (1898). In contracts for the sale of land, a vendee's assignment in violation of a provision against the assignability of the contract without the vendor's consent, does not excuse the vendor from performance when the vendee's assignee tenders the entire purchase price. Johnson v. Eklund, 72 Minn. 195, 75 N. W. 14 (1898). *Contra:* Lockerby v. Amon, 64 Wash. 24, 116 Pac. 463 (1911).

[12] State v. Kent, 98 Mo. App. 281, 71 S. W. 1066 (1903) (municipal employer).

[13] Tabler, Crudup & Company v. Sheffield Land, Iron, & Coal Company, 79 Ala. 377 (1885); Barringer v. Bes Line Construction Company, 23 Okla. 131, 99 Pac. 775 (1909).

[14] Sperry & Hutchinson Company v. Siegal, Cooper & Company, 309 Ill. 193, 140 N. E. 864 (1923). When the stipulation is waived by the debtor's payment of the claim into court without objection, the assignee is entitled thereto. Fortunato v. Patten, 147 N. Y. 277, 41 N. E. 572 (1895).

contracts is designed for the benefit of the employer alone, to avoid inconvenience in accounts or indecision as to the proper claimant, it is questionable whether the theory of freedom of contract should control where none in fact exists. On the other hand, it may be argued that the stipulation is designed for the protection of the employee as well, in order to discourage the oppressive activities of "loan-sharks" in inducing employees to make an improvident mortgage of their future wages. Such considerations have led in several states to the enactment of statutes which invalidate wage assignments unless accepted by the employer and filed with the town clerk.[15] But the salutary effects of the Uniform Small Loan Law in eliminating the "loan-shark" evil,[16] renders the danger of extortion from wage earners increasingly remote. In any event, where as in the principal case, the assignee is a merchandise creditor of the employee, the result reached by the Illinois court would seem unobjectionable.

PRIORITIES OF MORTGAGES ON AFTER-ACQUIRED PROPERTIES IN CASE OF MERGER

IN 1899 the Minneapolis & St. Louis Railroad mortgaged its lines under an indenture providing for a lien upon all after-acquired property, including subsequently purchased rolling stock. In 1912 it purchased the property of the Iowa Central Railroad and assumed a similar mortgage executed in 1901 upon this line. Thereafter the Iowa division comprising 503 miles and the Minneapolis division comprising 633 miles were operated as a unit. In 1923 the railroad went into receivership. In the years between the sale and the receivership, approximately five million dollars of new rolling stock had been acquired for and used indiscriminately upon the combined divisions. Upon foreclosure of both mortgages the Iowa trustee prayed for an equitable allocation of this rolling stock to the respective liens, but the relief was denied. The court in *Guaranty Trust Company v. Minneapolis & St. Louis R. R.*[1] held that, although the after-acquired property clause of the Iowa mortgage survived the sale,[2] the Minneapolis mortgage was a first lien upon all the acquisitions since it had been executed prior

[15] See Note (1912) 60 U. OF PA. L. REV. 504. In Massie v. Cessna, 239 Ill. 352, 88 N. E. 152 (1909), the Illinois court held a similar statute unconstitutional as an abridgement of employees' property rights, despite the increased possibility of extortion in that state under the rule that even a discharge in bankruptcy does not exonerate the employee from a claim under a prior assignment of future wages. Monarch Discount Company v. Chesapeake Ohio Ry. Co., 285 Ill. 233, 120 N. E. 743 (1918).

[16] See RYAN, USURY AND USURY LAWS (1924) 138.

[1] 52 F. (2d) 418 (C. C. A. 8th, 1931).

[2] The question as to whether the lien had survived was decided on a prior appeal. 36 F. (2d) 747 (1929). The instant appeal is from the decree of foreclosure. For a detailed study of the general question of survivorship of a predecessor company's after-acquired property clause, see Foley and Pogue, *After-Acquired Property Under Conflicting Corporate Mortgage Indentures* (1929) 13 MINN. L. REV. 81; Blair, *The Allocation of After-Acquired Mortgaged Property Among Rival Claimants* (1926) 40 HARV. L. REV. 222. See also Guaranty Trust Co. v. New York & Queens County Ry., 253 N. Y. 190, 199, 170 N. E. 887, 890 (1930), noted in (1931) 44 HARV. L. REV. 472.

in time to the assumption of the Iowa mortgage.[3] Thus while the Iowa mortgage theoretically has a second lien, the practical effect of the decision is to render nugatory its after-acquired property clause since it was conceded that the property is insufficient to pay the Minneapolis debt.

While it is true that the maxim *qui prior est tempore, potior est jure* is ordinarily decisive of the position of respective lienors, it is equally well settled that the rule is applied only where the equities are otherwise equal.[4] In the instant case the equities in favor of the Iowa mortgage bondholders seem to require a nicer adjustment of the problem.[5] The after-acquired property clause was designed to extend the lien to those future replacements and additions necessitated by the obsolescence and wear of the old, so that in the event of foreclosure the value of the road as security would remain intact. A decision that a sale operates to deprive bondholders of this necessary protection denies to them the very thing for which they contracted. A further inequitable result of the decision is to award to the purchaser's mortgagees rolling stock both beyond their needs and in excess of what would have been acquired solely for their own line.

The practical difficulty of a fair allocation in particular cases may be conceded, and yet the mere intricacy of the problem should not preclude its satisfactory disposition. Some broad considerations may be suggested. Where the subsequent acquisitions of the successor company are in the nature of structural improvements or additions to one division, such as bridges, extra trackage or machinery, they should feed the divisional mortgage alone.[6] The addition, however, may be constructed for the use of more than one division, as in the case of a new power house or car barn. Here there should be an allocation based upon the needs of the particular divisions, or in the event that the property is sold, the proceeds should be distributed according to a ratio which would take such needs into account.[7] Rolling stock purchased exclusively for one division or used for the most part thereon should probably not be allocated. But when, as in the instant case, there has been indiscriminate use, the property should be apportioned to

[3] Where the successor has acquired the property of constituent companies through consolidation, as distinct from merger or a sale, the question as to the priority of the respective liens does not arise since the predecessors' mortgages are simultaneously assumed. For a case in which the subsequent acquisitions of a consolidated company were allocated to the respective liens of the predecessor companies, see Citizens Savings & Trust Co. v. Cincinnati & Dayton Traction Co., 106 Ohio St. 577, 140 N. E. 380 (1922). See also Louisville Trust Co. v. Cincinnati Inclined Plane Ry. Co., 91 Fed. 699, 703 (C. C. S. D. Ohio 1897).

[4] 1 POMEROY, EQ. JUR. (4th ed. 1918) § 414. A common instance of where a mortgage executed subsequent in time takes precedence is that of a purchase money mortgage. Harris v. Youngstown Bridge Co., 90 Fed. 322 (C. C. A. 6th, 1898). See Westinghouse Electric & Manufacturing Co. v. Brooklyn Rapid Transit Co., 276 Fed. 152, 161 (S. D. N. Y. 1921). For a collection of cases see Douglas & Shanks, CASES AND MATERIALS ON BUSINESS UNITS, FINANCE (1931) 57, 58.

[5] For a contrary view expressed on a supposititious case similar to the instant one see Foley and Pogue, *op. cit. supra* note 2, at 100.

[6] See Hamlin v. Jerrard, 72 Me. 62, 80 (1881); Guaranty Trust Co. v. New York & Queens County Ry., *supra* note 2, at 206. But see Mississippi Valley Trust Co. v. Southern Trust Co., 261 Fed. 765, 767 (C. C. A. 8th, 1919).

[7] See Citizens Savings & Trust Co. v. Cincinnati & Dayton Traction Co., *supra* note 3, at 609.

the respective divisions on the basis of either mileage, heaviness of traffic, or extent of replacement needs in such a manner as to provide as nearly as possible a balanced equipment for each.[8] A further adjustment may be necessary, however, in a situation where the property has been acquired chiefly through the earnings of one division, for it would be obviously inequitable to apply mechanically any of the above standards without taking this factor into consideration.[9]

EFFECT OF THE INSOLVENCY OF THE ISSUING BANK IN A LETTER OF CREDIT TRANSACTION

THE contracts involved[1] when a buyer promises, in consideration of the issuance of the letter of credit by a bank, to pay it a sufficient amount, one day before maturity, to cover the drafts drawn by the seller are generally stated to be separate and distinct.[2] Proceeding upon this assumption the courts have uniformly allowed a seller who has strictly complied with the terms of the documentary credit, to recover from the issuing bank notwithstanding his breach of the underlying contract of sale.[3] But that the theory of independence is not even here fully accepted is indicated by the fact that the measure of damages for refusal to accept the seller's drafts is that applicable to a breach of the sales contract.[4] Two recent cases illustrate further limitations upon any such theory of independence. In *Seltzer v. Bank of the United States*[5] the bank sued the buyer for the face amount of drafts accepted by it although they had been protested for nonpayment upon presentation and had been taken up by the buyer himself, the bank having been closed by the state superintendent of banks. Arguing that the buyer was liable to it on an independent contract of reimbursement the bank claimed that his obligation was a general asset of the bank and that he was merely a general creditor. The court held that the bank had no cause of action since there was a failure of consideration for the reimbursement contract upon the bank's refusal to pay the drafts.[6] Shortly thereafter, this case was followed by the Circuit Court

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[8] *Ibid.* 616.

[9] *Cf.* Hamlin v. Jerrard, *supra* note 6, at 79.

[1] The typical set-up results in three contracts: that of bank and seller upon issuance of the letter of credit; the underlying contract of sale, and the contract here in question. See Comment (1926) 36 YALE L. J. 245, 246; McCurdy, *Commercial Letters of Credit* (1922) 35 HARV. L. REV. 539, 715; Mead, *Documentary Letters of Credit* (1922) 22 COL. L. REV. 297.

[2] See American Steel Co. v. Irving National Bank, 266 Fed. 41 (C. C. A. 2d, 1920); McCurdy, *op. cit. supra* note 1, at 724; Comment (1926) YALE L. J. 245, 246. But see dissent of Cardozo, C. J., in O'Meara v. National Park Bank of New York, 239 N. Y. 386, 146 N. E. 636 (1925); Note (1925) 9 MINN. L. REV. 657. *Cf.* LLEWELLYN, CASES AND MATERIALS ON SALES (1930) 837 note.

[3] O'Meara v. National Park Bank of New York, *supra* note 2; Note (1925) 39 A. L. R. 755 (1925); Frey & Son v. Sherbourne, 193 App. Div. 849, 184 N. Y. Supp. 661 (1st Dep't 1920); But the bank cannot be reimbursed if it fails to exact strict compliance with the terms of the letter of credit. Bank of Montreal v. Recknagel, 109 N. Y. 482, 17 N. E. 217 (1888); (1928) 38 YALE L. J. 111.

[4] O'Meara v. National Park Bank of New York, *supra* note 2.

[5] 233 App. Div. 225, 251 N. Y. Supp. 637 (1st Dep't 1931).

[6] The court found authority for this reasoning in Leslie v. Bassett, 129

of Appeals, when confronted by the same issue in *Greenough v. Munroe*.[7] In that case the receiver for the bank had demanded that the buyer account for goods or their proceeds held under trust receipts and the seller was threatening action for the price of the goods upon dishonor of its drafts. The buyer petitioned that the funds payable to the receiver be impressed with a trust for the payment of the drafts in the hands of their holders. In granting relief the court concluded that the bank could not complain since it was not entitled to recover from the buyer after repudiating payment of the drafts.

It is apparent that both courts considered the enforceability of the buyer's obligation to be dependent upon the capacity of the bank to perform its contract with the seller. An opposite result could be reached only by assuming that the mere issuance by the bank of the letter of credit is complete performance of its obligation to the buyer.[8] Such an assumption would be contrary both to the recognized function of the bank in financing the sale[9] and to the intention of the parties thereto.[10] It would imply that the seller accepts the bank's obligation in place of the buyer's. It seems better to throw the risk of the bank's insolvency on the buyer, who is more likely to escape unharmed. The bank's disability to perform because of insolvency, accompanied by the receiver's refusal to accede to the buyer's offer to pay the amount of the drafts conditioned upon the receiver paying the seller in full, amounts to an anticipatory breach of contract for which the buyer should have a provable claim for damages.[11] Although

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N. Y. 523, 29 N. E. 834 (1892), which was an action on a draft given to reimburse a bank which had accepted, but not paid, drafts drawn for goods sold to drawer of draft in question. Important letter of credit litigation dates from the World War. The Leslie case is the only one which has been found that presents our precise issue; in cases where the bank has failed to pay for reasons other than insolvency the action is generally by seller against the bank or against the buyer. See Llewellyn's introduction to FINKELSTEIN, LEGAL ASPECTS OF COMMERCIAL LETTERS OF CREDIT (1930).

[7] C. C. A. 2d. Decided Aug. 24, 1931.

[8] Whether a creditor accepts the obligation of a third party given contemporaneously with the creation of the debt as satisfaction is a question of intention. Bell v. Moss, 5 Whart. 189 (Pa. 1890); 3 WILLISTON, CONTRACTS (2d ed. 1926) § 1922; ANSON, CONTRACTS (Corbin's 5th ed. 1930) § 427; FINKELSTEIN, *op. cit. supra* note 6, at 155. The majority view is that the presumption, in absence of proof to the contrary, is one of conditional payment only, whether the obligation given is a negotiable instrument or simple contract. Note (1926) 40 HARV. L. REV. 294. For the suggestion that the relations of the parties resembles the bill of exchange, see Comment (1926) 36 YALE L. J. 245.

[9] The purpose of the letter of credit is to shift the credit strain during transit and resale by the buyer to an agency better qualified to assume it: a commercial bank. Llewellyn, *op. cit. supra* note 6, at XIX; WARD, AMERICAN COMMERCIAL CREDITS (1922) 124, 126, 127; Comment (1925) 34 YALE L. J. 77. The bank is in no sense a purchaser of the goods; it holds merely a security title under the trust receipt. In re James, 30 F. (2d) 555 (C. C. A. 2d, 1929); Comment (1923) 32 YALE L. J. 602.

[10] See Note (1926) 40 HARV. L. REV. 294. The use of the "acceptance" instead of payment on sight is for the benefit of the buyer. It cannot be presumed that the seller is willing to take the risk of the issuing bank's insolvency. In accord with sound business practice he desires both the obligation of the bank and buyer. See WARD, *op. cit. supra* note 8, at 196.

[11] Central Trust Co. v. Chicago Auditorium Association, 240 U. S. 581,

in the instant cases the buyer can show no such injury, in a transaction calling for payment by the bank on sight the latter should be liable for the profits the buyer would have realized on the deal. Moreover, in the case of an acceptance by the bank, if the seller has recovered from the buyer on the original contract of sale, the buyer at least should have his legal costs from the bank.

ADMINISTRATIVE EXPENSES OF RECEIVERSHIP—JUDGMENT FOR WRONGFUL ATTACHMENT DEFENDED BY RECEIVER

A WIFE sued in replevin in the Wisconsin state courts[1] against a national bank for the wrongful attachment of her property in a suit instituted by the bank against her husband, who was subsequently adjudicated a bankrupt. His creditors, including the plaintiff and the bank, stipulated that his trustee in bankruptcy should sell the attached property and then intervene in the replevin suit, holding the proceeds pending the outcome. Meanwhile, the bank became insolvent and a receiver was appointed who intervened to defend it. The state court held that the attachment was illegal, and gave judgment against the receiver.[2] In *Bereth v. Sparks*[3] the Federal Circuit Court held the Wisconsin judgment to be an administrative expense of the receivership, thereby entitling it to priority in payment over the general creditors.[4] The theory was that the receiver, by defending in place of the bank, ratified the tort of the bank, and became a joint tortfeasor *ab initio*.

A receiver is not liable even in his representative capacity for claims against an insolvent arising prior to his appointment, and a judgment therefor, even though entered against him as a formal party defendant, gains no priority over similar claims.[5] It is merely conclusive evidence of a general claim against the fund.[6] However, administrative expenses of a receivership are entitled to priority in payment, and include satisfaction for the tortious acts of the receiver or his agents[7] committed within the

36 Sup. Ct. 412 (1916); Pennsylvania Steel Co. v. New York City Railways Co., 198 Fed. 721 (C. C. A. 2d. 1912). See Ballantine, *Anticipatory Breach and the Enforcement of Contractual Duties* (1923) 22 MICH. L. REV. 329, 342.

[1] Sparks v. Kuss, 195 Wis. 378, 216 N. W. 929 (1927).

[2] Sparks v. First National Bank of Crandon, 200 Wis. 647, 228 N. W. 915 (1930).

[3] 51 F. (2d) 441 (C. C. A. 7th, 1931).

[4] See CLARK, RECEIVERS (2d ed. 1929) § 637.

[5] National Bank of Augusta v. Warren, 101 S. C. 453, 86 S. E. 21 (1914); *cf.* Bank of Bethel v. Pahquioque Bank, 81 U. S. 383 (1871); Green v. Walkill National Bank, 7 Hun. 63 (N. Y. 1876).

[6] Riehle v. Margolies, 279 U. S. 218, 49 Sup. Ct. 310 (1929); Beach, *Judgment Claims in Receiverships* (1921) 30 YALE L. J. 674. *Contra:* Attorney General v. Supreme Council A. L. H., 196 Mass. 151, 81 N. E. 966 (1907).

[7] McNulta v. Lochridge, 141 U. S. 327, 12 Sup. Ct. 11 (1891) (receiver held for predecessor's acts); Gray v. Grand Trunk Western Railway Co., 156 Fed. 736 (C. C. A. 7th, 1907) (subsequent purchaser liable); Hanlon v. Smith, 175 Fed. 192 (C. C. N. D. Iowa 1909); Bartlett v. Cicero Light, Heat & Power Co., 177 Ill. 68, 52 N. E. 339 (1898) (corporation liable after receivership). But see Hopkins v. Connel, 2 Tenn. Ch. 323, 325 (1875)

scope of his duties.[8] Thus a receiver has been held responsible as a representative of the estate for obtaining an injunction without cause against the removal of property,[9] or for misrepresentation at a sale of assets.[10] Moreover, when he continues some tortious act begun by the corporation prior to his appointment he can be held to have ratified it so as to become a tort-feasor thereby.[11] But while the plaintiff in an attachment suit may ratify a wrongful levy so as to be liable in tort for the injury,[12] one who assists in defending a wrongful attachment seems to be liable as a "joint tort-feasor" only when he is also an attaching creditor under a subsequent writ, and when actual possession of property is thereby withheld.[13] The receiver in the instant case could hardly have ratified or joined in the attachment since the possession of the property was in the hands of the husband's trustee in bankruptcy before he intervened. To give preference to a claim for tort against an insolvent corporation because of purely defensive action on the part of its receiver, undertaken in accord with his duty to test the validity of claims against the fund in his trust, is to place a serious obstacle in the way of beneficial receivership administration.

LIABILITY OF RECEIVER OF CORPORATION FOR STATE FRANCHISE TAX

IN *Michigan Trust Company v. People*,[1] the Circuit Court of Appeals for the sixth circuit held that the receiver of a mercantile corporation was under no obligation to pay a tax levied by the state of Michigan against the corporation "for the privilege of exercising its franchise and of transacting its business within [the] state" during the period in which he operated the business. Although the validity of such a tax in the case of a public utility receivership was admitted,[2] the court reasoned that where

(receiver as public agent). But *cf.* State of North Carolina v. Norfolk and Southern Ry. Co., 152 N. C. 785, 67 S. E. 42 (1910) (corporation not liable for receiver's misdemeanor).

8 Brazelton & Johnson v. J. I. Campbell Co., 49 Tex. Civ. App. 218, 108 S. W. 770 (1908); Fryar v. Hazelwood Holstein Farms, 97 Wash. 78, 165 Pac. 1084 (1917). A receiver can usually be held individually on his bond if he is not liable in his representative capacity. *Cf.* Gutsch v. McIlhargey, 69 Mich. 377, 37 N. W. 303 (1888) (replevin suit in which the court held the receiver liable but left it to the appointing court to decide whether the liability was not merely individual but representative instead).

9 Cox v. Stone, 146 La. 81, 83 So. 385 (1919).

10 Coe v. Patterson, 122 App. Div. 76, 106 N. Y. Supp. 659 (4th Dep't 1907).

11 Ratcliff v. Adler, 71 Ark. 269, 72 S. W. 896 (1903).

12 Cole v. Edwards, 52 Neb. 711, 72 N. W. 1045 (1897); Frick-Reid Supply Co. v. Hunter, 47 Okla. 151, 148 Pac. 83 (1915).

13 First National Bank of Pawnee City v. Avery Planter Co., 69 Neb. 329, 95 N. W. 622 (1903); Koch v. Peters, 97 Wis. 492, 73 N. W. 25 (1897).

1 U. S. Daily, Oct. 28, 1931, at 1956. The receiver was appointed in February, 1926, and conducted the business until December, 1929, when all mercantile assets were sold.

2 Accord: State v. Bradley, 207 Ala. 677, 93 So. 595 (1922); Armstrong v. Emmerson, 300 Ill. 54, 132 N. E. 768 (1921); State v. Sessions, 95 Kan. 272, 147 Pac. 789 (1915); Harvey v. Bay State Street Railway, 234 Mass.

the nature of the business was such that it might be engaged in "by any other citizen, in total disregard of the corporate capacity of the former possessor, and without any reliance whatever upon its franchises," the tax could not be levied.

Although the Supreme Court has held that the federal act imposing an excise "with respect to the carrying on or doing business" applies only where the business is carried on by the corporation itself,[3] imposition of state franchise taxes has been uniformly sustained when the business is conducted by a receiver whether it be of a mercantile or public utility nature.[4] The rule is generally otherwise where the corporation has been enjoined from transacting the business for which it was incorporated, and a receiver has been appointed for the purpose of winding up its affairs.[5] But in New Jersey it seems that a tax may be laid upon the franchise even though its exercise has been prohibited.[6] The specious distinction adopted in the instant case has been ignored in a number of cases involving the operation of mercantile corporations by receivers, and in others it has been expressly rejected.[7] Nor does the theory of the receiver's status lend support to the decision. For it is well established that, in the absence of statute, the legal existence of a corporation, regardless of the nature of its business, is neither terminated nor suspended by the appointment of a receiver,[8] and where the receiver proceeds to carry on the business he acts as the corporation to the same extent, *pro hac vice*, as if the board of directors were in charge.[9]

336, 125 N. E. 614 (1920); Central Trust Co. v. New York City & N. R. Co., 110 N. Y. 250, 18 N. E. 92 (1888).

3 United States v. Whitbridge, 231 U. S. 144, 34 Sup. Ct. 24 (1913). In In re Detroit Properties Corporation, 236 N. W. 850, 852 (Mich. 1931), the decision in the Whitbridge case was said to be "a special construction of a special law with a special background and was not founded upon, and did not establish, general principles applicable to other laws."

4 People v. Hopkins, 18 F. (2d) 731 (C. C. A. 2d, 1927); Gerke Brewing Co. v. Kuerze, 7 Ohio App. 37 (1916); The Guardian Savings & Trust Co. v. The Templar Motor Co., 116 Ohio St. 95, 155 N. E. 691 (1927); cases cited *infra* note 7.

5 Ohio v. Harris, 229 Fed. 892 (C. C. A. 6th, 1916); Johnson v. Johnson Brothers, 108 Me. 272, 80 Atl. 741 (1911); Commonwealth v. Lancaster Savings Bank, 123 Mass. 493 (1877); State v. Bradford Savings Bank & Trust Co., 71 Vt. 234, 44 Atl. 349 (1899) (tax construed to be one on doing business).

6 In re United States Car Co., 60 N. J. Eq. 514, 43 Atl. 673 (1899).

7 In re Detroit Properties Corporation, *supra* note 3; see Providence Engineering Corporation v. Downey Shipbuilding Corporation, 8 F. (2d) 304, 308 (E. D. N. Y. 1925); In re George Mather's Sons Co., 52 N. J. Eq. 607, 610, 30 Atl. 321, 322 (1894).

8 2 CLARK, RECEIVERS (2d ed. 1929) §§ 703, 707-709. That the appointment of a receiver does not destroy the corporation is further shown by the fact that even after the appointment the board of directors may have the power to act in certain matters as, for example, to pass a resolution authorizing the bankruptcy of the corporation and to file the same. See 2 CLARK, *op. cit. supra*, §§ 708, 767.

9 See Central Trust Co. v. New York City & N. R. Co., *supra* note 2; In re Detroit Properties Corporation, *supra* note 3.

OBSOLESCENCE AND REPLACEMENT DEDUCTIONS FTOM TAXABLE INCOME

IN order to meet a heavy increase in traffic and the active competition of other lines, the Kansas City Southern Railway, in the years 1909-1912, proceeded at great expense to eliminate certain grades by substituting sections of new road for portions of the old, and to construct a new shop and terminal plant, concurrently abandoning the one formerly used. The Interstate Commerce Commission ordered the company to charge the estimated cost of these replacements, less salvage, to operating expenses, and the validity of the order was subsequently sustained by the Supreme Court.[1] To avoid an undue burdening of its operating costs account for one year, the railroad then made application for, and was granted, permission by the Commission to allocate the charges over a fifteen year period. In making its tax returns for 1918 and 1919 the railroad sought to take advantage of these circumstances by claiming the aliquot amounts for each year as tax free items, either as deductions from net income as a reasonable allowance for obsolescence,[2] or on the unique theory that the sums were restorations of capital assets and as such not taxable income within the Sixteenth Amendment. The decision of the Board of Tax Appeals disallowing the claims was affirmed on appeal.[3]

Although the section of the Revenue Act under which the railroad made its claim for obsolescence does not specify the year in which the deduction is to be made, the court's refusal to extend the scope of the statute to permit a corporation to make a subsequent deduction for property abandoned in former years is well-founded. The Revenue Acts are premised upon the adoption of annual accounting periods and are designed to secure an accurate representation of yearly gains and losses as a basis for a tax on yearly income.[4] To indicate the true annual income, proportionate yearly deductions for predictable obsolescence and depreciation are properly made, inasmuch as a portion of the loss is attributable to each year in which the property is in use.[5] Similarly, if the obsolescence is not definitely predictable or occurs suddenly, no proration of the loss over a period of years having been possible,[6] the entire deduction may be made in the single year in which the loss becomes evident.[7] But to permit the taxpayer to make the deduction in years subsequent to those in which the obsolescence accrued would be to allow him to distort his actual income by giving him his choice as to when he will take his loss, a clear contravention of the

[1] Kansas City Southern Ry. v. United, 231 U. S. 423, 34 Sup. Ct. 125 (1913).

[2] Revenue Act of 1918, 40 STAT. 1057, c. 18, § 234 (a) (7).

[3] Kansas City Southern Ry. v. Commissioner of Internal Revenue, 52 F. (2d) 372 (C. C. A. 8th, 1931).

[4] See De Loss v. Commissioner of Internal Revenue, 28 F. (2d) 803, 805, (C. C. A. 2d, 1928); MONTGOMERY, INCOME TAX PROCEDURE (1923) 85.

[5] See Gambrinus Brewing Co. v. Anderson, 282 U. S. 638, 642, 643, 51 Sup. Ct. 260, 261 (1931); Burnet v. Niagara Brewing Co., 282 U. S. 648, 51 Sup. Ct. 262 (1931); Corsicana Gas & Electric Co. v. Commissioner of Internal Revenue, 6 B. T. A. 565 (1927); HOLMES, FEDERAL INCOME TAX (6th ed. 1925) § 585.

[6] Appeal of Columbia Malting Co., 1 B. T. A. 999 (to entitle the taxpayer to proportionate yearly reductions there must be substantial reasons for believing that the property will become obsolete, and a reasonable degree of certainty as to when that event will occur).

[7] Appeal of Dilling Cotton Mills, 2 B. T. A. 127 (1925); HOLMES, *op. cit. supra* note 5, at 590.

basal theory of a taxable year. The Commission's order in the instant case, was undoubtedly valid for its own purposes,[8] but to sustain the contention of the railroad that it also constituted a conclusive determination for tax purposes would give the Commission power, through accounting regulations, to set standards for the taxing authorities subversive of those they themselves had promulgated.

The plaintiff's alternative theory that the annual allocations were non-taxable as a restoration of capital disregards the rule that the test of income is its source, not the purpose for which it is subsequently used.[9] Although the allowance of deductions for obsolescence and depreciation is intended to and does permit the taxpayer to build up an untaxed reserve for replacement of such capital losses,[10] no authority can be found holding these sums of themselves tax free as restorations of capital. Such a procedure would give the taxpayer a double deduction, first when the property became obsolete, and again when he made provision for replacement.

STATUTE OF FRAUDS—PROMISES TO ANSWER FOR THE DEBT OF ANOTHER

IN *Witschard v. Brody & Sons*,[1] the New York Court of Appeals has recently held that an oral agreement by the owner of a building in process of construction to guarantee the credit of the general contractor in consideration of the resumption of deliveries by the promisee material man was unenforcible as a promise to answer for the default of another within the Statute of Frauds. The decision is at variance with the weight of authority, which excludes this type of transaction from the operation of the Statute.[2] The promise of the owner has been sometimes construed to come within the rule that a promise to pay out of the funds of the principal debtor is not within the Statute,[3] despite the absence of any specific reference to the source of payment.[4] It is, however, most frequently brought within the purview of the receipt of benefit, or leading purpose rules, which except a promise when the consideration therefor is new and original, moving between the newly contracting parties.[5] This new consideration must in most jurisdictions be beneficial to the promisor rather than merely detrimental to the promisee.[6] New York, among others, has further required that the promisor must have an "independent duty of

[8] See Kansas City Southern Ry. v. United States, *supra* note 1, at 452, 34 Sup. Ct. at 134, 135.

[9] *Cf.* cases cited in Note (1926) 10 MINN. L. REV. 270. The case of Edward v. Cuba R. R., 268 U. S. 628, 45 Sup. Ct. 614 (1925), cited by the plaintiff in support of its theory, was properly distinguished by the court in the instant case, at 378.

[10] See United States v. Ludey, 274 U. S. 295, 300, 301, 47 Sup. Ct. 608, 610 (1927).

[1] 257 N. Y. 97, 177 N. E. 385 (1931).

[2] I WILLISTON, CONTRACTS (2d. ed. 1920) § 481.

[3] *Ibid.*

[4] Robinson & Son Contracting Co. v. Twin City Bank, 103 Ark. 219, 146 S. W. 523 (1912); see Halstead v. Pelletreau, 101 App. Div. 125, 128, 91 N. Y. Supp. 927, 929 (2d Dep't 1905).

[5] Raabe v. Squier, 148 N. Y. 81, 42 N. E. 516 (1895); Howell v. Harvey, 65 W. Va. 310, 64 S. E. 249 (1909); Note (1909) 22 L. R. A. (N. S.) 1077.

[6] Davis v. Patrick, 141 U. S. 479, 12 Sup. Ct. 58 (1891); see 1 WILLISTON, CONTRACTS (2d. ed. 1920) § 472.

payment",[7] a requirement which merely assumes the result, since if the promisor has no independent duty, his promise is necessarily to answer for the debt of another.

The court in the instant case adopts a formula suggested by Professor Williston and inquires whether the promisor is "a surety." Under this test the promisee is within the Statute if as between the promisor and the original debtor the latter "ought to pay." [8] And since it is here held that "beneficial consideration" received by the promisor did not remove the "ought" from the principal debtor's obligation to pay, it would follow that the receipt of benefit and leading purpose rules as heretofor applied,[9] are definitely abandoned. Apparently under the rule of the principal case, the consideration necessary to take the promise out of the Statute must be the substantial equivalent of the performance promised, *i.e.*, of the debt, since where the benefit received is so equivalent, the principal debtor has no further obligation with regard to the debt.[10] And since the purpose of the Statute is to require satisfactory evidence of certain contracts,[11] this rule seems consistent with logic and legislative purpose. Nor is it unnecessarily harsh, since business practice requires such contracts to be in writing.

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[7] White v. Rintoul, 108 N. Y. 222 (1888).

[8] 1 WILLISTON, CONTRACTS, (2d. ed. 1920) § 475.

[9] These rules are normally exclusive of the idea that the consideration received by the promisor should be the substantial equivalent of the debt, and refer merely to a consideration equivalent to the risk that the promisor may be compelled to pay. See I WILLISTON, CONTRACTS (2d. ed. 1920) § 473.

[10] See Fullam v. Adams, 37 Vt. 391, 401 (1864).

[11] See The Richardson Press v. Allbright, 224 N. Y. 497, 502, 121 N. E. 362, 364 (1918).