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BANKRUPTCY - RIGHTS OF TRUSTEE AS AGAINST MORTGAGEE UNDER MORTGAGE CONTAINING AFTER-ACQUIRED PROPERTY CLAUSE

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BANKRUPTCY — RIGHTS OF TRUSTEE AS AGAINST MORTGAGEE UNDER MORTGAGE CONTAINING AFTER-ACQUIRED PROPERTY CLAUSE — A mortgage, containing an after-acquired property clause which described specifically many kinds of property which should pass under it when acquired, was given to bondholders as part of a refunding mortgage. Several mortgages were subsequently executed to the mortgagees covering some of the after-acquired property. After the intervention of bankruptcy a dispute arose between the mortgagees and the trustee over the right to possession of certain property not covered by the later mortgages and in the possession of the bankrupt at the time of the adjudication. *Held*, under section 47a(2)[1] of the Bankruptcy Act, the trustee takes the property as against the mortgagee. *In re National Cottonseed Products Corp.*, (D. C. Tenn. 1940) 34 F. Supp. 438.[2]

In view of the long line of federal decisions holding that the court must look to the state law to determine the force and effect of an after-acquired property clause in a mortgage as against a trustee in bankruptcy,[3] it is impossible to explain the complete absence in the decision of any reference to the law of Tennessee. But it is very doubtful if the result of the case would have been changed by reference to the state law. The Tennessee decisions give effect to

[1] 36 Stat. L. 838 at 840 (1910), 11 U. S. C. (1934), § 75a(2), re-enacted with a slight addition by 52 Stat. L. 840 at 881 (1938), 11 U. S. C. (Supp. 1939), § 110c. See infra at note 19.

[2] The nature of the property involved is not disclosed in the opinion and it is difficult to understand why it was not covered by the after-acquired property clause in view of the broad provisions quoted in the decision. However, the trustee admitted the validity of the clause as to property specifically described, and as to fixtures placed on the property so described, and admitted that as to other property it constituted a binding obligation to give a mortgage which could be specifically enforced. Presumably only property falling within this latter category was involved in the case.

[3] Thompson v. Fairbanks, 196 U. S. 516, 25 S. Ct. 306 (1905); Humphrey v. Tatman, 198 U. S. 91, 25 S. Ct. 567 (1905); Preetorious v. Anderson, 150 C. C. A. (5th) 55, 236 F. 723 (1916); In re Furness, (C. C. A. 2d, 1935) 75 F. (2d) 965; In re Cobb, (D. C. Mich. 1936) 14 F. Supp. 465; In re Downtown Athletic Club of New York City, (D. C. N. Y. 1936) 18 F. Supp. 712; The Fort Orange, (D. C. N. Y. 1933) 5 F. Supp. 833; In re Alabama Braid Corp., (D. C. Ala. 1935) 13 F. Supp. 336.

after-acquired property clauses at least as between the parties,[4] but have held that the rights of a judgment creditor are superior to the rights of the mortgagee under such a clause.[5] Since under section 47a(2) the trustee has been held to be in the position of an attaching creditor,[6] under the law of Tennessee he would be entitled to the possession of the property. The result would be different in states which hold that the mortgagee's equity is cut off only by bona fide purchase for value.[7] Prior to the enactment of section 47a(2) in 1910,[8] the trustee was generally limited to the title and interest which the bankrupt himself, or his creditor, had in his property. Although an early case involving an after-acquired property clause adhered to this position strictly,[9] the courts generally tended to favor the trustee over the equitable lienor even before the 1910 amendment to the Bankruptcy Act.[10] Section 47a(2), now 70c,[11] gives the trustee the power to claim the property in his own right in all states which hold that the rights of an attaching creditor are superior to the rights of the mortgagee under the after-acquired property clause. Although one case [12] which arose soon after the amendment of 1910 required the trustee to show that there was some creditor of the bankrupt holding a lien superior to that of the mortgagee, that element has not been discussed in any of the later cases. There are two situations where section 70c will not avail the trustee: first, when the mortgagee has taken possession or when a subsequent mortgage covering the after-acquired property has been executed before the filing of the petition; [13] second, where the state law gives the mortgagee a preference over attaching creditors. But the property may still pass to the trustee under other sections of the act. In both situations, the trustee may be able to set aside the transfer of the after-acquired property as preferential under section 60b [14] if the transfer was made within four months of the filing of the petition.[15] It makes no difference that the trans-

[4] McClung, Buffat & Buckwell v. Quincy Carriage & Wagon Co., 117 Tenn. 250, 96 S. W. 960 (1906); Grosvenor v. Bethell, 93 Tenn. 577, 26 S. W. 1096 (1894); Judge v. Jones, 99 Tenn. 20, 42 S. W. 4 (1897).

[5] Phelps, Dodge & Co. v. Murray, 2 Tenn. Ch. 746 (1877); Tennessee National Bank v. Ebbert & Co., 56 Tenn. 153 (1872).

[6] In re Jeandros Dye & Print Works, (D. C. Mass. 1938) 22 F. Supp. 26.

[7] In re Alabama Braid Corp., (D. C. Ala. 1935) 13 F. Supp; In re Allee, (C. C. A. 7th, 1932) 55 F. (2d) 76. Cohen and Gerber, "The After-Acquired Property Clause," 87 UNIV. PA. L. REV. 635 at 646 (1939).

[8] See COLLIER, BANKRUPTCY, 4th ed., (Gilbert) 699-703 (1937), for the historical background of § 47a(2).

[9] Mitchell v. Winslow, (C. C. Me. 1843) 17 F. Cas. No. 9,673.

[10] In re Hurley, (D. C. Mass. 1910) 185 F. 851; In re Marine Construction & Dry Dock Co., (C. C. A. 2d, 1906) 144 F. 649. Williston, "Transfers of After-Acquired Personal Property," 19 HARV. L. REV. 557 at 575-579 (1906).

[11] See note 1, supra.

[12] In re Flatland, (C. C. A. 9th, 1912) 196 F. 310. But see In re Whatley Bros., (D. C. Ga. 1912) 199 F. 326, expressly disagreeing with In re Flatland.

[13] Hayes v. Gibson, (C. C. A. 3d, 1922) 179 F. 812.

[14] 52 Stat. L. 870 (1938), 11 U. S. C. (Supp. 1939), § 96(b).

[15] Hayes v. Gibson, (C. C. A. 3d, 1922) 279 F. 812; In re Alabama Braid Corp., (D. C. Ala. 1935) 13 F. Supp. 336; Corney v. Saltzman, (C. C. A. 2d, 1927) 22 F. (2d) 268. There are several situations where § 60b will apply. There is a prefer-

fer was effectuated or the mortgage executed pursuant to an agreement entered into more than four months before bankruptcy.[16] In the first situation in states where an attaching creditor would prevail over the mortgagee, the trustee would take the title under section 70a (5).[17] The result of the principal case would not be altered by the law as amended in 1938.[18] Section 47a(2) was transferred to section 70c and the phrase "whether or not such a creditor actually exists" was added.[19] Since it was not required before the change that the trustee produce a creditor with a lien superior to that of the mortgagee,[20] the change seems merely to make the existing law more definite and certain.

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ential transfer if a mortgage expressly carrying after-acquired property is executed within four months of the filing of the petition or if the mortgagee takes possession within the four-month period.

[16] In re Traut's Estate, (C. C. A. 8th, 1924) 297 F. 458; Hayes v. Gibson, (C. C. A. 3d, 1922) 279 F. 812; Grandison v. National Bank of Commerce of Rochester, (C. C. A. 2d, 1916) 231 F. 800. For a complete discussion and collection of cases, see 22 A. L. R. 1372 at 1378 (1923). The acquisition of property is an act of bankruptcy under § 3a(2), 52 Stat. L. 844 (1938), 11 U. S. C. (Supp. 1939), § 21a(2), in states which hold that the property automatically becomes subject to the lien of the mortgage when acquired. In other states an act of bankruptcy would be committed if the mortgagee took possession or if a subsequent mortgage were executed to cover specifically the after-acquired property.

[17] In re Hurley, (D. C. Mass. 1910) 185 F. 851; Williston, "Transfers of After-Acquired Personal Property," 19 HARV. L. REV. 557 at 579 (1906).

[18] The case was decided under the law as it existed prior to 1938.

[19] 52 Stat. L. 881 (1938), 11 U. S. C. (Supp. 1939), § 110(c). Before 1938 the courts were in agreement that § 47a(2) was logically out of place and had consistently construed it in connection with § 70. In re Hammond, (D. C. Ohio, 1911) 188 F. 1020; Ignatius v. Farmers' State Bank of Havre, Montana, (C. C. A. 9th, 1921) 272 F. 33.

[20] See note 12, supra.