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## Bankruptcy - Summary Jurisdiction - Filing Proof of Claim as Basis for Money Judgment on a Counterclaim in Favor of the Trustee

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## RECENT DECISIONS

BANKRUPTCY — SUMMARY JURISDICTION — FILING PROOF OF CLAIM AS BASIS FOR MONEY JUDGMENT ON A COUNTERCLAIM IN FAVOR OF THE TRUSTEE — Appellant filed a proof of claim with the trustee in bankruptcy for unliquidated damages for an alleged breach of contract by the bankrupt. In response, the trustee filed a petition with the bankruptcy court for an order disallowing the appellant's claim and for a money judgment against appellant for a breach of the same contract.<sup>1</sup> The district court affirmed the referee's denial of appellant's claim and judgment in favor of the trustee.<sup>2</sup> On appeal, *held*, affirmed. Filing proof of claim gives the bankruptcy court jurisdiction not only to hear, but to grant the trustee's petition for affirmative relief on a counterclaim arising out of the same transaction. *Peters v. Lines*, 275 F.2d 919 (9th Cir. 1960).

In proceedings instituted under the Bankruptcy Act<sup>3</sup> the federal district court may act as a bankruptcy court presided over by a judge or referee with jurisdiction to decide summarily controversies pertaining to the collection of a bankrupt's estate.<sup>4</sup> In the exercise of its jurisdiction to hear civil cases, as distinguished from proceedings under the Bankruptcy Act, the federal district court may also entertain cases brought by a trustee or receiver.<sup>5</sup> However, the bankruptcy court may not decide cases brought by a trustee unless the bankrupt could have prosecuted his suit in the bankruptcy court without having instituted proceedings under the Bankruptcy Act, or unless the defendant consents to the bankruptcy court's summary jurisdiction.<sup>6</sup> In the principal case, the bankrupt could not have brought an action for breach of contract in the bankruptcy court because the appellant was asserting a bona fide adverse claim and the property involved was not within the court's possession;<sup>7</sup> therefore, the availability of that forum to the trustee, even though he brought the action by means of a counterclaim, depends upon the consent of the adverse claimant.<sup>8</sup> The right of an adverse claimant to a plenary hearing is procedural and may be waived.<sup>9</sup> The courts agree that the filing of a proof of claim is a sufficient manifestation of consent to give the bankruptcy court summary

<sup>1</sup> Bankruptcy Act § 57 (d), as amended, 52 Stat. 866 (1938), 11 U.S.C. § 93 (d) (1958).

<sup>2</sup> In the Matter of Snow Camp Logging Co., 168 F. Supp. 420 (N.D. Cal. 1958).

<sup>3</sup> 30 Stat. 544 (1898), as amended, 11 U.S.C. §§ 1-1103 (1958).

<sup>4</sup> Bankruptcy Act § 2 (7), 30 Stat. 545 (1898) [amended by 66 Stat. 422 (1952)], as amended, 11 U.S.C. § 11 (a) (7) (1958).

<sup>5</sup> 28 U.S.C. §§ 1331-32 (1958).

<sup>6</sup> Bankruptcy Act § 23 (b), as amended, 52 Stat. 854 (1938), 11 U.S.C. § 46 (b) (1958).

<sup>7</sup> Bankruptcy Act § 23 (a), as amended, 52 Stat. 854 (1938), 11 U.S.C. § 46 (a) (1958). See generally 2 COLLIER, BANKRUPTCY § 23.04 (14th ed. 1940, Supp. 1960).

<sup>8</sup> Bankruptcy Act § 23 (b), as amended, 52 Stat. 854 (1938), 11 U.S.C. § 46 (b) (1958).

<sup>9</sup> *Harris v. Avery Brundage Co.*, 305 U.S. 160 (1938); *MacDonald v. Plymouth County Trust Co.*, 286 U.S. 263 (1932). A plenary hearing is a formal civil trial including the right to a jury trial in an appropriate case. See 2 COLLIER, *op. cit. supra* note 7 § 23.02.2.

jurisdiction to decide the claim on its merits.<sup>10</sup> As a defense, the trustee may seek to reduce or extinguish this claim through recoupment or set-off.<sup>11</sup> However, where the trustee seeks to interpose a counterclaim, some courts have decided that the mere filing of a proof of claim is insufficient consent to allow a money judgment against the adverse claimant.<sup>12</sup> In these courts the counterclaim can be used only to extinguish the adverse claim, requiring the trustee to bring a plenary action in the state or federal district court if he wishes to recover the full amount of the counterclaim.<sup>13</sup> However, many recent decisions have held that the filing of a proof of claim is sufficient to give the bankruptcy court jurisdiction not only to hear and allow the defensive use of the trustee's counterclaim, but also to render a money judgment in his favor.<sup>14</sup> The Federal Rules of Civil Procedure, which have been made applicable to bankruptcy proceedings,<sup>15</sup> provide for the liberal use of counterclaims; however, many cases, just as the principal case, have limited the bankruptcy court's summary jurisdiction to compulsory counterclaims.<sup>16</sup> On the other hand, the use of the federal rules have led a few courts to affirm judgments allowing the trustee affirmative relief on a counterclaim which does not arise out of the same transaction.<sup>17</sup> The Federal Rules are not a source of jurisdiction for the

<sup>10</sup> *In re Muntz TV*, 225 F.2d 493 (7th Cir. 1955); *Coffman v. Cobra Mfg. Co.*, 214 F.2d 489 (9th Cir. 1954); *Britton v. Western Iowa Co.*, 9 F.2d 488 (8th Cir. 1925).

<sup>11</sup> *Coffman v. Cobra Mfg. Co.*, *supra* note 10; *In re Blake*, 150 Fed. 279 (8th Cir. 1906); Bankruptcy Act § 68, as amended, 52 Stat. 878 (1938), 11 U.S.C. § 108 (1958).

<sup>12</sup> *In the Matter of Prima Co.*, 98 F.2d 952 (7th Cir. 1938), *cert. denied*, 305 U.S. 658 (1938); *Fitch v. Richardson*, 147 F. 197 (1st Cir. 1906); *In re Houston Seed Co.*, 122 F. Supp. 340 (N.D. Ala. 1954); *In re Florsheim*, 24 F. Supp. 991 (S.D. Cal. 1938); *In re Pennsylvania Coffee Co.*, 8 F.2d 98 (W.D. Pa. 1925).

<sup>13</sup> Principal case at 925. See generally 4 COLLIER, *op. cit. supra* note 7, § 68.20.

<sup>14</sup> *Continental Cas. Co. v. White*, 269 F.2d 213 (4th Cir. 1959); *Inter-state Nat'l Bank v. Luther*, 221 F.2d 382 (10th Cir. 1955), *petition for cert. dismissed*, 350 U.S. 944 (1956), 69 HARV. L. REV. 377, 5 DUKE B.J. 149; *In re Solar Mfg. Corp.*, 200 F.2d 327 (3d Cir. 1952), *cert. denied*, 345 U.S. 940 (1953); *In re Petroleum Conversion Corp.*, 196 F.2d 728 (3d Cir. 1952), *cert. denied*, 344 U.S. 917 (1953), *affirming* 99 F. Supp. 899 (D. Del. 1951); *Columbia Foundry Co. v. Lochner*, 179 F.2d 630 (4th Cir. 1950), N.Y.U.L. REV. 893; *Chase Nat'l Bank v. Lyford*, 147 F.2d 273 (2d Cir. 1945); *Floro Realty & Inv. Co. v. Steem Elec. Corp.*, 128 F.2d 338 (8th Cir. 1942); *Florance v. Kresge*, 93 F.2d 784 (4th Cir. 1938); *In the Matter of Frederick Motors Co.*, 177 F. Supp. 758 (E.D. Ky. 1959); *In the Matter of Freas*, 176 F. Supp. 230 (S.D. Ind. 1959); *In the Matter of Barnhart Motors*, 142 F. Supp. 845 (N.D. Ohio 1956); *cf. Alexander v. Hillman*, 296 U.S. 222 (1935). However, affirmative relief may not be given on a counterclaim brought against the United States. *United States v. United States Fid. & Guar. Co.*, 309 U.S. 506 (1940); *Danning v. United States*, 259 F.2d 305 (9th Cir. 1958), 4 VILL. L. REV. 430 (1959); *In re Greenstreet*, 209 F.2d 660 (7th Cir. 1954).

<sup>15</sup> General Order No. 37, 305 U.S. 698 (1939).

<sup>16</sup> *Daniel v. Guaranty Trust*, 285 U.S. 154 (1932); *In the Matter of Majestic Radio & Television Corp.*, 227 F.2d 152 (7th Cir. 1955), 65 YALE L.J. 694 (1956); *B. F. Avery & Sons Co. v. Davis*, 192 F.2d 255 (5th Cir. 1951), *cert. denied*, 342 U.S. 945 (1952); *FED. R. CIV. P. 13 (a)*.

<sup>17</sup> *Inter-state Nat'l Bank v. Luther*, 221 F.2d 382 (10th Cir. 1955), *petition for cert. dismissed*, 350 U.S. 944 (1956); *FED. R. CIV. P. 13 (b)*.

bankruptcy court;<sup>18</sup> however, the filing of a proof of claim may form the basis for a reasonable implication that the claimant has consented to the summary jurisdiction of the court and the rules of procedure which govern its operation. Accordingly, the bankruptcy court should be able to hear any type of claim provided for by the Federal Rules.<sup>19</sup> Thus, some courts have allowed the trustee a money judgment on a counterclaim interposed to recover a voidable preference—an action which the bankrupt could not have brought and which is available only to the trustee in bankruptcy.<sup>20</sup> Indeed, it has been decided that the filing of a cross-claim against an adverse claimant will be sufficient to give the bankruptcy court summary jurisdiction to determine the rights of the cross-claimant.<sup>21</sup>

This increase in the scope of consent to the summary jurisdiction of the bankruptcy court over the trustee's counterclaims avoids the necessity of multiple suits to enable the trustee to satisfy his claims against a creditor of the bankrupt. Consequently, it helps to minimize the administration expenses of the trustee and gives effect to the purpose of the Bankruptcy Act by maximizing the debt-paying capacity of the bankrupt's estate.

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<sup>18</sup> In the Matter of Majestic Radio & Television Corp., 227 F.2d 152, 156 (7th Cir. 1955).

<sup>19</sup> Where the claimant expects a counterclaim to be interposed but does not want to defend against it in summary proceedings he should bring a plenary action to recover his claim.

<sup>20</sup> Continental Cas. Co. v. White, 269 F.2d 213 (4th Cir. 1959); Inter-state Nat'l Bank v. Luther, 221 F.2d 382 (10th Cir. 1955), *petition for cert. dismissed*, 350 U.S. 944 (1956); *In re* Nathan, 98 F. Supp. 686 (S.D. Cal. 1951), 27 N.Y.U.L. REV. 142 (1952), 37 IOWA L. REV. 431 (1952). *But cf.* B. F. Avery & Sons Co. v. Davis, 192 F.2d 255 (5th Cir. 1951), *cert. denied*, 342 U.S. 945 (1952). See Nadler, *Summary Jurisdiction To Render an Affirmative Judgment on Counterclaims, Set-offs and Reclamations*, 29 REF. J. 39 (1955).

<sup>21</sup> Reconstruction Fin. Corp. v. Riverview State Bank, 217 F.2d 455 (10th Cir. 1954); FED. R. CIV. P. 13 (g).