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BANKRUPTCY - REORGANIZATION - NATURE OF FARMER-DEBTOR'S RIGHT TO ADJUDICATION UNDER SECTION 75 (s)

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BANKRUPTCY — REORGANIZATION — NATURE OF FARMER-DEBTOR'S RIGHT TO ADJUDICATION UNDER SECTION 75 (s) — Plaintiff, a farmer, filed his original petition May 3, 1934, under section 74[1] of the Bankruptcy Act. Eleven months later he amended his petition, seeking relief under section 75 (a)-(r).[2] Until March 2, 1940, no progress was made, and at that time the plaintiff sought adjudication under subsection (s).[3] The district court entered an order that the petition be denied and the mortgagee's title recognized. The circuit court of appeals affirmed,[4] stating that the petitioner had an affirmative duty to proceed diligently in obtaining a composition and extension agreement under subsections (a)-(r). *Held*, reversed. The benefits of section 75(s) are

[1] As in the Bankruptcy Act of March 3, 1933, chapter 8, 47 Stat. L. 1467 (1933). In the 1938 revision this section was amended and incorporated in chapters XI-XIII, 52 Stat. L. 840 (1938), 11 U. S. C. (1940), § 701 et seq.

[2] 47 Stat. L. 1470 (1933), 11 U. S. C. (1940), § 203 (a)-(r).

[3] 49 Stat. L. 943 (1935), 11 U. S. C. (1940), § 203(s).

[4] (C. C. A. 7th, 1941) 119 F. (2d) 354.

not conferred in the discretion of the court. Adjudication thereunder is not conditioned on diligence in seeking a composition and extension agreement under subsections (a)-(r). *Wright v. Logan*, 315 U. S. 139, 62 S. Ct. 508 (1942).

Subsection (s) of section 75 of the Bankruptcy Act has been uniformly interpreted by the Supreme Court as entitling the debtor to administration according to its literal terms, with no requirement that the debtor comply wih standards of reasonable conduct usually demanded by an equity court as a condition to granting relief. Thus, in *John Hancock Mutual Life Insurance Co. v. Bartels*,[5] it was held that the element of the farmer's good faith was not to be considered in adjudicating him a bankrupt under subsection (s), if he were otherwise qualified under the statute. In *Wright v. Union Central Life Insurance Co.*,[6] the right of the debtor to redeem the land at its appraised or reappraised value was held to be absolute, and correspondingly superior to the right of the creditor to demand a public sale at which he might bid.[7] Similar interpretation of the subsection prevailed in *Kalb v. Feuerstein*,[8] and *Borchard v. California Bank*.[9] In the former case the stay of state court proceedings was found to be automatic and mandatory, while the latter decision held that a creditor to obtain foreclosure must follow the exact procedure of section 75(s). In the principal case, where the debtor was thought to be precluded from the benefits of subsection (s) by his laches and inequitable conduct in inducing the district court to extend his opportunity for redemption by promising to give up possession voluntarily,[10]

[5] 308 U. S. 180, 60 S. Ct. 221 (1939), noted 53 HARV. L. REV. 872 (1940). The good faith requirement which is referred to in this and subsequent cases appears in subsection (i) of § 75, 47 Stat. L. 1472 (1933), 11 U. S. C. (1940), § 203(i). For an exposition of the early view as to this requirement which prevailed in the lower federal courts, see Wilson v. Alliance Life Ins. Co., (C. C. A. 5th, 1939) 102 F. (2d) 365. The facts of the Bartels case required only a holding that a reasonable prospect of rehabilitation was not an element in determining the debtor's good faith, but, as is indicated by subsequent decisions, the reasoning goes much further.

[6] 311 U. S. 273, 61 S. Ct. 196 (1940), noted in 8 UNIV. CHI. L. REV. 539 (1941). The facts of the case present the question of priority of rights where the debtor has terminated his stay through failure to comply with a court order, and it was decreed that the debtor still has a right to pay in the appraised value within a reasonable time before the court may grant the creditor's petition and order a public sale.

[7] The clear implication of this case is that the stay under subsection (s) must always last three years unless earlier terminated by the debtor. This together with other cases prevents a narrow interpretation of the Bartels decision which might limit it to a ruling on procedure, to the effect that lack of ability to rehabilitate should not result in dismissal of the debtor's petition but might be sufficient reason to order a public sale after adjudication. See In re McClenahan, (D. C. Iowa, 1941) 41 F. Supp. 694.

[8] 308 U. S. 433, 60 S. Ct. 343 (1940).

[9] 310 U. S. 311, 60 S. Ct. 957 (1940).

[10] This was one of the reasons given by the circuit court of appeals for its ruling, (C. C. A. 7th, 1941) 119 F. (2d) 354. Whether there was no requirement of good faith whatever for adjudication under subsection (s) or whether some factors might not be considered as going to lack of good faith had not been made clear by the Bartels decision. Letzler, "Bankruptcy Reorganization for Farmers," 40 COL. L. REV. 1144 (1940). Lower federal courts were unwilling to adopt the interpretation that there was no requirement whatever, In re Carter, (D. C. Wash. 1941) 38 F. Supp. 726, but in view of the principal case it is difficult to see that this is not the correct interpretation.

the holding that it is erroneous to give such considerations any weight in the adjudication of the debtor under subsection (s) might well have been expected. Although it is doubtful whether such a long delay will often occur under subsections (a)-(r), this decision is of practical importance to procedure under section 75 because the court, in ruling that adjudication under subsection (s) is in no way discretionary, implicitly affirmed the decision in *Cohan v. Elder*,[11] where it was decided that although the farmer-debtor had operated under a confirmed extension agreement for thirty-three months, he still had an absolute right to "feel aggrieved" [12] at such agreement and thus qualify for adjudication under subsection (s). A court, it was held, is no more free to inquire into motive, good faith, or general equitable considerations than if the debtor were filing under subsection (s) in the more usual way, after having failed to obtain the consent of a majority of his creditors to a proposed composition and extension agreement.[13] The result of the rule, as confirmed by the principal case, operates to eliminate whatever lingering notions remain as to the importance of subsections (a)-(r) in comparison with subsection (s) and to enforce the realization that whatever similarity section 75 may bear to bankruptcy legislation must be found in the latter subsection. No debtor will offer a plan giving substantially greater benefits to the lien holder than would be accorded under subsection (s), and the only result of the creditors' consent is to forestall the time when the debtor will file under the moratorium subsection.[14] The decisions indicate heavy reliance on Congressional intent in their interpretation of section 75, that intent being to secure to farmers all benefits consistent with any rational explanation of constitutionality.[15] It is clear that this liberal construction does aid the farmer-

[11] (C. C. A. 9th, 1941) 118 F. (2d) 850, cert. denied 313 U. S. 583, 61 S. Ct. 1102 (1941). See Report 17, 1 PRENTICE-HALL, BANKRUPTCY SERVICE (1941), where a note on an unreported decision in accord is summarized. The facts in that decision were essentially those of Cohan v. Elder, the debtor "feeling aggrieved" at the end of thirty-four and one-half months.

[12] ". . . or if he feels aggrieved by the composition and/or extension. . . ." 49 Stat. L. 943 (1935), 11 U. S. C. (1940), § 203(s). See note 13, infra. Diamond and Letzler, "The New Frazier-Lemke Act," 37 COL. L. REV. 1105 (1937). The authors point out that allowing the debtor to feel aggrieved arbitrarily necessarily stultifies a good faith requirement, and that it is somewhat unusual to allow a person to feel aggrieved at a plan which he himself formulated in the absence of changed circumstances. See also Letzler, "Bankruptcky Reorganizations for Farmers," 40 COL. L. REV. 1140, note 32 (1940).

[13] "Any farmer failing to obtain the acceptance of a majority in number and amount of all creditors whose claims are affected by a composition and/or extension proposal, . . . may amend his petition or answer, asking to be adjudged a bankrupt." 49 Stat. L. 943 (1935), 11 U. S. C. (1940), § 203(s).

[14] It is evident that the relief which farmer-debtors are interested in is offered by subsection (s). Letzler, "Bankruptcy Reorganizations for Farmers," 40 COL. L. REV. 1144 at 1164 (1940). The author points out that if § 75 is to be interpreted so as to make subsections (a)-(r) merely formal steps in attaining the benefits of subsection (s) it would not be amiss to amend § 75 with such an end in view, and that even before the decision in the principal case creditors seldom consented to composition and extension agreements. Id., 1164.

[15] See cases cited in notes 5, 6, 8, 9, supra. And see particularly the footnotes of

debtors, although it may now be difficult for the Court to explain the constitutionality of the subsection as thus interpreted.[16]

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the court in Wright v. Vinton Branch of Mountain Trust Bank of Roanoke, 300 U. S. 440, 57 S. Ct. 556 (1937), wherein Congressional hearings on the subject are quoted.

[16] In the decision holding constitutional subsection (s) as amended, Wright v. Vinton Branch of Mountain Trust Bank of Roanoke, 300 U. S. 440, 57 S. Ct. 556 (1937), the Court was able to distinguish the present subsection from the previous one on such bases as control of the court over the property, absence of absolute stay, right of the creditor to demand a public sale at which he might bid. These bases as well as certain assumptions on which the Court predicated its reasoning in the Vinton Branch case have been to some extent overruled directly by John Hancock Mut. Life Ins. Co. v. Bartels, 308 U. S. 180, 60 S. Ct. 221 (1939), and by necessary implication. See In re McClenahan, (D. C. Iowa, 1941) 41 F. Supp. 694.