The Effect of Insolvency on Equitable Relief

Ralph A. Newman
THE EFFECT OF INSOLVENCY ON EQUITABLE RELIEF

THE BASIS OF EQUITY JURISDICTION.

Although the origins of equity jurisdiction have been variously defined, it is generally agreed that one of its most fundamental bases was the necessity of supplementing with more flexible forms of relief the rigid remedies of the common law; that is, where the legal remedy was inadequate. Were it not for statements of legal authors and decisions of courts to the contrary, it might well be assumed that hardly

1 This was originally true in both the exclusive and concurrent jurisdictions and is still true in the concurrent jurisdiction. Earl of Oxford’s Case, 1 Ch. Rep. 1, 4–11 (1616); 3 Bl. Comm. (2d ed. 1884) 434, 436 (as to the concurrent jurisdiction); Maitland, Equity (3d ed. 1927) 6–11; 1 Pomeroy, Equity Jurisprudence (4th ed. 1918) §§ 62, 219–221; 2 Story, Equity Jurisprudence (14th ed. 1918) § 718; 1 High, Injunctions (4th ed. 1905) § 23; Bitterman v. Louisville & N. R. R., 207 U. S. 205, 28 Sup. Ct. 91 (1907); Seymour v. Delancy, 3 Cow. 445 (N. Y. 1824); Thomas v. Mutual Prot. Union, 121 N. Y. 45, 24 N. E. 24 (1890); Bomeisler v. Forster, 154 N. Y. 229, 48 N. E. 534 (1897); Livingston v. Painter, 28 How. Pr. 517, 520 (N. Y. 1865); Parker v. Garrison, 61 Ill. 250 (1871).

There are, of course, other bases of the equity jurisdiction, e.g., affording a forum for poor complainants. See Baildon, Select Cases in Chancery (1896) (especially cases 6 (1388) and 43 (Tem. Ric. II, 1377–1399)).

The fact that there is no legal remedy at law does not necessarily and of itself give the court of equity jurisdiction. Rutland Marble Co. v. Ripley, 10 Wall. 339 (U. S. 1870); nor need equity always restrain its hand even though damages can be calculated, for plaintiff cannot, for example, be compelled to surrender his property to defendant. Gregory v. Nelson, 41 Cal. 278 (1871); cf. Meyer v. Phillips, 97 N. Y. 485 (1884); see remarks of Jessel, M. R., in Smith v. Smith, 40 Eng. L. & Eq. R. 500 (1875) (even after Lord Cairn’s Act).


For a concise description of the exclusive and concurrent jurisdictions, see 1 Pomeroy, supra, §§ 137–143. In the exclusive jurisdiction the primary right violated is purely equitable, and the remedial right is likewise purely equitable; in the concurrent jurisdiction the same kind of relief is given as at law, i.e., when the legal remedy is inadequate. Of course, it is unnecessary in this connection to consider the auxiliary jurisdiction.

2 Blank v. La Montaigne. 123 Misc. 238, 205 N. Y. Supp. 45 (1924); see Williston, Sales (2d ed. 1924) §§ 143, 144; (1901) 1 Col. L. Rev. 267.
any thesis of the law is less open to question than that the recovery of a judgment which the defendant is unable to satisfy will not redress the injury which he has caused to the plaintiff; that is, that the legal remedy of a judgment against an insolvent defendant is not adequate. Yet in some cases equitable relief is denied although the defendant is insolvent, in others relief is granted because he is insolvent, in others relief is denied because he is insolvent, in others relief is granted although he is insolvent, and in still others the question of his solvency is regarded as immaterial. It will be the aim of this paper to discuss the reasons for such strange incongruities of legal philosophy, and to suggest a possible solution.

In the case of contracts concerning the purchase or sale of land, the doctrine of inadequacy as the basis of the equity jurisdiction has crystallized into a legal rule, regardless

1 Hodgson v. Duce, 2 Jur. (n. s.) 1014 (1856), involved a bill for injunction to restrain repeated trespasses on plaintiff's property; Sir J. Stuart, V.C.: "It had been suggested that for these trespasses an adequate remedy might be had at law * * * Unquestionably, a court of law would award damages in such a case, but damages against whom? The defendant is a pauper, and as against persons in her position such a form of redress would be the merest mockery of justice."


3 Zimmerman v. Gerzog, 13 App. Div. 210, 43 N. Y. Supp. 339 (2d Dept. 1897); Petrolin Mfg. Co. v. Jenkins, 29 App. Div. 403, 51 N. Y. Supp. 1028 (1st Dept. 1898); Speare v. Cutter, 5 Barb. 486 (N. Y. 1849); Ran v. Seidenberg, 53 Misc. 386, 104 N. Y. Supp. 798 (1907); see Doty v. Doty, 171 N. Y. Supp. 852 (1918) (damages against insolvent defendant deemed inadequate; yet they would also have been inadequate against a solvent defendant); Walker v. Walker, 51 Ga. 55 (1874); Kerlin v. West, 4 N. J. Eq. 499 (1844); 5 Pomeroy, op. cit. supra note 1, §§ 1911, 1931, n.38; 1 Ames, CASES ON EQUITY JURISPRUDENCE (1904) 524, n.2.

4 City Fire Ins. Co. v. Olmsted, 33 Conn. 476 (1866); see Chaee v. Sprague, 16 R. I. 189, 13 Atl. 121 (1886); see Williston, CONTRACTS (1937) § 1420.

5 Hurley v. A. T. & S. F. Ry., 213 U. S. 126, 29 Sup. Ct. 466 (1909); Sieg v. Greene, 225 Fed. 955 (C. C. A. 8th, 1915), wherein delivery, less than four months prior to bankruptcy, of bricks manufactured with defendant's money, was held not to be a preference.


7 "** The doctrine is settled that in contracts for the purchase and sale of land, damages are inadequate, and this general rule would not yield to the special circumstances of a particular case"., Pomeroy, SPECIFIC PERFORMANCE OF CONTRACTS (3d ed. 1926) § 27 at 90.

8 In this article the expression "legal rule" is used in the sense of a rule applicable to both law and equity.
of circumstances, because land is historically regarded as unique and irreplaceable; and the vendor's right of specific performance against the purchaser, although attempts have been made to rationalize it, has also attained the judicial sanctity of a legal rule because of the doctrine of affirmative mutuality. In the case of contracts concerning unique personal property some courts seem regrettably reluctant, although giving lip service to the doctrine enunciated in *Duke of Somerset v. Cookson* and adopted by the United States Supreme Court in *Mechanic's Bank v. Seton*—that the ground of equity jurisdiction there also is based upon the impossibility of arriving, at least with any reasonable degree of certainty, at a legal measure of damage at all—to apply the doctrine to the cases before them.


12 3 P. Wms. 390 (1735).

13 1 Pet. 299 (U.S. 1828).

14 The New York courts have usually either confined the granting of relief to cases where other grounds for equitable relief were present or have found that the legal remedy was adequate, and have therefore declined to grant specific performance. Thus Johnson v. Brooks, 93 N.Y. 337 (1883), a case frequently stressed and the only New York case cited in *5 American and English Annotated Cases*, 269n. on the general doctrine, was a case of the enforcement of an agreement to purchase stock made by an agent to whom the money for the purpose had been given by the plaintiff. Other cases, the decisions of which are explainable on varying grounds, are Menier v. Donald, 98 Misc. 684, 165 N.Y. Supp. 50 (1917) involving a contract for sale of a ship, said by the court to be, perhaps, personal property of a "special kind"; see also Clark v. Flint, 22 Pick. 238 (Mass. 1839). Cushman v. Thayer Co., 76 N.Y. 365 (1879) (judgment directing transfer of stock on books of defendant corporation); Schwartz v. Marjolet, Inc., 214 App. Div. 530, 212 N.Y. Supp. 464 (1st Dept. 1925) (trust relationship between plaintiff, an agent, and defendant, a principal, who had agreed to deliver stock as partial compensation for services rendered); Topken v. Schwartz, 223 App. Div. 328, 227 N.Y. Supp. 561 (1st Dept. 1928) (the reverse of the situation in the previous case), where employer corporation was held entitled to recover stock previously given to employee and agreed by him to be surrendered on termination of his employment; the decree was reversed in 249 N.Y. 206, 163 N.E. 206 (1928) because not mutually binding; Scruggs v. Cotterall, 67 App. Div. 583, 73 N.Y. Supp. 882 (1st Dept. 1902) (option agreement between holders of a majority of shares of stock to purchase stock of deceased share-holder); Matter of Petition of Argus Co., 138 N.Y. 557, 34 N.E. 388 (1893) (contra to Scruggs case); Winchester v. Simmons, 222 App. Div. 639, 227 N.Y. Supp. 408 (1st Dept. 1928) (fraud in sale of stock represented to be completely owned by defendant corporation); Ran v. Seidenberg, 53 Misc. 386, 104 N.Y. Supp. 798 (1907) (promoter-investor relationship); Bailey v. Colleen Products Corp., 120 Misc. 297, 198 N.Y. Supp. 418 (1923) (same situation except that the corporation had adopted the promoter's contract).

A necessary preliminary inquiry is whether a party to a contract is entitled to the performance stipulated for, or whether the payment of damages by the party who has broken the contract is an alternative privilege of the wrong-doer.\textsuperscript{15} The easy morality of the latter view has never appealed to

\textsuperscript{15}Professor Beale in his treatise on the \textit{Conflict of Laws}, has stated in convincing fashion the classification of rights as static and protective; see 1 \textsc{Beale}, \textit{The Conflict of Laws} (1935) §8 A.11, and pp. 68, 78, 82, and 290. \textit{Cf.} 2 Bl., \textit{op. cit. supra} note 1, at 438: "The primary right to a satisfaction for injuries is given by the law of nature, and the suit is only the means of ascertaining and recovering that satisfaction." The remedial or protective rights, according to Professor Beale, are the rights to sue and to be satisfied. See also \textsc{Pound}, \textit{The Theory of Judicial Decision} (1922) 36 Harv. L. Rev. 641, 647.
the conceptions of ethics of the Continental or Scotch jurists, and although the view is hinted at in some of the earlier English decisions, it is now definitely discarded. However, the fact that a party is ideally entitled to performance in kind does not mean that such a right will be enforced by equity in all cases. It is only where the considerations opposed to the awarding of a decree of specific performance, such as the objection of the necessity for continuous supervision, the reluctance to impose involuntary servitude, the distaste of imposing restrictions on economic competition, the undesirability of eliminating a jury trial, or the burden on the defendant, the public or other credit-

1 See Wills, An Inquiry into the Principles of the Law of Contracts (1922) 46 HARV. L. REV. 1, 16, 26; Horack, Insolvency and Specific Performance (1918) 31 HARV. L. REV. 702, 703; Langdell, A Brief Survey of Equity Jurisdiction (1887) 1 HARV. L. REV. 70, 71. Contra: Gollew v. Bacon, 1 Bulst. 112 (1611), cited in 1 CHAFEE AND SIMPSON, CASES ON EQUITY (1934) 245, 246, n.1. For the best discussion of the history of specific performance see 1 HOLDSWORTH, HISTORY OF ENGLISH LAW (4th ed. 1927) 455, 457, also 321, 324. See also 2 Cook, CASES ON EQUITY (2d ed. 1932) 1-4.


3 Gollew v. Bacon, 1 Bulst. 112 (1611); see Simms v. Burnette, 55 Fla. 702, 46 So. 90 (1928). The elimination of a trial by jury is not a constitutional objection, Walker v. Sarravint, 92 U. S. 90 (1875), as no such right ever existed where the remedy was by injunction, People v. Elmore, 256 N. Y. 489, 493, 177 N. E. 14 (1931). See Lynch v. Metro. Ry., 129 N. Y. 274, 279, 29 N. E. 315 (1891); CHAFEE, CASES ON EQUITABLE RELIEF AGAINST TORTS (1924) 257, n.1, cases cited. The statutory and constitutional provisions against imprisonment for debt prevent enforcing through contempt proceedings an equity decree for the payment of a money obligation arising out of contract.


5 See note 23, supra.
EFFECT OF INSOLVENCY

On the question as to what is meant by adequacy, courts and text-writers have frequently differed, and the Supreme Court of the United States has changed its mind. The New York courts also have wavered considerably before arriving at a uniform conclusion. It is however becoming less and less unpopular to question the soundness of the

---


28 In the following cases, treatises, and articles, the question was discussed from the viewpoint of the problem presented by the defendant's insolvency: Doty v. Doty, 171 N. Y. Supp. 882 (1918) (remedy found inadequate); Blank v. La Montaigne, 123 Misc. 238, 205 N. Y. Supp. 45 (1924) (specific performance denied—"The ability to bring an action and recover judgment determines the adequacy of the legal remedy, irrespective of the ability to collect on that judgment"); McClintock, Adequacy of Ineffective Remedy at Law (1931) 16 MINN. L. REV. 233 (remedy deemed inadequate); (1931) 21 KY. L. J. 464; (1931) 22 KY. L. J. 1, and (1936) 24 KY. L. J. 318 (remedy deemed adequate); 5 POMEROY, op. cit. supra note 1 (re specific performance—remedy deemed adequate; but cf. 5 POMEROY, § 1911 (remedy inadequate re torts)); 1 LAWRENCE, EQUITY JURISPRUDENCE (1929) § 265 (remedy found adequate in specific performance cases; but see § 79 (inadequate in tort cases)); 5 POMEROY, supra, § 2171 at 4832, n. 35. "*** The inadequacy of the legal relief which is the basis of equitable remedies is ordinarily in the nature of that relief in cases of a certain type, not in the difficulty of collection of damages in the individual instances."

29 Compare Thompson v. Allen County, 115 U. S. 550, 554 (1885) ("The want of a remedy and the inability to obtain the fruits of a remedy, are quite distinct") with Terrance v. Thompson, 263 U. S. 197, 214, 44 Sup. Ct. 15 (1923) ("But the legal remedy must be as complete, practical and efficient as that which equity could afford"). In accord with Thompson v. Allen County, supra, see Tampa R. R. v. Mulhern, 73 Fla. 146, 74 So. 297 (1917); McGann v. LaBrecque Co., 91 N. J. Eq. 307, 109 Atl. 501 (1920); Preston v. Sturgis Milling Co., 183 Fed. 1 (C. C. A. 6th, 1910), cert. denied, 220 U. S. 610, 31 Sup. Ct. 714 (1911). Contra: Lyman v. Suburban R. R., 190 Ill. 320, 330, 60 N. E. 315 (1901); Clark v. Flint, 22 Pick. 231, 238 (Mass. 1839); Yarbrough v. Thornton, 147 Ala. 221, 42 So. 402 (1906) (collection of purchase money by insolvent grantor who has conveyed, with warranty, a title which had failed, enjoined).

30 The old New York view was that the remedy is adequate if it is in its nature fitted to the end in view, even though it means a failure to produce the money. Nessle v. Reese, 19 Abb. Pr. 240 (N. Y. 1865) (insolvency not a ground of equity jurisdiction where contract provided for liquidated damages). Accord: Duffy v. Lodebush, 173 App. Div. 205, 159 N. Y. Supp. 299 (2d Dept. 1916). The present New York view is exemplified by Zeiser v. Cohn, 207 N. Y. 407, 422, 101 N. E. 184 (1913), where insolvency was stated to be an important consideration. The opinion cites Mills v. Bliss, 55 N. Y. 139, 142 (1873). See to the same effect, Speare v. Cutter, 5 Barb. 486, 489 (N. Y. 1849); Mulry v. Norton, 100 N. Y. 424, 438, 3 N. E. 581, 587 (1885) (an action to quiet title—"The evidence also tended to show that the defendant Levy was a person of little pecuniary responsibility and presumably unable to respond in damages for the injury his conduct was liable to inflict upon the plaintiff's rights").
theory that an uncollectible judgment is adequate compensation to a person whose contract has been broken.\textsuperscript{31}

It should be noted that inadequacy is only one of various objections to the completeness of the alternative remedy of damages. Indefiniteness,\textsuperscript{32} which is present when damages cannot be satisfactorily measured by any practicable standard, and difficulty of calculation,\textsuperscript{33} which exists where damages would be speculative or conjectural, are also grounds for passing to the primary right of the injured party and enforcing it. We are by no means entering *terram incognitam* when we question the completeness of the legal remedy on the ground of insolvency.\textsuperscript{34}

### THE EFFECT OF INSOLVENCY ON INJUNCTIVE RELIEF AGAINST TORTS.

The subject of the effect of insolvency on equitable rights must necessarily be considered from the separate points of approach of injunctive relief against torts and specific performance of contracts. Assuming the correctness of the modern definition of adequacy, there would appear to be no satisfactory reason why the presence of the element of insolvency should not permissibly be used as a determinant in controlling the decision of the court to award injunctive relief. Whether in such a case the presence of this factor is the basis

\textsuperscript{31} See Mulry v. Norton, 100 N. Y. 424, 3 N. E. 581 (1885); McClintock, *loc. cit. supra* note 28; cf. *Restatement, Contracts* (1937) § 361 (d): "In determining the adequacy of the remedy of damages, the following factors are influential * * * the degree of probability that damages awarded cannot in fact be collected."

\textsuperscript{32} Roseberg v. Am. Hotel Co., 95 N. J. Eq. 640, 121 Atl. 9 (1923).


\textsuperscript{34} Note MARYLAND ANN. CODE (Bagby, 1924) art. XVI, § 246, which forbids the court to deny specific performance on the mere ground that the legal remedy is adequate, unless the defendant posts a bond or makes an equivalent showing of property owned.

Section 149, New York Personal Property Law, is a statute giving discretion to allow specific performance where it is for any reason a superior form of relief. It was derived from Section 68, Uniform Sales Act, largely derived in turn from Section 52 of the English Sale of Goods Act, and appears to enlarge the legal principles applicable and might permit more readily the awarding of specific performance in cases of insolvency. There would seem to be no objection, under fusion, to further extending equity jurisdiction.
of jurisdiction or merely an element in inducing the court to exercise its discretion is largely, it is submitted with deference to those who have emphasized the distinction, a question of verbiage rather than of difference in intellectual concept. If A, B and C are necessary points of support of a raised triangle placed parallel to the ground, and if one apex of the triangle will fall without its particular support, all of the supports are necessary; even though we have two of them, the presence of the third is required. Similarly, if for example the court will ordinarily refuse specific performance of a contract for the sale of a commodity which, although actually unique, can be replaced substantially, but will grant specific performance if the plaintiff cannot get from the defendant the money with which to procure even a substantially similar replacement, the factor of insolvency is in fact a jurisdictional element, by whatever name it is called. What is meant by the particular distinction is not whether insolvency is a jurisdictional element or merely one which may induce the exercise of the chancellor's discretion, but whether or not it is the sole jurisdictional element necessary. On this point, whatever might be the ideally desirable answer if we recognize the right to specific performance as the plaintiff's primary right in all cases of contracts for the sale of chattels, the answer on the authorities must be up to the present time definitely in the negative, however "probably desirable" such a theory might be.

Reverting to the problem of the effect of insolvency on equitable relief against torts, the courts and text-writers have recognized this as a controlling factor in the important heads of trespass, waste and actions in the nature of waste. In such cases no one is injured by the granting of
injunctive relief; the plaintiff is protected in his property rights; the sensibilities of the chancellor are in no danger of being ruffled, and the plaintiff is spared the shock of being informed that a judgment which it will be impossible to collect is an adequate compensation for the loss or deprivation of the use of his property.

In many tort situations the question of the right to injunctive relief might well turn on whether the legal remedy is inadequate as matter of law, even if damages are calculable and recoverable; otherwise stated, the problem is, has the original basis of equity jurisdiction of inadequacy of remedy crystallized, as in the cases of injunction against waste, into a theory which regards damages as inadequate as matter of law? In such cases the presence of insolvency adds no additional weight; on the other hand, the factor of insolvency is not a reason for denying relief, because no one else is prejudiced. In the case of ordinary trespass, where the equity jurisdiction has not become thus crystallized, insolvency might well be regarded as the controlling factor. As has been stated, no one will be injured if it is so treated. This result has been reached in New York with regard to the threatened asportation of a non-unique chattel. When the chattel is unique or has been severed from the realty, damages are regarded as inadequate even though the defendant be solvent; insolvency is, therefore, in such a situation, immaterial.

Equity will ordinarily refuse to enjoin a trespass un-

---

43 1 Ames, op. cit. supra note 5, at 524, n.2; see 5 Pomeroy, loc. cit. supra note 40.
44 An owner of property should not be obliged to part with it, even though the loss is measurable in money. Gregory v. Nelson, 41 Cal. 278 (1871); Smith v. Smith, 20 Eng. L. & Eq. R. 500 (1875).
45 Vane v. Lord Barnard, 2 Vern. 738 (1716); Rolt v. Lord Somerville, 2 Eq. Cas. Abr. 759, pl. 8 (1737); Cairns v. Chabert, 3 Edw. Ch. 312 (1839); Lane v. Newdigate (per Lord Eldon), 10 Ves. 192 (1804) (negative injunction).
46 Electric Construction Co. v. Heffernan, 34 N. Y. St. Rep. 436, 12 N. Y. Supp. 336 (1890); Speare v. Cutter, 5 Barb. 486 (N. Y. 1849); the court based its decision on the multiplicity of suits theory. But where defendant was not insolvent, similar relief was thought inappropriate in Watson v. Hunter, 5 Johns. Ch. 168, 172 (1821) (dictum).
47 Equity will usually refuse to enjoin a trespass which is not in the nature of waste, 14 R. C. L. (1916) 442; Gates v. Johnson, 172 Mass. 495, 52 N. E. 136 (1899); Note (1924) 32 A. L. R. 463, 464.
EFFECT OF INSOLVENCY

less it is a continuing one or a multiplicity of suits would otherwise be necessary. In such cases the element of irreparable injury required as a basis for awarding relief means the same thing as inadequacy of the legal remedy. Even if damages can be calculated in the case, for example, of a continuing trespass, the plaintiff cannot be compelled to surrender his property to the defendant. In such situations also, therefore, the question of defendant's possible insolvency is immaterial, the law having pronounced its formula that damages would be inadequate even if collectible.

Asportation of unique chattels will ordinarily be enjoined, on the same principle that leads to the specific enforcement of contracts to sell unique chattels. If the chattel is not unique, the owner is remitted to his legal remedy.

Waste is ordinarily enjoined. In all of the foregoing cases where equitable relief is granted, the inadequacy of the legal remedy must be pleaded, and on the question of adequacy the equity court's decision is final.

Within the general boundaries of the foregoing situations are cases such as those of a single and non-continuing trespass, asportation of a non-unique chattel, and, in jurisdictions where the rule of inadequacy has not become crystallized, waste where the legal remedy would be adequate. In all of these and similar situations, the factor of the defendant's insolvency might well determine the granting of injunctive relief.

THE EFFECT OF INSOLVENCY ON SPECIFIC PERFORMANCE.

In the field of specific performance, however, the inquiry involves considerations which, whatever the conclusion ulti-

---

49 See 5 PomEROY, op. cit. supra note 1, § 1910, n. 22; Note (1924) 32 A. L. R. 463, 465, 448-450.
50 See Watson v. Hunter, 5 Johns. Ch. 168, 169 (N. Y. 1821); cf. Speare v. Cutter, 5 Barb. 486 (N. Y. 1849), where defendant was insolvent and an injunction was granted on the multiplicity of suits ground; Electric Construction Co. v. Hefferman, 34 N. Y. St. Rep. 436, 12 N. Y. Supp. 336 (1890).
51 See note 45, supra.
52 See In re Seymour, 124 U. S. 200, 221, 8 Sup. Ct. 482 (1888); Blair v. Sup. Council, 208 Pa. 262, 57 Atl. 564 (1904).
mately to be reached, create a fundamentally different problem. We cannot always necessarily say in this situation, as in the case of injunctive relief against torts, or as is sometimes true in injunctive relief against breaches of contract, for example to render personal services, that no one will be injured by the granting of the relief. The pivotal inquiry is not whether the defendant has property, but whether he has property which other creditors could subject to the payment of their claims by the ordinary processes of the law other than specific performance.\(^5\) If for example the defendant is judgment-proof, with no property on which creditors can levy execution, the fact that he has property which is exempt either under the state debtor and creditor laws or under the Federal Bankruptcy Act,\(^6\) is of merely academic interest to other creditors. Under such circumstances no one will be prejudiced by the specific enforcement of the debtor's contract with the plaintiff.

Professor George L. Clark points out\(^6\) that there are other situations where this same result is reached; for example, where for any reason the defendant cannot be petitioned into involuntary bankruptcy, or perhaps where for practical reasons it would be extremely unlikely that his other creditors would file a petition, because of the relatively high cost of administration, the small amounts of the claims, or the smallness of the probable dividend. Such cases are, however, of course exceptional. In the usual situation, where the debtor's property is subject to execution and where a petition in bankruptcy could and might well be filed, we are confronted squarely with the problem of the relative impor-

---

\(^5\) Henry v. Whidden, 48 Fla. 268, 269, 37 So. 571 (1904); Williston, op. cit. supra note 6, § 1420.

\(^6\) In re Ferguson, 95 Fed. 429 (S. D. N. Y. 1899); if such is the situation the debtor is not subject to attack. In re Chapman, 99 Fed. 395 (N. D. Ga. 1900) (as, e.g., a mortgagor's equity of redemption which is not subject to sale under execution in Missouri); Matter of Moark-Nemo Mining Co., 219 Fed. 340 (W. D. Mo. 1915); Vitzthum v. Large, 162 Fed. 685 (N. D. Ia. 1908); First Nat. Bank v. Orten, 11 Okla. Cr. 80, 142 Pac. 1096 (1914); 2 Collier, Bankruptcy (13th ed. 1925) 1277, n.136. Exempt property constitutes no part of the bankrupt's estate, In re Oleson, 110 Fed. 796 (N. D. Iowa 1901), 2 Collier, supra, § 70 (a) at 1744, and does not pass to the trustee. Exemptions are created by state law. Lockwood v. Exchange Bank, 190 U. S. 294, 23 Sup. Ct. 751 (1902).

\(^6\) See Clark, Some Problems in Specific Performance (1917) 31 Harv. L. Rev. 271, 276.
tance of the equities of the plaintiff and of the other creditors. In this connection there is no longer any significance in the distinction between unique and non-unique chattels, since in neither case is the legal remedy adequate. On the other hand, if insolvency is a bar in the case of non-unique chattels, the same bar will be encountered in seeking the specific performance of contracts to sell unique chattels. On this problem the courts have reached different conclusions which fall primarily into two classes: one, that the presence of insolvency requires that the equitable jurisdiction be exercised; the other, that insolvency is a ground for declining equitable jurisdiction and refusing specific performance.

**The Policy of the Federal Bankruptcy Act.**

The view has been expressed by various writers, led by Professor Williston, that the enforcement of contract rights

---

58 City Fire Ins. Co. v. Olmsted, 33 Conn. 476 (1866); see Chafee v. Sprague, 16 R. I. 189, 13 Atl. 121 (1886); (1921) 34 HARV. L. REV. 309.

Professor Williston in his works on SALES, Section 144 and on CONTRACTS, Section 1420 (the *erratum* in the 1920 edition at line 9 of p. 2527 where the word "from" was inadvertently omitted, changing the sense considerably, has been corrected at page 3964 of the 1937 edition) argues that since the Bankruptcy Act does not forbid an insolvent to make a transfer of his assets for a return honestly bargained for as an equivalent, there is no objection to the performance by him of a fair executory contract, or to the enforcement of it by a court of equity; but that if the insolvent had already received the whole or part of the consideration, subsequent performance by him could never be justified on the ground of insolvency, since in bankruptcy an insolvent's obligations by way of mere contract must be sharply distinguished from his obligations to surrender specific property where the legal or equitable ownership is in another; so that if the bankrupt has been paid in advance, a subsequent delivery within the four-month period would be a preference, and a decree of specific performance because of insolvency would order the debtor to do something the Bankruptcy Act has forbidden him to do. Cf. RESTATEMENT, CONTRACTS (1932) § 362, comment c, incorporating the above views. It may well be asked, however, with all deference to the great authority supporting the statement, why, if it would not violate the policy of the Act for equity to order specific performance of a wholly executory "fair" contract made "in good faith", it would violate its policy to order the enforcement of the contract if the insolvent has already received "the whole or part of the consideration". WILLISTON, op. cit. supra note 2, § 144 at 271. Is this not preeminently a case of sacrificing substance to form? No equitable lien, of course, attaches in favor of one who has contracted to purchase even a unique chattel; see WILLISTON, supra, § 602; cf. Pusey v. Pusey, 1 Vern. 273 (1684); Onondaga Nation v. Thatcher, 53 App. Div. 561, 65 N. Y. Supp. 1014 (4th Dept. 1900), aff'd, 169 N. Y. 384, 62 N. E. 1098 (1901): "If adequate reasons exist for specific performance, the Bankruptcy Act is in no sense a bar." WALSH, op. cit. supra note 38, at 321.
by permitting specific performance against an insolvent defendant would directly violate the policy of the bankruptcy statute, itself the expression of an equitable policy, and should for that reason be refused. In view of the authoritative nature of the foregoing expressions of opinion, a somewhat detailed examination of the statute is warranted. That the purpose of the Act is to secure the equal distribution of the debtor's assets among all creditors of each class, is axiomatic. The Act itself has, however, created certain standards by which such equality of distribution is to be judged. At the outset of this part of the discussion certain distinctions must be observed.

A preference is of course viewed from two angles; as an act of bankruptcy, and as a voidable transfer of the debtor's property. From the first point of view, an intent to prefer is requisite; from the latter, merely, reasonable ground for belief by the creditor that the debtor was insolvent at the time of the transfer is necessary. Only such transfers, moreover, as diminish the debtor's estate, fall within the prohibi-

The framework of Professor Williston's theory is incorporated in his phraseology of RESTATEMENT, CONTRACTS (1932) § 362: "Specific enforcement will not be decreed if the performance required will constitute a preference of one creditor over others that is inconsistent with the purpose of an existing bankruptcy statute or of other rules of law governing the distribution of insolvent estates. In cases where the performance required will not constitute such a preference, the existing or prospective insolvency of the defendant will be considered in determining the adequacy of the remedy in damages." The section is, however, phrased with such admirable restraint as to permit the equity court to decree specific performance if such a result would not violate the purpose of the Bankruptcy Act.

See cases cited note 58, supra.

Wilson v. City Bank, 17 Wall. 473, 480 (U. S. 1873); 1 REMINGTON, BANKRUPTCY (1934) 18.

Note that the creation of the lien of a conditional vendor, even though possession changed, is not a transfer of such property. Bailey v. Baker Ice Machine Co., 239 U. S. 268, 36 Sup. Ct. 50 (1915), aff'd, 209 Fed. 603 (C. C. A. 8th, 1913). For a factor's lien to be effective, it is absolutely necessary that the property consigned be delivered to the consignee. Ommen v. Talcott, 188 Fed. 401 (C. C. A. 2d, 1911). Similarly, a pledge must be delivered, to give rise to a lien. Matter of Sullivan Co., Inc., 247 Fed. 139 (N. D. N. Y. 1918), aff'd, 254 Fed. 660 (C. C. A. 2d, 1918); Matter of Imperial Textile Co., 255 Fed. 199 (N. D. N. Y. 1919). Delivery may be symbolical (e.g., set aside and earmarked), Ward v. First Nat. Bk., 202 Fed. 609 (C. C. A. 6th, 1913).

U. S. BANKRUPTCY LAW, 52 STAT. 844, 11 U. S. C. A. § 21 (Supp. 1938). Section 96 is a definition when applied to a transaction voidable under Section 21.
tion of the statute, and the test of diminution is two-fold; first, whether the allegedly preferred creditor receives a greater percentage of the estate than other creditors, and secondly, in case there are different classes of creditors, whether, as among other creditors of the same class, such an undue advantage results from the transfer. Section 60 of the Act is the section which deals with preferred creditors. The Act itself, although nowhere defining classes of creditors eo nomine, refers in Sections 56-b, 57-e and 57-h, to holders of liens; in Section 64 to claims for wages, taxes, and debts owing to any person who, by the laws of the United States, is entitled to priority, and, generally throughout the statute, to general creditors. These are the kinds of classes meant by the Act. Where there is only one creditor of a class, as for example a distraining landlord, there can be no question of his being preferred within his class. Preferences through legal proceedings are dealt with in Sections 60 and 67.

Creditors entitled to priorities, preferred creditors and secured creditors are terms of art in the statute. Secured creditors are those having liens on assets of the debtor. Preferred creditors are those who have received preferences, whether voidable or not; and creditors entitled to priority of payment are merely, as their name implies, general creditors who are in different strata of preferment, as to the payment of their claims, from other dissimilarly created creditors. Priority does not refer to liens.


Preferences were not always repugnant to the policy of the insolvency statutes. The modern doctrine that they are wrongs to other creditors was first declared by Lord Mansfield in Worsely v. de Mattos, 1 Burr. 467 (1758), and was not incorporated into our law until 1841.
In determining the effect of the defendant's insolvency on the plaintiff's right to specific performance, certain dis-

Prior to the amendment on June 22, 1938 of Section 64 of the Federal Bankruptcy Act, eliminating the provision in subdivision b (7) for the recognition of priorities created by state law, it might indeed have been contended with considerable force that the Act expressly recognized whatever priorities (not, of course, inconsistent with the express priority provisions of the Act) were so created. Apart from legal verbiage, there is no doubt that the granting of relief by way of specific performance, because of the very nature of the relief, would constitute recognition by the state of the creditor's right as a prior one.

Prior to the amendment it had been held, construing former Section 64 b (7), defining, as the last class of prior claims in the statutory hierarchy, debts owing to any person who by the laws of the states or of the United States was entitled to priority, that, although a different view had been expressed (6 REMINGTON, op. cit. supra note 61, § 2857.70) the right need not be created by statute, but might be "created" or "recognized", depending on our view of the theory of judicial decision, by pronouncement of the courts. In re Newark Shoe Stores, 3 F. Supp. 293 (D. C. Md. 1933); State of Oregon v. Ingram, 63 F. (2d) 417 (C. C. A. 9th, 1933), cert. denied, 290 U. S. 630, 54 Sup. Ct. 49 (1933).

Moreover the decision of the highest state court was followed in determining the nature of the state priority. State of Oregon v. Ingram, 63 F. (2d) 417 (C. C. A. 9th, 1933); Comm. of Pa. v. Stocker, 70 F. (2d) 453 (C. C. A. 3d, 1934). Where there was no decision, the bankruptcy court would follow general rules of construction. Wintermore v. MacLaflerty, 233 Fed. 95 (C. C. A. 9th, 1916). Such a recognition of state priorities was constitutional; see 1 REMINGTON, op. cit. supra note 61, § 5.


Various priorities other than those resulting from the right of specific performance had been granted by statute in some states; for example, claims for materials furnished to manufacturing establishments, as in Mott v. Wessler, 135 Fed. 697 (C. C. A. 4th, 1905), In re Bennett, 153 Fed. 673 (C. C. A. 6th, 1907), In re Starks, 171 Fed. 834 (C. C. A. 6th, 1909); and see 6 REMINGTON, op. cit. supra note 61, § 2857; fiduciary debts, In re Crow, 116 Fed. 110 (W. D. Ky. 1902); and claims to community property, In re Chavez, 149 Fed. 73 (C. C. A. 8th, 1906). The rule of former Section 64 b (7) did not, however, prevent the application of Section 67 d (2), annulling liens obtained by legal proceedings within four months prior to the filing of the petition. Globe Bank v. Martin, 236 U. S. 288, 35 Sup. Ct. 377 (1914); 6 REMINGTON, op. cit. supra note 61, § 2849.

As to rights to specific property, however, even though not rising to the dignity of an equitable lien, but on the other hand not acquired merely as the result of greater diligence in bringing a legal proceeding, the only question would seem to have been whether the state law recognized the creditor's right as a prior one. Of course, even under the former statute, priorities as such could be dealt with only by the bankruptcy court and not by the state court; but the former recognition of priorities created by state law would appear to
tinctions must be borne in mind. Holders of equitable rights must be differentiated from holders of equitable liens,\textsuperscript{70} and holders of implied equitable liens, as for example a grantor’s lien, must be distinguished from holders of express equitable liens.\textsuperscript{71} As to holders of equitable rights merely, the time-honored distinction between rights and remedies, encountered so frequently in the fields of Conflict of Laws and of Constitutional Law, becomes relevant in this connection also. Before we can reach a conclusion upon our ultimate problem, however, a further inquiry must, it will be evident, be directed to the nature of the right of specific performance in the case of contracts concerning chattels. Does the right to obtain specific performance rest upon an equitable lien on some specific property, or is it merely a right to obtain specific property? And even if the latter, must the relief necessarily fail as opposed to the policy of the bankruptcy statute? Illustrating the distinction between the creation of an equitable lien and a right to specific performance generally, is the case of an agreement to give security, which was not, even prior to the recent amendment of Section 64

have been an express statutory indication of a policy approving their creation, since if the state could create a right of priority through recognizing the right to specific performance, and if this right would have been recognized in the administration of the bankrupt’s estate, it would have been decidedly incongruous for the federal court to authorize its trustee to bring an action to set aside a transfer made pursuant to a state court judgment decreeing specific performance on the ground that complying with the decree would constitute a preference. Since the amendment of Section 64 by the elimination of the recognition of state priorities, however, the foregoing deduction of the policy of the Bankruptcy Act is, of course, no longer permissible. The analysis is presented, however, in the thought that the amendment eliminating state priorities is probably a conscious or subconscious manifestation of the tendency towards the strengthening of federal control of the administration of our commercial economy. Since it is not inconceivable that the centrifugal forces may in time overcome the centripetal ones observed during the last five years, a restoration at some future time of the right of states to establish their own priorities might render pertinent the foregoing analysis.


of the Bankruptcy Act, entitled to priority, and an agreement which has given rise to an equitable lien on specific property, as setting aside in escrow for delivery to a pledgee, within the four-month period. If an equitable lien has been created, it will be specifically enforced in bankruptcy.

THE QUESTION OF POLICY APART FROM THE EXPRESS PROVISIONS OF FEDERAL BANKRUPTCY ACT.

On the question of whether the courts should incline to an interpretation of the spirit or policy of the Act as forbidding the granting of specific performance in the event of the defendant's insolvency, a short and evasive answer might be that the Act could speak for itself, but is silent as to any such policy. On the question of policy apart from any indication of such statutory intent, there is no doubt but that equity is not inclined to favor one creditor over others similarly situated. Who has the greater equity? The other creditors may have become such otherwise than through contracts of purchase, as for example through contracts of employment, or loans, and may therefore not have acquired the right to receive any specific property of the defendant. Will the other creditors actually be benefited by equity's withholding from the plaintiff the relief of specific performance? These are the questions, the answers to which, taken conjointly, should greatly assist in solving the problem. As to who has the greater equity, a distinction might well be drawn, based on sound principles of equity, as to whether the other creditors would be unduly prejudiced by the granting of specific performance. If the estate will not be diminished, there is no problem under the Bankruptcy Act. Even if the estate would be diminished, however, looking exclusively at the element of delivery apart from the antecedent payment of the purchase price, this factor is not necessarily of con-

---

trolling force in weighing the conflicting equities. The test might well be whether or not other creditors have been misled to their damage. If for example a purchaser has paid the purchase price for the chattel, and the seller's other creditors never knew of the seller's ownership, where would be the injustice of allowing specific performance to the purchaser, as is done in the case of land? But even if the purchaser has not paid, a court of equity will of course grant a decree only on condition of payment or adequate security for payment. What the other creditors "lose" in such a case, or rather what they are prevented from acquiring, is the purchaser's profit in the transaction; but equity in recognizing the right to specific performance really recognizes that the purchaser is entitled to his profit. Indeed there is no objection even under the letter of the Bankruptcy Act to granting specific performance where the contract is executory on both sides, since a transfer in good faith for fair value presently received is not a preference. The true equities are more clearly discernable through an examination of the situation where the purchaser has paid in full but has not received the article contracted for. In this situation the other creditors would be sharing in the profit which the purchaser alone was entitled to derive from his contract; yet anomalously enough, it is in such case, where the purchaser has already paid for the goods but has not yet received them, that his right to specific performance is most seriously questioned. The remarks of Dean Pound on another aspect of the problem are equally applicable here. "If the contract is unilateral and defendant has the consideration, as it were, in his pocket, insolvency of the defendant in the sense that he is proof against execution, may be a strong ground for exercising jurisdiction where ordinarily it would not be exercised."

But the injustice of the rule may well be even more extreme. Suppose that the insolvent, instead of having the purchase price of the undelivered goods "in his pocket", to use Dean Pound's phrase, has paid other creditors, who there-

---

\[See 1 \text{ WILLISTON, op. cit. supra note 6, § 1420.}\]
\[Ibid.\]
\[Pound, supra note 36, at 430.\]
fore have it in their pockets. Would not the application of the rule usually advocated require the courts to declare that to be a preference in law which is not a preference in fact, because it has not diminished the insolvent’s estate; and would it not require the court of equity by withholding the relief of specific performance, to really prefer over the applicant before the court, the other creditors who have been paid in full out of the purchase price? True, the estate is, in all of these cases, in form, diminished; but if we recognize the purchaser’s right to performance in kind, there is no more actual diminution, looking at the transaction as a whole, than where an equitable conversion of land has been created. Substantive rights should not depend upon such fictions as the doctrine of equitable conversion.

Is the substantive equity or right of the person who has dealt with an insolvent any less because he has, instead of buying land, sold it, thereby acquiring merely a grantor’s lien for the price? Or is it any less because instead of buying land he has bought personal property, the value of which he may lose in part because of the seller’s insolvency? Or is it any greater than in a contract to give and receive security because he has, through the setting aside in escrow of security to be pledged to him, acquired an equitable lien? In recognizing the equitable right to specific performance generally, we are merely disregarding the fortuitous circumstance that an equitable lien has not been created. Where liens need not be filed or recorded, they constitute in fact no greater notice than do equitable rights of lesser dignity. Even if the estate were really to be diminished, the answer to the question as to whether the other creditors will be benefited by the denial of specific performance is by no means clearly in the affirmative. Perhaps there will be no bankruptcy; perhaps the other creditors will never be paid at all; perhaps the purchase price of the property will never go to them; perhaps the plaintiff will prove to be the only unsecured creditor.

Where an equitable lien on specific property has been created, it, of course, prevails in a subsequent bankruptcy proceeding, Sexton v. Kessler and Co., 172 Fed. 535 (C. C. A. 2d, 1909), aff’d, 225 U. S. 90, 32 Sup. Ct. 657 (1912); In re McConnel, 197 Fed. 438 (N. D. N. Y. 1912); see also cases cited in 2 Collier, op. cit. supra note 55, at 1253, n.42.
EFFECT OF INSOLVENCY

It would therefore appear that it is by no means certain that the object of the bankruptcy statute will be attained by denying specific performance before a bankruptcy has occurred. A possible theory, although one apparently never suggested in the cases, would be to let the decree of specific performance stand unless bankruptcy subsequently shortly intervenes, staying execution, that is, for four months. Section 67 (d) 2 might then operate to prevent the enforcement of the decree. It is by no means clear equity that a litigant before the court, concededly entitled to relief, should be denied relief because others may possibly be prejudiced, when he will certainly be prejudiced by a denial of his conceded right.

The foregoing conclusion that the right to specific performance of contracts concerning chattels may be recognized even in insolvency, and that such recognition will not violate the policy of the Bankruptcy Act, may be fortified by illustrations derived from other heads of the law.

1. The equitable right of set-off in insolvency. This right unquestionably operates to give the solvent debtor of an insolvent creditor, having a counterclaim against the insolvent, a greater percentage than other creditors.

2. The right of specific performance of a contract for the sale of land.

3. In the field of Suretyship, the surety can set off the claim of the principal debtor against that of the creditor when the creditor is insolvent, although not otherwise.

---

79 See note 68, supra.
81 The trustee in bankruptcy of an insolvent vendor will be required to convey; Chaffee and Simpson, op. cit. supra note 19, at 685.
82 Coffin v. McLean, 80 N. Y. 560 (1880); Davidson v. Alfars, 80 N. Y. 660 (1880); Scroggin v. Holland, 16 Mo. 419 (1852); Springfield Engine & Thresher Co. v. Park, 3 Ind. App. 173, 29 N. E. 444 (1891); see Arant, Suretyship (1931) 214: "If the principal is insolvent he seems to be entitled to no consideration. But this should be true, irrespective of his insolvency, because the principal owes his surety the duty to pay the creditors so that the surety cannot be required to pay."
4. In the field of Partnership, when assets of a firm and its members are in the possession of a court for distribution, individual creditors share first in the individual assets even though those assets were regarded by firm creditors prior to the bankruptcy as an ultimate source of payment.\textsuperscript{84}

5. Where the bankrupt has acquired property by fraud, bankruptcy courts, under their equity powers, always give in specie to the claimant of personal property the property itself.\textsuperscript{85}

6. If the purchase money has been paid in advance to the insolvent seller, he will be required to deliver the goods if an equitable lien had been created or the money was to be held conditionally until delivery should be made, and a transfer within the four months period is not preferential.\textsuperscript{86}

7. A contract to give security,\textsuperscript{87} when property of the insolvent has been set aside in escrow for the purpose, is held to give rise to an equitable mortgage and is specifically enforced.\textsuperscript{88}

8. "Where part of an entire contract relates to personal property, and the rest to a subject-matter, such as land, over which equity jurisdiction may ordinarily be exercised, specific performance may be had of the contract as a whole, including the clause relating to personal property."\textsuperscript{89}

\textsuperscript{84} N. Y. Partnership Law § 71(h) (added by Laws of 1921, c. 23). See Prashker, Cases and Materials on Partnership (1933) 373, for a discussion on partnership property and the individual property of the partners in the possession of a court for distribution; see also Rodgers v. Meranda, 7 Ohio St. 180 (1837).

\textsuperscript{85} In re Gold, 210 Fed. 410 (C. C. A. 7th, 1913); German Nat. Bk. v. Princeton State Bk., 128 Wis. 60, 107 N. W. 454 (1906); see Horack, \textit{op. cit. supra} note 11, at 713.

\textsuperscript{86} In re Gold, 210 Fed. 410 (C. C. A. 7th, 1913); German Nat. Bk. v. Princeton State Bk., 128 Wis. 60, 107 N. W. 454 (1906); see Horack, \textit{op. cit. supra} note 11, at 713.

\textsuperscript{87} See Sleeth v. Sampson, 237 N. Y. 69, 142 N. E. 355 (1923).


Perhaps the most authoritative expression of the policy of the Bankruptcy Act is to be found in the decisions of the federal courts, and it is particularly there that we find authority for the conclusion that the policy of the statute does not oppose the granting of specific performance against insolvent defendants.

In "Mills v. Virginia-Carolina Lumber Co." a delivery of lumber was made by an insolvent, the lumber having been paid for in advance under a contract for the whole output of a planing mill. The buyer's proof of claim was objected to by the trustee on the ground that the buyer had received a preference in accepting the lumber. The proof of claim was allowed, on the ground that the transfer was not a preference. The basis of the rule is more fully explained in "Templeton v. Kehler." where the defendant contracted for the purchase of cattle, paying part of the purchase price in advance. The seller, while insolvent, and within four months prior to the filing of the petition, delivered the cattle. A settlement of the balance due was agreed upon and the agreed amount was paid. The trustee sued to set aside the delivery of the cattle as a preference. The court directed a verdict for the defendant, (although a jury had found for the plaintiff), on the ground that the purchaser was not the insolvent's creditor, whose claim had been preferred by the delivery, but his debtor, the delivery and the payment of the compromised balance of the purchase price being, not the payment of a debt by delivering cattle, but merely the completion of an executory contract of sale. The transaction was looked at, properly, as a whole, and not merely from the viewpoint of that part of it which consisted of the delivery of the cattle and the payment of the balance of the purchase price.


61a Compare the reasoning in Bridgers v. Hart, 200 N. C. 685, 158 S. E. 242 (1931), where the court held that it was a question for the jury whether or not the advancement of money by a corporation's president for traveling expenses, and the corporation's repayment after his return, at a time when the corporation had become insolvent, should be regarded as a single transaction, under which view the subsequent repayment of the advances would not constitute a preference.
The Mills and Templeton cases are explained in the second edition of "Remington on Bankruptcy", Section 1316, as falling within the exceptions, to what is there stated to be the general rule, such as cases where either title has passed, or an equitable lien has been created, or the purchase money has been held in escrow as a separate fund pending delivery. Obviously none of these exceptions, however, were applicable to the situation in either case. In the fourth edition of Mr. Remington's work, published seventeen years later, the Templeton case is cited at Section 1692 together with Gage Lumber Co. v. McEldowney (where the same result was reached on the ground of the creation of an equitable lien) as authority for the statement that "Where a purchaser from the bankrupt has paid partly in advance, the delivery of the goods purchased has been held not to be a preference, if the transaction is bona fide, for the purchaser is not a 'creditor', but is, rather, a debtor for the balance due." In this edition no attempt is made to reconcile the Templeton case with the rule stated later in the same paragraph that "such could not be the rule unless title to the goods had already vested in the purchaser or there were some equitable lien thereon in the purchaser's favor, since, if it were simply a payment in advance, then the purchaser was a creditor to the amount theretofore paid, the bankrupt fulfilling his obligation by delivery of goods instead of money." The only authority cited for the latter statement is a suggested comparison of the case of Willen v. Schillicci, which proceeded on the theory that the article contracted for in that case, flour, had been physically set aside in a warehouse, out of the insolvent seller's control, which vested title in the purchaser as against the seller's trustee in bankruptcy. The warehouseman was obviously the purchaser's bailee, and the case is readily distinguishable for the foregoing reasons. The author appears therefore in 1934, the date of the fourth edition, to regard the Templeton case as expressing the settled law, and the contrary rule, which he regards as the more desirable, as not resting on well-established authority. The attempt to distinguish, in such situations, between whether the buyer under

---

EFFECT OF INSOLVENCY

an executory contract is the seller's debtor or creditor, that is, whether the seller is the debtor of the buyer or the buyer is the debtor of the seller, suggests inquiries such as whether a squirrel is running around a man who is, within the squirrel's orbit, walking around a tree, or whether a man is standing in front of a wall or the wall is standing behind the man. When we reach such a point of inquiry we might well turn in desperation to the maxim that equity looks at the substance and not at the form;\textsuperscript{94} and the substance of the transaction is that a buyer who has paid "even" wholly in advance, has not in the net result depleted the insolvent's estate by accepting delivery of the article purchased.

In \textit{Hurley v. Atchison, T. & S. F. Ry.},\textsuperscript{95} although the United States Supreme Court uses the language of equitable mortgage, the case involved from any point of view either a contract for the sale of coal to be mined or a contract to give security for a loan, neither of which situations would create an equitable mortgage; yet the trustee, having assumed the lease of the mine, was required to mine and deliver to the buyer sufficient coal to cover its advances. It is interesting to note that Mr. Justice Holmes concurred in the judgment, without opinion, from which we may permissibly infer that he agreed with the result although not with the reasoning upon which it was based. The case has been frequently cited, always with approval.\textsuperscript{96} The state courts of Illinois, Idaho, Massachusetts, Wisconsin, Oregon, Maryland and Alabama have adopted the same conclusion as was reached in the \textit{Templeton} case.\textsuperscript{97} The New York courts are pursuing a

\textsuperscript{94}This maxim is used in connection with the very problem in \textit{Hurley v. Atchison, T. & S. F. Ry.}, 213 U. S. 126, 24 Sup. Ct. 466 (1908).

\textsuperscript{95}See note 94, \textit{supra}.

\textsuperscript{96}The most recent citation is in \textit{In re South Shore Co-operative Ass'n, Inc.}, 23 F. Supp. 743 (W. D. N. Y. 1938).

\textsuperscript{97}See \textit{Parker v. Garrison}, 61 Ill. 250, 253 (1871): "What had the complainant in the way of any adequate remedy at law? Garrison was insolvent. Any recovery of damages against him would have been worse than useless, as it would only have entailed upon the complainant an additional loss in the form of a bill of costs." \textit{Diburn v. Youngblood}, 85 Ala. 449, 5 So. 175 (1888) (\textit{dictum}); \textit{Ridenbaugh v. Thayer}, 10 Idaho 662, 80 Pac. 229 (1905); \textit{Ames v. Witbeck}, 179 Ill. 458, 53 N. E. 969 (1899); \textit{Sullivan v. Tuck}, 1 Md. Ch. 59, 63 (1847); \textit{Clark v. Flint}, 22 Pick. 231 (Mass. 1839); \textit{Livesley v. Johnston}, 45 Ore. 30, 39, 76 Pac. 13, 946 (1904); \textit{Livesley v. Heise}, 45 Ore. 148, 76 Pac. 952 (1904); \textit{Avery v. Ryan}, 74 Wis. 591, 600, 43 N. W. 317 (1889) (\textit{dictum}).
course which may perhaps be most accurately described as stumbling in the right direction.\textsuperscript{98}

\textsuperscript{98}The course of the few decisions of the New York courts has been far from uniform, although a prediction as to future development may be ventured. Zimmerman v. Gerzog, 13 App. Div. 210, 43 N. Y. Supp. 339 (2d Dept. 1897) was an action to enjoin a breach of a contract by defendant, who had sold his business to plaintiff, not to compete with him. The contract contained a provision for liquidated damages in the event of a breach, but the complaint alleged that the defendant was insolvent. The court held the provision for liquidated damages inapplicable, and granted the injunction. In its opinion the court remarked that “even were the remedy limited to the recovery of liquidated damages, it is quite probable that equity would enjoin the vendor, if he were insolvent, until the damages were paid.” The case, of course, although the injunction in effect required specific performance of the contract, falls within the easy field of cases where, since the provisions for the sale of the business had been fully executed by the insolvent, the granting of the particular relief requested could not harm his other creditors, and therefore casts little light on our problem.

In Petrolia Mfg. Co. v. Jenkins, 29 App. Div. 403, 51 N. Y. Supp. 1028 (1st Dept. 1898), the contract, for the manufacture and sale of soap sufficient for plaintiff’s requirements, appears to have been executory on both sides at the time of the action. An injunction against breach of the contract was granted, the court saying, “There is no other valid objection to an action for specific performance which would not have to be remitted to an action at law for many reasons. It is sufficient to mention the insolvency of the defendant Jenkins.” In Blank v. La Montaigne, 123 Misc. 238, 205 N. Y. Supp. 45 (1924) specific performance was denied because the legal remedy for breach of the contract was deemed adequate. The court regarded the insolvency of the defendant as of no consequence, saying, “The ability to bring an action and recover judgment determines the adequacy of the legal remedy, irrespective of the ability to collect the judgment.” The force of the decision as opposed to the granting of specific performance in case of insolvency is, of course, greatly weakened because the opinion was predicated on the old view of adequacy, subsequently discarded. See note 30, supra.

An indication of the trend of the New York opinions may be obtained from Halstead v. Schnitzpahn, 152 N. Y. Supp. 561 (1915), a decision by Woodward, J., at a Special Term of the Erie County Supreme Court, where the court vacated a temporary injunction restraining defendant from violating a contract to sell certain patented mechanical devices to the plaintiff, on the expressed ground that the difficulty of establishing the measure of damages, the invention being new and untried, did not, in the absence of any allegation of defendant’s insolvency, establish irreparable injury. In Fox v. Fitzpatrick, 190 N. Y. 259, 82 N. E. 1103 (1907), the court in denying specific performance of an agreement for the sale of trees, some standing and some cut, because the damages could readily be calculated, had stressed the fact of the solvency of two of the defendants; “Ball and Sherman were insolvent, so that a right of action against them was of no value, but both the milling companies were solvent.”

Doty v. Doty, 171 N. Y. Supp. 852 (1918), a decision of the Special Term of Schoharie County, although not a case of specific performance, involved the same principle. There plaintiff’s husband, after deserting her, had agreed to and did provide her with a lot and house. The house burned, and the husband refused to rebuild or furnish another house, and claimed the proceeds of the fire insurance policy as his individual property. The action was to enjoin the insurance company from paying the fire loss to the husband. The court dismissed the complaint. “While the plaintiff in her complaint alleges that she has no adequate remedy at law, she nowhere alleges that the defendant, Job Doty is insolvent. * * * The damages are clearly ascertainable, and may be
The learned editor of the *fourth* edition of Pomeroy's "Equity Jurisprudence", speaking of specific performance of contracts for the sale of ordinary chattels, states that "it is believed that in no case has insolvency alone been the ground for relief", although he adds that a few cases contain contrary *dicta*. Of the cases dismissed as *dicta*, however, there are some which base the granting of relief solely on the ground of insolvency. The rule is based by the editor of the fourth edition on two stated grounds: first, because the purchaser would be made a preferred creditor, and second, because inadequacy is to be judged from the nature of relief by way of damages in cases of a certain type, not from the difficulty of collection of damages in the individual instance. The grounds stated in justification of the rule are those usually urged in its support. The latter of these objections will certainly not appeal to jurists of the functional school in these days of realism in law and living; the former objection is subject to possible rebuttal by demonstration that the recognition of the superior equities of the plaintiff will not contravene the policy of the Federal Bankruptcy Act as expressed in the Act and in the decisions of the federal courts themselves.

The conclusion that specific performance should be granted against an insolvent seller in all cases is by no means a logically inevitable, or even ethically essential *sequitur* from the foregoing discussion. In the opinion of the writer it is an equitable doctrine, and logically permissible with proper regard for the requirement of coherence in judicial theory.

RALPH A. NEWMAN.

St. John's University School of Law.