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Bankruptcy - Summary Jurisdiction

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NOTES

BANKRUPTCY — SUMMARY JURISDICTION

Katchen, accommodation maker of notes given by a corporation, had sole control of a "trust account" in which corporate funds were placed after a disastrous fire. From this account Katchen made payments on the notes; within four months, the bankruptcy of the corporation occurred. Katchen presented two claims against the bankrupt, one for other payments, made on the notes from his personal funds and one for rent due. The trustee in bankruptcy asserted that the payments on the notes from the trust account were voidable preferences to Katchen under section 60 of the Bankruptcy Act,[1] and section 57g[2] required disallowance of claims of creditors holding voidable preferences. He then demanded summary judgment against Katchen for the amount of the preferences. Overruling Katchen's objection to the exercise of summary jurisdiction,[3] the referee rendered judgment for the trustee and ruled that Katchen's claims were to be allowed only after satisfaction of the judgment against him for the preference. The district court and court of appeal affirmed. The United States Supreme Court *held*, the Bankruptcy Act confers summary jurisdiction on the bankruptcy court to compel surrender of a voidable preference that under section 57g would require disallowance of the claim. *Katchen v. Landy*, 382 U.S. 823 (1966).

1. Bankruptcy Act § 60, 64 Stat. 24 (1950), *as amended*, 11 U.S.C. § 96 (1963): "*Preferred Creditors.* a. (1) A preference is a transfer as defined in this Act, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding under this Act, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class."

Katchen was alleged to be given a preference because payment on the notes inured to his benefit, he being an accommodation maker.

2. Bankruptcy Act § 57(g): "The claims of creditors who have received or acquired preferences, liens, conveyances, transfers, assignments or encumbrances, void or voidable under this Act, shall not be allowed unless such creditors shall surrender such preferences, liens, conveyances, transfers, assignments, or encumbrances."

3. The main reason the issue of summary versus plenary jurisdiction is important is that in the informal summary proceeding of the bankruptcy court, the right to jury trial is not allowed.

Prior to the instant case, the most restrictive view of summary jurisdiction to order a return of preferences void or voidable under the act, represented by *B. F. Avery & Sons v. Davis*,[4] held that the trustee might oppose claims under section 57g in a summary proceeding, but that in the absence of the claimant's consent, summary proceedings for return of property could be maintained only when at the time of bankruptcy the property in question was in the possession of or for the bankrupt, or where the claimant's claim to the property was merely colorable or sham. In *Avery* the court found no consent to summary jurisdiction and found that the property alleged to have been transferred preferentially was in the possession of the claimant under a substantial claim of right; therefore, summary proceedings were stayed until the preference issue could be tried by plenary proceeding in a non-bankruptcy court.

A more liberal view distinguished between permissive and compulsory counterclaim and allowed the bankruptcy court to grant affirmative relief summarily only in the latter case.[5] However, claimants in bankruptcy proceedings were found to consent implicitly to summary jurisdiction over compulsory counterclaims, because they would normally expect the court to consider evidence relevant to the claim.[6]

The third theory maintained that when one presents a claim to the bankruptcy court, one consents by implication to summary jurisdiction over all issues necessary to dispose of the claim in all cases where the trustee would have a 57g objection or where the counterclaim is related to his claim.[7]

In *Katchen* the Court reasserted its power to determine, in the absense of specific legislation, the scope of summary jurisdiction.[8] Finding Congress intended that bankruptcy proceed-

4. 192 F.2d 255 (5th Cir. 1951).

5. Permissive counterclaims as distinguished from compulsory are defined in FED. R. CIV. P. 13: "(a) *Compulsory Counterclaims*—A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim.

"(b) *Permissive Counterclaims*—A pleading may state as a counterclaim any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party's claim."

6. See Peters v. Lines, 275 F.2d 919 (9th Cir. 1960); Dwyer v. Franklin, 350 U.S. 995 (1956); *In re* Majestic Radio & Television Corp., 227 F.2d 152 (7th Cir. 1955); *In re* Solar Mfg. Corp., 200 F.2d 327 (3d Cir. 1952).

7. Interstate Nat'l Bank of Kansas City v. Luther, 221 F.2d 382 (10th Cir. 1955).

8. 382 U.S. at 328.

ings be as quick and inexpensive as possible,[9] the Court extended summary jurisdiction to encompass ordering a claimant to surrender a voidable preference that under section 57g would require disallowance of his claim.[10] Here, the claim for reimbursement for payment of corporate notes out of Katchen's personal funds was clearly related to the trustee's motion under 57g based on allegedly preferential payments made from the corporate trust account on the same notes; they arose from the same subject matter.[11] The Court would necessarily have to determine the preference issue in deciding whether 57g required disallowance of the claim, thus leaving nothing to be determined in a later plenary proceeding.[12]

Moreover, the Court indicated that *Katchen* does not reach the limits of summary jurisdiction, for the reason that summary jurisdiction will extend to claims where the 57g objection is to transactions *unrelated* to the claim.[13] Reliance on broad equity principles from *Alexander v. Hillman*[14] implies further that the Court may perhaps extend summary jurisdiction to all cases in which the claimant has presented a claim against the estate,[15]

9. *Id.* at 328.

10. *Id.* at 335.

11. *In re* Majestic Radio & Television Corp., 227 F.2d 152, 156 (7th Cir. 1955); *In re* Solar Mfg. Corp., 200 F.2d 327 (3d Cir. 1952).

12. The Court in *Katchen* clearly rejected the approach taken in *Avery*, in that in *Katchen* the Court said: "[O]nce it is established that the issue of preference may be summarily adjudicated absent an affirmative demand for surrender of the preference, it can hardly be doubted that there is also summary jurisdiction to order the return of the preference. This is so because in passing on a § 57g objection a bankruptcy court must necessarily determine the amount of preference, if any, so as to ascertain whether the claimant, should he return the preference, has satisfied the condition imposed by § 57g on allowance of the claim. . . . Thus, once a bankruptcy court has dealt with the preference issue nothing remains for adjudication in a plenary suit." 382 U.S. at 333-34.

13. If the dictum of *Katchen* is followed it will overrule the cases in note 6 *supra* to the extent that 57g objections will be extended to permissive as well as compulsory counterclaims, and the bankruptcy court will have summary jurisdiction over voidable preferences where the 57g objection could be sustained. Katchen v. Landy, 382 U.S. 323, 330 (1966). "The language of this section it will be observed, is concerned with *creditors* rather than *claims* and thus contemplates that allowance of a claim may be conditioned on surrender of preferences received with respect to the transactions unrelated to the claims. The exact reach of § 57g is not entirely settled . . . and that question is not involved here."

14. Alexander v. Hillman, 296 U.S. 222 (1935).

15. The Court in *Katchen* said that though *Hillman* is a case dealing with a receivership, what was said in *Hillman* is equally applicable to bankruptcy. In *Hillman* the Court was dealing with the issue of summary jurisdiction of four counterclaims some of which were permissive counterclaims. The Court in granting summary jurisdiction to all the counterclaims said: "It would seem that necessarily most of the issues in respect of the counterclaim will be quite similar to those litigated in the main suit. Unquestionably all matter in the controversies between the parties may be tried and determined more conveniently and promptly in the receivership court than elsewhere. . . . Nothing is more clearly a part of the main suit than recovery of all that to the 'res' belongs." Alexander v. Hillman,

even though the trustee might not invoke 57g. Such an issue was raised in *Katchen* but was not brought to the Supreme Court.

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BANKRUPTCY — UNRECORDED FEDERAL TAX LIENS — RIGHTS OF A TRUSTEE UNDER SECTION 70c OF THE BANKRUPTCY ACT

Trustee in bankruptcy sought to invalidate an unrecorded federal tax lien on the property of the bankrupt, alleging that section 70c of the Bankruptcy Act gave him the status of a "judgment creditor," thereby enabling him to prevail over the unrecorded tax lien. The referee invalidated the lien, and his decision was upheld by the district court and court of appeals.[1] The United States Supreme Court affirmed; *held*, a federal tax lien unrecorded at the time of bankruptcy is invalid against the trustee. *United States v. Speers*, 382 U.S. 266 (1965).

Since the trustee in bankruptcy represents general, or unsecured creditors,[2] his primary objective is to preserve as much of the assets of the bankrupt as possible for distribution to this class. To foster this objective and to protect the bankrupt estate against secret liens the trustee has been vested with title to the bankrupt's property superior to unrecorded liens.[3] The first significant legislation gave the trustee the rights of a creditor with a judicial lien on all property of the bankrupt in the custody of the court and with the rights of a "judgment creditor" as to all other property.[4] Three years later, by amendment of the prede-

296 U.S. 222, 242 (1935). The "res" in *Hillman* was the receivership, but by analogy in a bankruptcy case the "res" would be the bankrupt estate.

1. In the Matter of Kurtz Roofing Co., 335 F.2d 311 (6th Cir. 1964).

2. Bankruptcy Act § 44c, 30 Stat. 544 (1898), *as amended*, 11 U.S.C. § 110 (1958) [hereinafter cited as Bankruptcy Act]: "The creditors of a bankrupt . . . shall, at the first meeting of creditors . . . appoint a trustee." .

Bankruptcy Act § 56(b): "Creditors holding claims which are secured or have priority shall not . . . be entitled to vote at creditors meetings."

See also generally 2 COLLIER, BANKRUPTCY §§ 44.02-44.20 (14th ed. 1940) [hereinafter cited as COLLIER]; 3 COLLIER §§ 56.02-56.11.

3. The first of these statutes, Bankruptcy Act § 70a(5) was sharply limited as to its effectiveness by the case of York Mfg. Co. v. Cassell, 201 U.S. 344 (1906), which interpreted the provision to mean that the trustee was vested with superior title only where creditors existed who were similarly protected by state law. In 4 COLLIER § 70.48, at 1401, the author stated: "Since under the laws of many states, unrecorded mortgages, pledges, conditional sales, and the like, as well as many other types of secured transactions dangerous to creditors, are not valid except as to creditors who have levied upon or have fastened a lien on the property in dispute, the *York* case sharply limited the usefulness of the provisions of section 70a(5) . . . ."

4. 36 Stat. 838 (1910), now Bankruptcy Act § 70c. The purpose of this