Smith Vs. Kernochen

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Appeal No. : 48 U.S. 198

Appellant : Smith

Respondent : Kernochen

Judgement :

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Smith v. Kernochen

48 U.S. (7 How.) 198

ERROR TO THE CIRCUIT COURT OF THE UNITED STATES

FOR THE SOUTHERN DISTRICT OF THE STATE OF ALABAMA

SYLLABUS

When a mortgagor and mortgagee are citizens of the same state, and the mortgagee assigns the mortgage to a citizen of another state for the purpose of throwing the case into the circuit court, it is necessary, in order to divest the court

of jurisdiction, to bring home to the assignee a knowledge of this motive and purpose. Till then, he must be considered an innocent purchaser without notice.

If the assignment was only fictitious, then the suit would in fact be between two citizens of the same state, over which the court would have no jurisdiction.

The question of jurisdiction, in such a case, should have been raised by a plea in abatement. Upon the trial of the merits, it was too late.

A former suit in chancery between the original parties to the mortgage involving directly the validity of that instrument, in which suit a bill to foreclose was dismissed, upon the ground that the mortgage was void, was good evidence in an ejectment brought by the assignee claiming to recover by virtue of the same mortgage. The instrument had been declared void by a court of competent jurisdiction, and neither the parties nor their privies could recover upon it.

There is no difference upon this point between a decree in chancery and a verdict at law. Either constitutes a bar to a future action upon the instrument declared to be void. The authorities upon this point examined.

The highest court of the State of Alabama having decided that the original mortgagee (an incorporated company) violated its charter in the transaction which led to the mortgage, this Court adopts its construction of a statute of that state.

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The plaintiff below, Kernochen, a citizen of New York, brought an action of ejectment against the defendants to recover the possession of eleven hundred and sixty acres of land, situate in that state, and to which he claimed title.

On the trial it appeared that Archibald K. Smith, being the owner in fee of the premises, executed a mortgage of the same, on 9 April, 1839, to the Alabama Life Insurance and Trust Company, a corporation duly incorporated by the Legislature of the State of Alabama, to secure the sum of seven thousand five hundred dollars, payable in five equal annual payments, with interest. And, further, that the

mortgage had been duly assigned and transferred by that company to Kernochen, the plaintiff, in consideration of the sum of one thousand dollars, on 26 August, 1844. Possession being admitted by the defendants, the plaintiff rested.

It appeared, on the part of the defense, that the mortgage and bond accompanying it, with other securities belonging to the Life and Trust Company, were placed in the hands of Hunt, an agent of the company, to procure a loan of money in New York, and that one thousand dollars was loaned, at his instance and request, by the plaintiff to the company, for the security of which the assignment of the above mortgage was made. That the motive of the company in making the assignment was to obtain a decision of the federal courts upon the questions decided in the court below, but that Kernochen was not advised of the motive at the time of the advance of the money, nor was he in any way privy to it.

It further appeared, that a bill of foreclosure of the mortgage had been filed in the court of chancery of Wilcox County, State of Alabama, by the company, against Smith, the mortgagor, which was defended by him. In the answer he admitted the execution of the bond and mortgage, but denied their validity, setting out the consideration, which consisted of bonds and obligations of the company made and delivered to him for the like sum of seven thousand five hundred dollars, payable at a future day, with six percent interest. The mortgage in question bore eight percent.

The proofs taken in the case sustained the answer, and showed that the transaction between the company and the mortgagor consisted simply in an exchange of securities with each other, with an advantage to the former of two percent profit.

The chancellor decreed that the contract was valid, and the bond and mortgage binding upon the defendant, and that unless

the principal and interest were paid within thirty days, the mortgage be foreclosed.

Upon an appeal to the supreme court of the state, this decree was reversed, and a decree entered dismissing the bill. That court held that the charter of the Life and Trust Company conferred no authority upon it to lend its credit, or issue the bonds for which the mortgage in question was given, and that the bond and mortgage taken therefor were inoperative and void.

The charter of the company, together with several amendments of the same, were given in evidence.

When the evidence closed, the defendants prayed the court to charge the jury, that, if they believed that the transfer of the mortgage to the plaintiff was made for the purpose of giving jurisdiction to the federal courts, and to enable the company to prosecute its claim therein, and that the plaintiff was privy to the same, the deed was void, and did not pass any title to the plaintiff which the court would enforce.

The defendants further prayed the court to charge, that the judgment and decree of the Supreme Court of Alabama between the company and Smith, the mortgagor, was conclusive upon the parties in this suit, and that neither the mortgagees, nor those claiming under them, since the rendition of the decree, could recover the lands embraced in the mortgage at law or in equity.

The court refused to charge according to the above prayers, and charged as follows:

1. That any matters which might abate the suit should have been pleaded in abatement, and that, after the plea of the general issue, the facts proved by the defendants, as set forth in the bill of exceptions, could be of no avail, and were insufficient to abate the suit. And,

2. That the defendants, claiming title under Smith, the mortgagor, were estopped from denying the consideration of the mortgage as set forth in that instrument, and that the consideration as there stated was good, and valid, according to the charter of the company, and sufficient to sustain the validity of the mortgage and title of the plaintiff.

The jury found a verdict for the plaintiff.

A writ of error brought the case up to this Court.

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MR. JUSTICE NELSON, after reading the statement of the case prefixed to this report, proceeded to deliver the opinion of the Court.

We are of opinion, that the charge of the court below upon the question of jurisdiction was substantially correct.

It might have been placed upon ground less open to objection. The case admits that Kernochen, the plaintiff, was not chargeable with notice of the motive of the company in assigning the mortgage to a citizen of another state; he was not chargeable, therefore, with the legal consequences that might result from the existence of such knowledge. He advanced his money, and took the security in good faith, and became thereby possessed of all the title that belonged to the mortgagees, and had a right to enforce it in any court having cognizance of the same.

The most that can be claimed is that the company intended a fraud upon the eleventh section of the Judiciary Act, in seeking to obtain a decision of the federal courts upon the validity of the mortgage between themselves and the defendants, both parties residents and citizens of the same state, using the name of the plaintiff as a cover for that purpose. But admitting this to be so still, upon general principles, the rights of the plaintiff under the assignment could not be affected by the

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fraud, unless notice was brought home to him. Till then, he stands on the footing of a *bona fide* purchaser without notice.

But the charge, we think, may also be sustained upon the ground on which it was placed by the court below. For even assuming that both parties concurred in the motive alleged, the assignment of the mortgage, having been properly executed and founded upon a valuable consideration, passed the title and interest of the company to the plaintiff. The motive imputed could not affect the validity of the conveyance. This was so held in *McDonald v. Smalley,* 1 Pet. 620.

The suit would be free from objection in the state courts. And the only ground upon which it can be made effectual here is that the transaction between the company and the plaintiff was fictitious and not real, and the suit still, in contemplation of law, between the original parties to the mortgage.

The question, therefore, is one of proper parties to give jurisdiction to the federal courts, not of title in the plaintiff. That would be a question on the merits, to decide which the jurisdiction must first be admitted.

The true and only ground of objection in all these cases is that the assignor, or grantor, as the case may be, is the real party in the suit, and the plaintiff on the record but nominal and colorable, his name being used merely for the purpose of jurisdiction. The suit is then in fact a controversy between the former and the defendants, notwithstanding the conveyance, and if both parties are citizens of the same state, jurisdiction of course cannot be upheld. 26 U. S. 1 Pet. 625; 2 U. S. 2 Dall. 381; 1 Wash.C.C. 70, 80; 2 Sumner 251.

Assuming, therefore, everything imputed to the assignment of the mortgage from the company to the plaintiff, the charge of the court was correct. The objection came too late, after the general issue. For when taken to the jurisdiction on the ground of citizenship, it must be taken by a plea in abatement, and cannot be raised in the trial on the merits. *D'Wolf v. Rabaud,* 1 Pet. 476; *Evans v. Gee,* 11 Pet. 80; *Sims v. Hundley,* 6 How. 1.

But we are of opinion the court erred in giving the second instruction, which denied the conclusiveness of the decree in the bill of foreclosure against the right of the plaintiff to recover in this action.

The suit in chancery was between the original parties to the mortgage, and involved directly the validity of that instrument; it was the only question put in issue by the bill and answer, and the only one decided by the court. The mortgage was held to be void, on the ground that the bonds of the company which were given in exchange for it were illegal,

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and created no debt or liability for which a mortgage security could be taken or upheld; that every part of the transaction was beyond any of the powers conferred upon the company by its charter, and therefore wholly unauthorized and void. On these grounds, the court decreed that the bill be dismissed. The present is an action of ejectment, brought by the assignee of the complainants in that suit against defendants representing the interest of the mortgagor, and in which the right to recover depends upon the force and validity of the same instrument.

A mortgagee, or anyone holding under him, may recover possession of the mortgaged premises, after default, on this action, unless it appears that the debt has been paid, or is extinguished, or the mortgage security for good cause held ineffectual to pass the title. Here it has been shown to have been declared null and void by a court of competent jurisdiction, in a suit between parties under whom the present derive title, and in which, as we have seen, the question of its validity was put directly in issue. The case therefore falls within the general rule, that the judgment of a court of concurrent jurisdiction directly upon the point is as a plea, a bar, or as evidence conclusive between the same parties or privies upon the same matters, when directly in question in another court.

It is suggested on the brief submitted on the part of the plaintiff below, that a decree in equity between the same parties is not a bar to an action at law; and hence, that the decree in the bill of foreclosure in this case is no bar to the action of ejectment; and the case of the *Lessee of Wright v. Deklyne,* 1 Pet.C.C. 199, is referred to as sustaining that position. On looking into the case, it will be seen that the decree dismissing the bill, which was set up as a bar to the action of ejectment, was placed upon the ground that the complainant had a complete

remedy at law, and did not, therefore, involve the legal title to the property in question. The court said that if a complainant seeks in a court of equity to enforce a strictly legal title, when his remedy at law is plain and adequate, the dismissal of his bill amounts to a declaration that he has no equity, and the court no jurisdiction; but it casts no reflection whatever upon his legal title; it decides nothing in relation to it, and consequently can conclude nothing against it. It was admitted that the decision of a court of competent jurisdiction directly upon the point was conclusive where it came again in controversy.

The case of *Hopkins v. Lee,* 6 Wheat. 109, illustrates and applies the principle which governs this case. There, Hopkins purchased of Lee an estate, for which he agreed to pay

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$18,000; $10,000 in military lands at fixed prices, and to give his bond for the residue. The estate was mortgaged for a large sum, which encumbrance Lee agreed to raise. The whole agreement rested in contract. Hopkins filed a bill against Lee, charging that he had been obliged to remove the encumbrance, and claiming the repayment of the money, or, in default thereof, that he be permitted to sell the military lands which he considered as a pledge remaining in his hands for the money. Lee put in an answer denying the allegations in the bill, whereupon the cause was referred to a master, who reported that the funds with which Hopkins had lifted the mortgage belonged to Lee, upon which report a decree was entered accordingly. The suit in 6 Wheaton was an action of covenant brought by Lee against Hopkins, to recover damages for not conveying the military lands which he had agreed to convey upon the aforesaid encumbrance being removed. The defense was that the encumbrance had not been removed. And upon the trial, Lee relied upon the suit and the decree in chancery as conclusive evidence of the fact that he had complied with the condition, which was admitted by the court below, and the decision sustained here on error.

The court, after referring to the general rule, observed that a verdict and judgment of a court of record, or a decree in chancery, although not binding upon strangers,

puts an end to all further controversy concerning the points thus decided between the parties to such suit. In this there is, and ought to be, no difference between a verdict and judgment in a court of common law and a decree of a court of equity. They both stand on the same footing, and may be offered in evidence under the same limitations, and it would be difficult to assign a reason why it should be otherwise.

If any further illustration of the principle were necessary, we might refer to the case of *Adams v. Barnes,* 17 Mass. 365, where it appeared that a mortgagee had brought an action to recover possession of the mortgaged premises, in which the mortgagor had defended on the ground of usury, but, failing in the defense, the mortgagee had judgment. The mortgagor afterwards conveyed his interest to a third person, who brought a writ of entry against the mortgagee to recover the possession, relying upon the usury in the mortgage as invalidating that instrument, and rendering it null and void. But the court held the parties concluded by the previous judgment, the same point having been there raised and decided in favor of the mortgagee.

The same principle will be found in *Betts v. Starr,* 5 Conn. 550, where it was held that a judgment recovered upon a

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note secured by the mortgage, notwithstanding the plea of usury, precluded the mortgagor from setting up that defense again, in an action of ejectment by the mortgagee to recover the possession of the mortgaged premises.

Further illustrations of the principle will be found by referring to Cowent & Hill's Notes to Phillips on Ev., 804, note 558; and 2 Greenleaf on Ev., 528-531.

The case of *Henry Raguet v. Peter Roll,* 7 Ohio, 76, has been referred to as maintaining a different doctrine. That was a *scire facias* on a mortgage to charge the lands in execution. The defense set up was that the mortgage had been given to secure the payment of a note of five hundred dollars, which was made to the mortgagee to compound a felony. There had been a suit between the same

parties on the note, in which the same defense was set up and prevailed. The case is reported in 4 Ohio 400. But this former suit was not interposed or relied on in the *scire facias* on the mortgage, and the question here, therefore, was not involved in that case, and probably could not have been. For on looking into the report of the suit upon the note, it appears to have been brought originally in the common pleas, where the plaintiff recovered. This judgment was afterwards reversed by the supreme court on error, without any further order in the case. This left the parties and the note as they stood before the judgment in the common pleas. Cowen & Hill's Notes, 826, note 587.

There is another principle that would probably be decisive of this case, over and above the ground here stated, upon a second trial, arising out of the thirty-fourth section of the Judiciary Act, which provides that the laws of the several states, with the exceptions there stated, shall be regarded as rules of decision in trials at common law in the courts of the United States in cases where they apply.

The highest court of the State of Alabama has given a construction to the act of the legislature chartering this company, which we have seen is fatal to a recovery. It belongs to the state courts to expound their own statutes, and when thus expounded the decision is the rule of this Court in all cases depending upon the local laws of the state. 20 U. S. 7 Wheat. 361; 31 U. S. 6 Pet. 291.

It is unnecessary, however, to pursue this inquiry, as the grounds already mentioned are in our judgment conclusive upon the rights of the parties.

In every view we have been able to take of the case, we think the court erred in the second instruction given to the jury, and that the judgment below must be

Reversed.

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ORDER

This cause came on to be heard on the transcript of the record from the Circuit Court of the United States for the Southern District of Alabama, and was argued by counsel; on consideration whereof, it is now here ordered and adjudged by this Court, that the judgment of the said circuit court in this cause be and the same is hereby reversed with costs, and that this cause be and the same is hereby remanded to the said circuit court, with directions to award a *venire facias de novo.*