Sexton Vs. Kessler and Co., Ltd.

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Court : US Supreme Court

Decided On : May-27-1912

Appeal No. : 225 U.S. 90

Appellant : Sexton

Respondent : Kessler and Co., Ltd.

Judgement :

Sexton v. Kessler & Co., Ltd. - 225 U.S. 90 (1912)
U.S. Supreme Court Sexton v. Kessler & Co., Ltd., 225 U.S. 90 (1912)

Sexton v. Kessler & Company, Limited

No. 92

Argued December 12, 13, 1911

Decided May 27, 1912

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APPEAL FROM THE CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

SYLLABUS

The conduct of businessmen, acting without lawyers and in good faith, attempting to create a personal security for an actual debt should be fairly construed as actually effecting what the parties meant, and so *held* in this case that an escrow of securities made by a banking firm in New York to secure its drafts upon a foreign bank amounted to a lien on the securities to be preferred to the claim of the trustee in bankruptcy, notwithstanding that the New York firm retained physical power over the securities, as agent for the foreign house, and had the right to substitute other securities for those withdrawn and sold.

Under the decisions of this Court and the courts of New York, a customer has such an interest in securities carried for him by a broker that a delivery to him after the insolvency of the broker is not necessarily a preference under the bankruptcy law. *Richardson v. Shaw,* 209 U. S. 365 .

172 F. 535 affirmed

The facts, which involve the question of whether, under the Bankruptcy Act of 1898, certain transfers of securities b the bankrupt constituted a fraudulent preference, are stated in the opinion.

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MR. JUSTICE HOLMES delivered the opinion of the Court.

This is a bill brought by a trustee in bankruptcy to set aside an alleged fraudulent preference. The circuit court of appeals reversed a decree of the district court for the plaintiffs, and dismissed the bill. 172 F. 535. It will be enough for our decision to state the following facts: the appellee was an English company and the bankrupts a New York firm, intimately connected with it, which for many years had drawn upon it. In February, 1903, the English house requested the New York firm to set aside securities for their drawing credit. The New York firm wrote on June 30 that they had that day placed in a separate package in their safe deposit vaults

certain securities named, the package being marked, "Escrow for account of Kessler & Co., Limited, Manchester," adding, "This escrow is intended as a protection against our long drawings against your good selves." This letter was acknowledged, and it was added,

"If at any time you have the opportunity to realizing these securities or any part of them, you are at liberty to take them and to replace them by others of equal value, though in that case we should, of course, like to see rather better quality."

In

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December of the same year, the English house suggested a form of certificate as follows:

"We certify that we have specially set aside and hold for your account, on this, the 31st day of December, '03, as security for the drawing credit which you accord us, the following securities. Name secs. and market value."

This was conformed to, and the New York house also entered the securities and all substitutions on their loan book. Substitutions were made from time to time, and the English house notified. The securities always were either negotiable by delivery or indorsed in blank. They were marked and kept as stated in the letter upon a separate shelf of the New York firm's vault, and they never were removed except in 1905 and 1906, when they were taken to the office to be examined and checked off by representatives of the English company. Business went on in this way until the panic of 1907. On October 25 of that year, the stability of the New York firm being in doubt, it handed over the escrow securities to an agent of the English company then in New York, and he deposited them in a safe deposit vault in the name of the company. On November 8, a petition of bankruptcy was filed, and on November 27 the New York firm was adjudged bankrupt. Notwithstanding arguments to the contrary, it may be assumed that the arrangement between the parties was made in good faith and intended and believed to be valid, and, on the other hand, that at the time of the change of custody on October 25, within four

months of the petition, the New York firm was insolvent, and that the English company had reasonable cause to believe that a preference was intended if its rights began only on that date.

So far as the interpretation of the transaction is concerned, it seems to us that there is only one fair way to deal with it. The parties were businessmen, acting without lawyers, and in good faith attempting to create a present security out of specified bonds and stocks. Their

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conduct should be construed as adopting whatever method consistent with the facts and with the rights reserved is most fitted to accomplish the result. If an express declaration of an equitable lien, or, again, a statement that the New York firm constituted itself the servant of the English company to maintain possession for the latter, or that it held upon certain trusts, or that a mortgage was intended, or any other form of words, would effect what the parties meant, we may assume that it was within the import of what was done, written, and said. So the question is whether anything in the situation of fact or the rights reserved prevents the intended creation of a right *in rem,* or at least one that is to be preferred to the claim of the trustee.

The bankruptcy law by itself does not avoid the transaction. *Thompson v. Fairbanks,* 196 U. S. 516 ; *Humphrey v. Tatman,* 198 U. S. 91 , 198 U. S. 95 . A trustee in bankruptcy does not stand like an attaching creditor; he gets no lien by the mere fact of his appointment. *York Mfg. Co. v. Cassell,* 201 U. S. 344 ; *Zartman v. First National Bank of Waterloo,* 216 U. S. 134 , 216 U. S. 138 . The most obvious objection is that the continued physical power of the New York firm over the securities, and its right to withdraw and substitute, admittedly reserved, are inconsistent with a title or lien of the English house in any form. But the decisions of this Court and of New York agree that there may be title in a stronger case than this. When a broker agrees to carry stock for a customer, he may buy stocks to fill several orders in a lump; he may increase his single purchase by stock of the same kind that he wants for himself; he may pledge the whole block

thus purchased for what sum he likes, or deliver it all in satisfaction of later orders, and he may satisfy the earlier customer with any stock that he has on hand, or that he buys when the time for delivery comes. Yet, as he is bound to keep stock enough to satisfy his contracts, as the New York

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firm in this case was bound to substitute other security if it withdrew any, the customer is held to have such an interest that a delivery to him by an insolvent broker is not a preference. *Richardson v. Shaw,* 209 U. S. 365 ; *Markham v. Jaudon,* 41 N.Y. 235. So, a depositor in a grain elevator may have a property in grain in a certain elevator, although the keeper is at liberty to mix his own or other grain with the deposit, and empty and refill the receptacle twenty times before making good his receipt to the depositor concerned.

Whether enough has been done to give a right of any kind in certain property is a question of more or less. *See Union Trust Co. v. Wilson,* 198 U. S. 530 , 198 U. S. 537 . In the case of ordinary goods and chattels, where, for instance, a man mortgages his stock in trade as it may be from time to time, retaining possession and full power to sell and replace or not, as he sees fit, it well may happen that the security fails. *Skilton v. Codington,* 185 N.Y. 80; *Zartman v. First National Bank of Waterloo,* 189 N.Y. 267. So, a general promise to give security in the future is not enough. But the present was a more limited and cautious dealing. It was confined to specific identified stocks and bonds on hand, and purported to give an absolute present right, qualified only by possible substitution and perhaps by a right of partial withdrawal of the remaining securities had risen sufficiently in value. It purported not to promise, but to transfer, and the subject matter was not goods and chattels in the sense of the New York mortgage law, as we understand that law to be interpreted by the New York courts. The transaction was not void as against creditors, irrespective of attachment, as in *Knapp v. Milwaukee Trust Co.,* 216 U. S. 545 ; *Niles v. Mathusa,* 162 N.Y. 546. There can be no doubt, as was said by the court below, that, before the bankruptcy, the English house had an equitable right at least, to possession if it wanted it. While the phrase "equitable lien"

may not carry the reasoning further or do much more than express the opinion of the court that the facts give a priority to the party said to have it, we are of opinion that the agreement created such a lien at least; or, in other words, that there is no rule of local or general law that takes from the transaction the effect it was intended to produce. *Hurley v. Atchison, Topeka & Santa Fe R. Co.,* 213 U. S. 126 , 213 U. S. 134 . When the English firm took the securities, it only exercised a right that had been created long before the bankruptcy, and in good faith. Such we understand to be the law of New York, and, in the absence of any controlling statute to the contrary, such we understand to be what the law should be. *Parshall v. Eggert,* 54 N.Y. 18. *National Bank of Deposit v. Rogers,* 166 N.Y. 380.

Decree affirmed.