"The laws," says the celebrated BECCARIA, "are always several ages behind the actual improvement of the nation which they govern." This observation, while true of law in general, is particularly true of the criminal law.

SUPREME COURT OF TENNESSEE.

NASHVILLE TRUST CO. *v.* FOURTH NATIONAL BANK.

SYLLABUS.

Assignment for Benefit of Creditors—Set-off in Insolvency.—A bank held the notes of a depositor who became insolvent and made an assignment for the benefit of creditors. *Held*, that the bank had a right to set off the notes against the deposit, although the assignment occurred before their maturity.

The facts are sufficiently stated in the opinion of the Court.

E. H. EAST, ESQ., and J. C. MCREYNOLDS, ESQ., for appellants.

Messrs. DICKENSON and FRAZER for appellee.

OPINION OF THE COURT.

PITTS, Special Judge.—The Connell-Hall-McLester Company, a Tennessee mercantile corporation located at Nashville, executed a general assignment to the Nashville Trust Company, for the benefit of creditors, on the 4th day of June, 1891. The deed of assignment conveyed to the assignee all the property and assets belonging to the assignor company, schedules being annexed under oath, specifying, among other things, all moneys on deposit in the Fourth National Bank of Nashville. At the date of the assignment the assignor company had on deposit, subject to its check, in said bank, $5,222.66, and the bank held its four notes for borrowed money, due as follows:

One due July 3, 1891, for	$10,000 00
One due July 17, 1891, for	4,500 00
One due July 19, 1891, for	9,000 00
One due August 22, 1891, for	4,500 00
Making total of	$28,000 00

The bank, after the assignment was made and noted for registration, and on the same day it was made, with knowledge of the assignment, applied said deposit to the credit of the assignor upon its indebtedness to the bank on the above-stated notes. Within three days after the assignment the assignee drew its check upon the bank for the amount of the deposit, caused the same to be presented for payment, and payment was refused. The assignor is insolvent, and was insolvent at the date of the assignment, and will not pay its debts in full. On the 4th day of December, 1891, the assignee and the Fourth National Bank submitted an agreed case to the Chancery Court at Nashville for decision upon the foregoing facts; the assignee claiming, as stated in the agreed case, "that it had the right to collect the deposit, and that it still has such right, or, if it has not this right, that, in the *pro rata* distribution of the proceeds of the assets among the creditors of the Connell-Hall-McLester Company, it has the right to charge said bank with the sum so on deposit and appropriated, as so much cash received on its *pro rata* share of said proceeds upon its debt of $28,000;" and the bank claiming "that it had the right to appropriate said deposit in payment on said notes, prove its debt for the balance, and collect its *pro rata* share of the trust fund on said balance as other creditors, and that it now has such right." These questions were submitted for decision, with the agreement that costs should be paid by the losing party. The Chancellor held for the defendant, the bank, grounding his decision upon the doctrine of equitable set-off, and the complainant has appealed.

Two questions are now presented for decision. The first is whether the doctrine of equitable set-off applied, and gave to the bank, immediately upon the assignment being made and the insolvency of the assignor established, the right to have the deposit credited upon or allowed as a set-off against the indebtedness of the assignor not then due. The complainant's counsel argues, with much force and plausibility, that the mere fact that one of the parties to independent cross-indebtedness is insolvent constitutes

no ground for equitable set-off; that some connection of dependence, or "mutual credit," in addition to insolvency, is essential; that more especially is this so when the indebtedness of one of the parties is not due, and that, too, of the party who is seeking to obtain the set-off; that to apply the doctrine of set-off to such a case would be to allow a party to collect a debt before it is due, without the consent of his debtor, and thus violate the contract which the parties have made; and that in this case such a result would give the bank a preference over other creditors of the assignor, and violates the statute which provides for the equal *pro rata* distribution of the assets of insolvent debtors under general assignments, as well as the like statutory provisions in regard to insolvent corporations. On the other hand, it is argued with equal force and plausibility for defendant that insolvency is, of itself, a sufficient ground for equitable set-off, without any connection or "mutual credit" between the debts or parties; that connection and insolvency are separate and distinct grounds for such relief, each being alone sufficient; that, where insolvency exists, it makes no difference that the indebtedness on one side is not due, nor which party is insolvent, —whether the party seeking the set-off or the party resisting it; that, under the statutes providing for the equal *pro rata* distribution of the assets of insolvent persons and corporations, the assets of the insolvent, in respect to choses in action, are only the balances due the insolvent estate after deducting all proper credits, counterclaims and set-offs, as its liabilities are only the balances due from it, ascertained in like manner, and therefore that to allow the set-off claimed in this case is not to disturb, but to preserve and enforce, equality among creditors; and that to refuse it would be to give other creditors a preference over the bank, and work injustice to the latter by compelling it to pay in full what it owes to the insolvent, and take a *pro rata* on what the insolvent owes it.

The second question is, the indebtedness on both sides being due when the agreed case was filed, whether the bank has the legal right of set-off. On this question, in

addition to the contentions already suggested, it is insisted for complainant that the rights of the parties were fixed at the date of the assignment, and, the bank having no right to set-off at that date, it has not such right now; that the lapse of time did not enlarge defendant's right in this respect; and that the assignee represents the creditors of the assignor, and not the assignor only; and therefore that the assignee is not to be regarded as standing in the shoes of the assignor simply. On the other hand, it is insisted for defendant that the assignee takes, not only as a volunteer, subject to all the equities existing against the assignor, and not as a purchaser for value, but also as the personal representative of the assignor, and stands for and in the place of the assignor in all respects, except as to personal liability; that the agreed case is, in effect, a suit to recover the deposit by the Connell-Hall-McLester Company, by its assignee and personal representative, and that, the debts being mutual and all due, the bank has the legal right of set-off to the extent of the deposit.

Opposed as they are to each other, the positions of counsel are each supported by apparently well-considered cases on both of the general questions stated; but no adjudication of this Court, upon a similar state of facts, has been cited, nor is the Court aware of any case in this State in which the precise questions here raised have been decided. The adjudged cases in this country and in England, and the text-books founded upon them, are in hopeless and irreconcilable conflict on many of the points involved. Any effort to reconcile them would be utterly futile. There is no touchstone of reason that will distinguish and harmonize them upon any general principle applicable to all of them, for their antagonism is not apparent, simply, but real and fundamental. They but furnish one of the many illustrations of that diversity of judgment which is inherent in the minds of men, which often, out of substantially similar raw materials and general conditions, has founded and built up dissimilar systems of jurisprudence, and which too often proves a delusion and snare to the worshipper of mere precedent. We must therefore look for guidance to

our own State on the general subject, and to the principles involved, which appear to be sustained by reason and the weight of authority; and, first of all, it must be remembered that the doctrine of set-off, whether legal or equitable, is essentially a doctrine of equity. It was that natural justice and equity which dictates that the demands of parties, mutually indebted, should be set off against each other, and only the balance recovered, that gave birth to the idea of accomplishing the result in a judicial proceeding. The common law, for simplicity of procedure, determined otherwise, and held that each claim must be prosecuted separately. "The natural sense of mankind," says Lord MANSFIELD, "was first shocked at this in the case of bankrupts; and it was provided for by 4 Anne, Ch. 17, § 11, and 5 Geo. II., Ch. 30, § 28."[1] "In pursuance of these old statutes, and of the dictates of equity," says the Supreme Court of the United States in Carr *v.* Hamilton,[2] "the principle of set-off between mutual debts and credits has, for nearly two centuries past, been adopted in the English bankrupt laws, and has always prevailed in our own whenever we have had such a law in force on our statute book; and it mattered not whether the debt was due at the time of bankruptcy or not,"—citing authorities.

The jurisdiction of courts of equity over the subject of set-off was exercised before there was any statute upon the subject,[3] and has often been applied in cases not within the statutes.[4] By the civil law, from which the great body of our system of equity comes, a cross-debt was, by mere operation of law, without any act of the parties, extinguished. It was treated as an absolute payment. Courts of equity in this country, while not going so far, have accomplished the same results in numerous cases, by granting

[1] Gree *v.* Farmer, 4 Burrows, 2214, 2220, cited in 2 Story, Eq. Jur., § 1433.

[2] 129 U. S., 255, 256; 9 Sup. Ct. Rep., 295.

[3] Hawkins *v.* Freeman, 2 Eq. Cas. Abr., 10; Chapman *v.* Derby, 2 Vern., 117.

[4] Williams *v.* Davis, 2 Sim., 461; *Ex parte* Prescott, 1 Atk., 331; Lanesborough *v.* Jones, 1 P. Wms., 326; Greene *v.* Darling, 5 Mason, 207.

perpetual injunctions against judgments in favor of insolvent persons who were indebted in larger amounts to the judgment debtor,[1] and in other cases, where, on account of the non-residence of the judgment plaintiff, or for other reason, the defendant could not save the demand due himself except by setting it off against the judgment.[2] The Court, in all such cases, is governed, not by the statute of set-off, but by the general principles of equity,[3] and the general principle of equitable set-off seems to be allowed where the party claiming it appears, in good conscience, to be entitled to it, and no superior equity in favor of the party resisting it will be thereby defeated.[4] The same author says: "The natural equity, to have mutual, but unconnected, demands, between two parties who have been dealing with each other, set off, is, as a general rule, superior to the claim of any other creditor who has not dealt with the insolvent upon the faith of specific fund against which the right of set-off is claimed."[5] With these general principles in view, we proceed to examine the reasons urged in arguments for and against the application of the doctrine of equitable set-off in this case.

And, *first*, as to the capacity in which the complainant stands before the Court. Is the Nashville Trust Company to be regarded as standing in the shoes of its assignor, the Connell-Hall-McLester Company, or upon different and higher ground? On the first point the authorities are in harmony; but we are of opinion that reason and the weight of authority support the view that an assignee for the benefit of creditors takes the choses in action of his assignor, not as a purchaser for value, but as a volunteer, and therefore subject to all the defences and equities existing against them in the hands of the assignor; and not only so, but that he holds as the representative of the assignor

[1] Brazelton *v.* Brooks, 2 Head, 193; Hough *v.* Chaffin, 4 Sneed, 238.

[2] Gregory *v.* Hasbrook, 1 Tenn., Ch. 220; Edminson *v.* Baxter, 4 Hayw., Tenn., 112; Wat. Set-off, § 431.

[3] Jeffries *v.* Evans, 43 Amer. Dec., 158.

[4] Wat. Set-Off, § 439.

[5] *Ibid.*, § 438.

and his estate, and in this respect is to be distinguished from a particular assignee, holding for himself, either as volunteer or purchaser.[1] He receives the legal title, not for himself, but in trust, to collect and disburse to creditors. All rights of action of the assignor pass to him for this purpose; and to all suits against the assignor's estate, and which are to affect the assets in his hands, he must be a party. This is the estate, and these are the functions, of an ordinary administrator or personal representative. It is frequently said of such an assignee that he represents the creditors, as it is said of an administrator, where the estate is insolvent, that he represents creditors, and, where it is solvent, that he represents distributees; and in the sense in which it is so said it is true. But by this is manifestly meant no more than that the representative's ultimate accountability is to the classes of persons who stand to him in the relation of beneficiaries, who are ultimately to receive the fruits of the trust he is administering, whether it be the estate of a living or dead person or that of a corporation. His right to maintain suits upon the choses in action, passed to him from the assignor by the assignment, obviously rests upon the fact that he represents the assignor, in whom were vested originally the title and right of action. This title and this right of action were never vested in the creditors, and did not come to the assignee from them.

Secondly, as to insolvency. Is insolvency of itself a sufficient ground for the application of equitable set-off? "It is deducible from the general scope of the authorities," says Mr. WATERMAN, "that insolvency has long been recognized as a distinct equitable ground of set-off."[2] Numerous authorities are cited by the learned author, but it is

[1] Burrill, Assignm., § 391; Receivers *v.* Paterson Gas-Light Co., 23 N. J. Law, 283; Saunders *v.* Nevil, 2 Vern., 428, note 1; Mitford *v.* Mitford, 9 Ves., 100; Brown *v.* Heathcote, 1 Atk., 162; Clason v. Morris, 10 Johns., 540; Murray *v.* Lylburn, 2 Johns., Ch. 443.

[2] Wat. Set-Off, § 432.

not deemed useful or necessary to review them, as this Court has repeatedly so held.[1]

Thirdly, as to the fact that the indebtedness on one side is not due when the set-off is claimed. It seems to be conceded by counsel for complainant that the indebtedness from the party claiming the right of set-off is not due would constitute no obstacle, as he might be allowed, if he chose, to expedite payment of a debt due from himself, without doing any injustice to the opposite party. But it is earnestly insisted that it is quite different where it is the debt against which the set-off is claimed that it is not due; that in such case to allow the set-off, and thereby compel payment of a debt not due, without the consent of the debtor, is to violate the contract of the parties, and work injustice to the debtor, whose demand is thus anticipated and collected before maturity. The argument is persuasive, and not without the support of respectable authority. Spaulding *v.* Backus,[2] Hannon *v.* Williams,[3] Jordan *v.* Bank,[4] Lockwood *v.* Beckwith[5] and Wat. Set-Off[6] —all seem to support this position, as do other cases not cited. The most of these and like cases seem to be, and many of them are, expressly based on the principle stated and illustrated in Poth,[7] as follows: "I am your debtor for six pipes of wine, of a particular vintage; you are my debtor for six pipes of wine generally. I may demand the six particular pipes, and therefore you cannot offset the general debt for six pipes; but I may offset my particular pipes, if I please, against yours, because I could turn them out to you in payment of the general debt." It is obvious that this illustration does not involve any principle of equitable set-off. It is only the statement of the general principle, applicable, not only to the law of set-off,

[1] Brazelton *v.* Brooks, 2 Head, 193; Hough *v.* Chaffin, 4 Sneed, 238; Gregory *v.* Hasbrook, 1 Tenn., Ch. 220; Edminson *v.* Baxter, 4 Hayw. (Tenn.), 112; Richardson *v.* Parker, 2 Swan, 529; Moseby *v.* Williamson, 5 Heisk., 287; Comfort *v.* Patterson, 2 Lea, 670; Machine Co. *v.* Zackary, 2 Tenn., Ch. 478; Catron *v.* Cross, 3 Heisk., 584; Smith *v.* Mosby, 9 Heisk, 501; Fiedds *v.* Carney, 4 Baxt., 137.

[2] 122 Mass., 553. [3] 34 N. J. Eq., 255. [4] 74 N. Y., 467.

[5] 6 Mich., 168. [6] §§ 131, 132. [7] Obl., 590.

but to contracts as well, that an obligation payable in one commodity cannot be paid in another without the consent of the payee. At most, as applied to the case in hand, it means that a debtor whose debt is due has no right, nothing more appearing, to set off against it a debt in his favor, not due; but this is only stating a general rule of legal set-off, everywhere conceded. The fact of insolvency of one of the parties is not involved. In the absence of insolvency, or some equivalent equity, it will not be anywhere contended that a debt not due can be set off against a debt that is due, any more than that six pipes of wine generally can be set off against six particular pipes of wine.

The case of Spaulding *v.* Backus, *supra*, relied on for the distinction under consideration, is not, strictly, an authority for the position; for while the learned Court does approve the distinction that a party cannot anticipate payment of an unmatured debt to himself, by setting off against it a debt due from himself, presently payable, notwithstanding the insolvency of the complainant, the suit in that case was by or for the benefit of an asignee by purchase, and the real question was whether a debt owing by the defendant to the assignor at the date of the assignment, though not then due, was to be regarded as an equity so attached to the assigned debt as to carry with it the right of set-off as against the assignee with notice of assignor's insolvency. The holding in the negative is not necessarily inconsistent with the right of set-off as between the original parties, and appears entirely consistent with the decisions of this Court, that a right of set-off, to be so attached to the debt as to be available against it in the hands of an assignee for value, must be complete and perfect at the date of the assignment. Gatewood *v.* Denton,[1] Litterer *v.* Berr,[2] Catron *v.* Cross,[3] Lockwood *v.* Beckwith, Jordan *v.* Bank, Hannon *v.* Williams, do fairly hold the proposition contended for by complainant's counsel. The effect of the sections cited from Wat. Set-Off is that the set-off will be allowed where the debt not due is in favor of the party against whom the right of set-off is asserted. It is only by implication that the learned

[1] 3 Head, 381. [2] 4 Lea, 193. [3] 3 Heisk., 584.

author can be treated as against the right in cases like the present. We cannot agree with these authorities, either in their reasoning or result. The question is, assuming the insolvency of the party owing the unmatured debt, can his debtor, when sued by the insolvent on a debt which is due, set off against it, in equity, the unmatured debt, because of the insolvency? We are of opinion that both reason and the weight of authority answer in the affirmative.

In connection with the general principle of equity before alluded to, that a set-off will be allowed when the party appears in good conscience to be entitled to it, and where no opposing equal or superior equity will be defeated —and we are treating the case now upon the idea that it is only the insolvent himself that is resisting—it must be remembered that it is only where, for some reason, the law cannot avail the party that equity intervenes at all. If both parties were solvent, so that both debts might ultimately be collected, the law would afford adequate relief, and no injustice would be wrought to either party. The one could not suffer by having to pay his own debt according to his contract, if he could ultimately compel the other to pay his debt according to his contract. But it is this very fact that, if the one pays the debt due from him, he cannot compel payment of the debt due to him, and will thereby suffer irreparable loss, and his inability to protect himself by set-off at law because his debt is not due, that create his equity, and the necessity for equitable relief. Does it lie in the mouth of an insolvent to say that his contract is violated, and thereby defeat so manifest an equity, when it is apparent that he cannot himself perform that contract? Should a court of conscience be so overscrupulous of the rights of one party to a contract as to refuse to permit a slight variance, even as to him, when it can plainly see that thereby it will wholly destroy the contract as to the other party? Technicalities are not to be so sweeping in their consequences. This Court looks to the substance, and not to the shadow of things. It is the very fact that the contract cannot be performed literally as made that calls upon the Court, *ex æquo et bono*, to compel such substantial performance as is possi-

ble. But it will be found, upon examination, that this objection may be urged with equal force in almost, if not in every case where the doctrine of equitable set-off has been applied. Take, for example, the cause of a judgment on the one side and a simple contract debt on the other. The judgment plaintiff is entitled to immediate execution and to collect his money at once. He does not have to await the law's delay and the expense of litigation. He has not only the right to demand his money, but to compel payment at once by final process, before the defendant can possibly obtain judgment, and place himself on equal footing in respect to the debt due him. He must await the delay of legal proceedings while the plaintiff in the judgment may, in the meantime, in the exercise of not only a contract right, but a contract right sanctioned by the final judgment of the court, proceed to collection at once. And yet it has never been considered that this right of a judgment plaintiff, if he is insolvent, stands in the way of equitable relief to the other party by injunction and set-off, although it cannot be said that there is here any less violation of the clear legal right than there is in setting off a debt not due against one that is due and payable.

The right of set-off in such and like cases is sanctioned by many authorities. In Jones *v.* Robinson,[1] approved in 2 Wat.,[2] it appeared that Jones had to his credit in bank a deposit of $924, at the time the bank failed and a receiver was appointed, and the bank held Jones' note for $391.43, which matured three days after the receiver was appointed. Held set-off proper. In Fera *v.* Wickham,[3] reported in 15 N. Y. Supp., 892, the right of set-off was upheld in a case like this, except that the parties were natural persons instead of corporations. In Schuler *v.* Israel[4] the Supreme Court of the United States approves the same doctrine in a garnishment proceeding; the syllabus, fairly supported by the opinion, on this point being: "A garnishee has a right to set up any defence against the attachment process which

[1] 26 Barb., 310. [2] Corp., § 371.
[3] Sup. Ct. N. Y., Oct., 1891.
[4] 120 U. S., 506; 7 Sup. Ct. Rep., 648.

he could have done against the debtor in the particular action, and if the debtor be insolvent, and owes the garnishee on a note not due, for which he has no sufficient security, he is not bound to risk the loss of his debt in answer to the garnishee process." The facts appearing in the answer of the garnishee, he was discharged. In Carr *v.* Hamilton[1] the same doctrine was applied between an insolvent life insurance company and the holder of an unmatured endowment policy, who was also indebted to the company for a loan, past due at the date of insolvency. In Kentucky Flour Co.'s Assignee *v.* Merchants' Nat. Bank (Ky.)[2] the doctrine was applied by the Supreme Court of Kentucky in a case precisely similar to this. Referring to the particular question now under consideration, the Court in that case say: "It is unquestionably the law that, as between individuals, the right of equitable set-off exists, although the debt had not matured at the time of the insolvency. Ordinarily, of course, a debt not due cannot be set off against one already due. To allow it would be to change the contract and advance the time of payment. But where the party asserting the due debt is a non-resident, or becomes insolvent, then either of these conditions, *ipso facto*, gives to the other party the right of equitable set-off, although his debt had not matured when the debtor became insolvent or the conditions arose giving the right of equitable set-off." We conclude, therefore, that insolvency is a good ground of equitable set-off, even where the indebtedness on one side is not due, and that it makes no difference in which party's favor is the unmatured debt. The supposed hardship or injustice resulting from the anticipation of the unmatured debt may and should be wholly obviated by discounting it, or adding interest to the due debt for the unexpired time of the debt not due, and in this way equalize the interest.

Fourthly, as to the effect of the statutes providing for the equal and ratable distribution among creditors of the assets of insolvents under general assignments, and of in-

[1] 129 U. S., 252; 9 Sup. Ct. Rep., 295.
[2] 13 S. W. Rep., 910.

solvent corporations. Without elaborating this question, it is sufficient to say we are of opinion that the position of defendant is the correct one. Under a similar statute, in reference to the estates of insolvent deceased persons, this court held in Richardson *v.* Parker[1] that it is only the balance remaining in favor of the estate, after all just settlements with debtors, that goes into the fund for distribution. These balances are the "assets," to which the statute refers. In that case a set-off was allowed to the debtor of an insolvent estate in a suit by the administrator against him; and, although it was a case of legal set-off purely, we are of opinion the principle announced applies equally to the case of equitable set-off. The Court has, in fact, shown a disposition to extend the principle to every case. It was so expressly extended to insolvent corporations in Moseby *v.* Williamson,[2] and to a general assignment by an insolvent bank, in Comfort *v.* Patterson.[3] It has also been recognized that the same principle is applicable to the estates of bankrupts under national bankrupt laws,[4] and the principle has been uniformly so applied by the bankrupt courts.[5] It is applicable to receivers of corporations, under State statutes.[6] Also to receivers of insolvent national banks.[7] And this, too, although the law of set-off is held not to have been enlarged by either the bankrupt or national bank acts. Sawyer *v.* Hoag,[8] Platt *v.* Bently, *supra.*

In these and numerous like cases the Court proceed upon the idea so well expressed by the New Jersey Court in Receivers *v.* Gas-Light Co.: "The object of the act is to do equal justice to all the creditors, and equality is equity. But equality of what and among whom? Clearly, of the

[1] 2 Swan, 529. [2] 5 Heisk., 287. [3] 2 Lea, 670.

[4] Richardson *v.* Parker, 2 Swan, 530; 5 Heisk., 287; 2 Tenn. Ch., 479, and cases there cited.

[5] Drake *v.* Rollo, 4 N. B. R., 689; *In re* City Bank of Savings, 6 N. B. R., 71; *In re* H. Petrie, 7. N. B. R., 332; 2 Vern. 428, note 1.

[6] Receivers *v.* Gas-Light Co., 23 N. J. Law, 283; Miller *v.* Receiver, 1 Paige, 444; McLaren *v.* Pennington, 1 Paige, 112.

[7] Platt *v.* Bently (N. Y.), 11 Amer. Law Reg. (N. S.), 171; Wait. Insolv. Corp., § 549.

[8] U. S. Sup. Ct., 1873; 17 Wall., 610.

assets of the bank among the creditors of the bank. In cases of cross-indebtedness, the assets of the bank consist only of the balance of the accounts. That is all the fund which the bank itself would have had to satisfy its creditors in case no receiver had been appointed. And there is no equality and no equity in putting a debtor of the bank, who has a just and legal set-off as against the corporation, in a worse position, and the creditors in a better position, by the failure of the bank and the appointment of receivers."[1] In that case, although the debt to the bank was not due at the time of failure and the appointment of receivers, the defendant was allowed, in a suit brought after maturity, to set it off against a debt due by him to the bank at the date of failure.

These considerations and authorities are equally conclusive against the argument of complainant that the rights of the parties were fixed at the date of the assignment. It is true they were fixed, in the sense that a debtor of the assignor could not thereafter purchase or acquire a debt against the assignor, and set it off against his own debt to the assignor.[2] Unless the debt was held at the date of assured insolvency, in case of a corporation, or at the date of the assignment of an insolvent debtor, or the death of an insolvent decedent, it cannot be set off.[3] If the estate be solvent, the set-off will be allowed, although acquired after the death of plaintiff's intestate.[4]

The second question presented by the agreed case is whether the legal right of set-off existed when the suit was commenced. The indebtedness on both sides being then due and mutual, under the rules herein announced, it would seem that the only question remaining is whether the agreed case is to be treated as, in effect, a suit to recover the deposit. We are of opinion that it must be so treated. We do not so hold simply because the assignee appears as complainant on the record and in the agreed statement. That

[1] McGinnis *v.* Allen, 2 Swan, 645.
[2] 5 Heisk., 287; 2 Swan, 529; 9 Heisk., 501, 506; 8 Baxt., 408.
[3] 2 Swan, 645.
[4] 23 N. J. Law, 294, 295.

is a circumstance, it is true; and, the case being a controversy between parties, one or the other must be regarded as the actor or complainant. Looking to the substance of the controversy and relief sought, it is seen that the assignee asserts the right to recover the deposit, in the first instance, or, if not, then to have the Court declare its right to charge up the amount of the deposit to the bank as so much cash paid on its *pro rata*, which is manifestly the same thing, as the statement shows the bank will be entitled to receive more than that amount in any event. On the other hand, the bank is seeking no decree at the hands of the Court, further than to have declared valid its previous act applying the deposit as a payment on the notes, or its right now to have it so applied; either right being sufficient to repel the assignee. We think, therefore, that the case is in effect a suit by the assignee to recover the deposit, commenced on the 4th day of December, 1891, and therefore that the Chancellor's decree, in its result, is supported by the bank's legal, as well as equitable, right of set-off; the original equitable right having ripened into and become a legal one before the suit was commenced.[1] The Chancellor's decree is therefore affirmed, and the assignee, out of the assets in its hands, will pay costs.

SET-OFF IN INSOLVENCY.

It was remarked in a recent case, with reference to the doctrine of set-off, that "Well-defined and easy of comprehension as the doctrine is, however, its application to the varying state of facts which arise is attended with the same degree of difficulty that attends the administration of other plain legal principles, under unusual circumstances." (Per BUTLER, J., in Yardley *v.* Clothier, 49 Fed. Rep., 337.) No state of facts presents greater difficulty to the application of this doctrine, and none has given rise to greater diversity of opinion amongst juridical writers as to its legal effect than the insolvency of one of the parties. It is not in every case, however, where one of the parties is insolvent, that this result follows, as, in its general features, insolvency presents no obstacle which interferes with the application of

[1] Keith *v.* Smith, 1 Swan, 92; Mill & V. Code, § 3628, subsection 1. Mill & V. Code, § 3628, provides: "The defendant may plead, by way of set-off or cross-action: (1) Mutual demands held by the defendant against the plaintiff at the time of action brought, and matured when offered in sett-off," etc.

this doctrine. Since the earliest bankrupt statute, that of 4 and 5 Anne, Ch. 17, there has been universally contained in that class of laws a provision that where there are mutual debts or mutual credits between the parties, the balance of the accounts shall constitute the true debt and shall be alone recovered.

Prior to the existence of these statutes, however, courts of equity were accustomed to exercise the doctrine of equitable set-off where, owing to the peculiar state of facts, it would have been inequitable to have permitted a creditor to have recovered the full amount of his claim without reference to any cross demand: Van Wagoner *v.* Patterson Co., 23 N.J. Law, 283, 1 Modern, 215.

Since the enactment of those statutes the courts have been accustomed to apply the doctrine of equitable set-off independently of the statutes, where its non-application would cause a result contrary to the universally accepted ideas of equity.

It is well settled that where a remedy at law is adequate and complete, the fact that it may prove ineffectual by reason of insolvency of the defendant, confers no jurisdiction upon a court of equity.

But in the distribution of the estates of insolvents, there is a disposition upon the part of many of the courts to hold that mere insolvency of a person, without the support of other circumstances, is sufficient to permit a court to exercise its equitable powers of set-off, and, as shown by the principal case, they have gone so far as to permit a debt not due to be set off against one already matured. Upon this point much conflict exists, however, and the question is not yet free from doubt in those jurisdictions where there has been no express declaration upon the subject.

Three classes of cases have arisen, calling for the application of this doctrine in cases of insolvency:

I. Where at the time of insolvency both the debt due to the insolvent and that due from him had fully matured.

II. Where at the time of the insolvency the indebtedness owing by the insolvent was fully due and payable, but the debt due to him had not matured.

III. Where at the time of insolvency the indebtedness to the insolvent was due and payable, but that owing by him had not matured.

(1) The first of these cases, where both debts are due and payable at the time of insolvency, presents no difficulty. It will be observed that in those States where bankrupt laws are in force, the provision that where mutual debts and mutual credits exist, the balance of accounts shall constitute the true debt, covers this case completely. Where no such statutes exist the courts will, in the exercise of their chancery powers, permit only the balance due to be recovered under these circumstances: Light *v.* Leininger, 8 Pa., 403; McDonald *v.* Webster, 2 Mass., 498.

The debt which it is proposed to set off must, however, be one which was owing to the defendant at the time of insolvency. The acquisition, subsequent to that time, of a claim owing to another person at the time of insolvency gives no right of set-off. Irons *v.* Irons, 5 R. I., 624; Northampton Bank *v.* Balliet, 8 W. & S., 317; Pass *v.* McRea, 36 Miss., 143.

To the general rule, that where

both debts are payable at the time of insolvency set-off is allowed, there are exceptions which arise out of the peculiar relations prevailing between the parties.

A depositor in an insolvent savings bank, who is also a debtor to the institution for money borrowed from it, is not entitled to offset the amount of his deposit against his indebtedness. These decisions are based upon the ground that the debt owed by the depositor belongs in fact to all the depositors, but neither the bank nor the depositors owe him anything more than his just proportion of the assets owned by the bank: Hannon *v.* Williams, 34 N. J. Law, 255; Stockton *v.* Mechanics' Savings Bank, 5 Stewart Eq. (N. J.), 163; Osborne *v.* Byrne, 43 Conn., 155. The same exception has also been made in the case of members of a mutual insurance company, the courts holding that a member of such company cannot setoff any indebtedness of the company to him in a suit against him to recover unpaid assessments: Hillier *v.* Allegheny Mut. Ins. Co., 3 Pa. St., 70; Lawrence *v.* Nelson, 21 N. Y., 158; Sawyer *v.* Hoag, 17 Wall, 610.

(2) The second class of cases, where the debt from the insolvent is due at the time of insolvency, but the debt to him matures subsequently, is free from difficulty. In the absence of controlling statutory regulations, where at the time of insolvency the proposed set-off was due, it has always been allowed, irrespective of the fact whether the debt to the insolvent had then matured or not: Jordan *v.* Sherlock, 84 Pa., 366; Skiles *v.* Houston, 110 Pa., 254; Yardley *v.* Clothier, 49 Fed. Rep., 377; Houston *v.* Nicholson, 4 Camp., 342; Van Wagoner *v.* Patterson Co., 23 N. J. L., 283; Platt *v.* Bentley, 11 Am. Law Reg., N. S., 172; Smith *v.* Felton, 43 N. Y., 19; *In re* Receiver of Middle District Bank, 1 Paige, 585; Miller *v.* Receiver of Franklin Bank, 1 Paige, 444; Hade *v.* McVey, 31 Ohio St., 231; American Bank *v.* Wall, 56 Me., 167; Colt *v.* Brown, 12 Gray, 233.

To this rule an exception has been made in the cases of insolvency of national banks. In Armstrong *v.* Scott, 36 Fed. Rep., 63, it was held that in such cases a depositor could not set off his deposit against his indebtedness to the bank, maturing after insolvency, as it was prohibited by Section 5242 of the Revised Statutes, which makes all payment of money by a national bank to its shareholders or creditors, after the completion of its insolvency, or in contemplation thereof, "with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another, except in the payment of its circulating notes," utterly null and void. SAGE, J., said: "The unmistakable force and meaning of the law is to place all creditors upon the same footing of equality. When the plaintiff was appointed receiver, the defendant was in the list of unsecured depositors, to whom payment, the bank being insolvent, was prohibited. The defendant had then no right of set-off, nor any equity against its note, not then matured, which had passed to the receiver." To the same effect is Stephens *v.* Schuchman, 32 Mo. App., 333.

The same question came before the Circuit Court of the United States, Eastern District of Pennsylvania, in Yardley *v.* Clothier, 49

Fed. Rep., 337, and in an opinion by BUTLER, J., in which ACHESON, J., concurred, a conclusion directly opposite to that of Armstrong *v.* Scott, *supra*, was reached. That case was carefully examined, but was not followed, the Court being of opinion that the allowance of set-off would not create any preference among creditors prohibited by Section 5242 of the Revised Statutes. To the same effect is Platt, Receiver, *v.* Bentley, 11 Am. L. Reg., N. S., 171. These decisions seem to be more in accord with the current of authorities than Armstrong *v.* Scott, *supra*.

In this class of cases an attempt has sometimes been made by the debtor of an insolvent estate, whose debt was due at the time of insolvency, to restrain the representative of the insolvent from disposing of a note or other indebtedness held by the insolvent at the time of insolvency, but not then payable.

In Lindsay *v.* Jackson, 2 Paige, 581, in May, 1831, the complainants gave to the defendant two negotiable notes for the sum of $1,500 each, payable in six months, with interest. About the same time the defendant became indebted to the complainant, on an acceptance of $4,000, payable on June 13, 1831. A few days before this acceptance became due, the defendants became insolvent. In July, 1831, the complainants filed their bill to restrain the defendants from transferring the notes, and praying that the amount to become due thereon might be set off or applied in part satisfaction of the $4,000 due on the acceptance. The injunction was granted. Although in this case the debt of the complainants was not due at the time of insolvency, it is doubtful whether it can be considered as an authority to that extent, as the question was not discussed. The debt to the complainants was due at the time of suit, and it was expressly stated that if the debt to the complainants was not due it could not be set off. No distinction was made between the time of insolvency and the time of suit. That this is the extent of Lindsay *v.* Jackson as an authority is shown by Smith *v.* Felton, 43 N. Y., 19.

In *In re* Commercial Bank, 1 Chan. App., 538, a different conclusion was reached. In that case the debt from the insolvent bank to Smith, Fleming & Co. was due at the time of insolvency. The bank held notes of Smith, Fleming & Co., which were not due until some subsequent time. The Court refused to restrain the official liquidator from transferring the notes, although it was acknowledged that if the notes had been held by the official liquidator until maturity, Smith, Fleming & Co. could have set off the amount of their deposit against the amount of the note.

(3) The right to set off the debt of an insolvent which matures subsequent to insolvency, against a debt due to him at that time, is involved in so much doubt as to fully warrant the statement in the principal case, that "the cases are in hopeless and irreconcilable conflict on many of the points involved. An effort to reconcile them would be futile."

At law, insolvency has no effect whatever upon the question of set-off; but in equity it has always been recognized as allowing its application, either when connected with other circumstances, or where the claims are due, but the damages are not liquidated. Whether in-

solvency alone, without the presence of other facts conferring jurisdiction upon a court of equity, will warrant the application of the doctrine of equitable set-off, is a question where great diversity of opinion exists.

In the principal case, after a careful consideration of the subject, the Court arrived at the conclusion that insolvency alone is sufficient ground to permit a court to exercise its powers of equitable set-off, and that it would be inequitable and unjust to compel a person occupying the dual position of debtor and creditor of an insolvent estate to pay his indebtedness to the estate in full and receive only a *pro rata* share of his claim against the estate, simply because at the time of insolvency the indebtedness against the insolvent had not matured.

This doctrine has received much support, and is applied in Aldrich *v.* Campbell, 4 Gray, 284; McDonald *v.* Webster, 2 Mass., 498; Bigelow *v.* Folger, 2 Metc., 255; Bemis *v.* Smith, *Ibid.*, 194; Denmon *v.* Boylston Bank, 5 Cush., 194; Berrigan *v.* Pearsall, 46 Conn., 276; Carter *v.* Compton, 79 Ind., 37; Clark *v.* Hawkins, 5 R. I., 219; Green *v.* National Security Bank, 6 W. N. C. (Pa.), 399.

In Campbell *v.* Aldrich, *supra*, THOMAS, J., says: "This case is not to be determined upon the technical rules of set-off, but upon the principles regulating the settlement of insolvent estates, whether of persons living or deceased. The settlements with such estates are final, and all mutual demands are to be balanced. Claims not liquidated and debts, though not absolutely due, though payable in the future, are to be included. The balance found upon such adjustment is the only debt remaining. In the case of an insolvent estate of one deceased, all claims existing at the time of the death are to be set off; in the case of an insolvent estate of a person living, all claims existing at the time of the first publication of the notice of the issuing of the warrant may likewise be set off." In Greene *v.* National Security Bank, *supra*, ELCOCK, J., said: "If any equity springs from the fact of Stewart's insolvency in favor of the bank, then it can hold, or stop, or defalcate, or set off, or defend to that extent. The relationship between the bank and its depositor or customer is simply that of debtor and creditor, for no ear-mark follows the deposit and the banker uses the same for the general purposes of his business. The bank becomes a creditor of the maker of the notes when it discounts the same, and his debtor when he makes the deposits. The maker's debt is created when he issues his notes; it is true that the time to maturity is his right before payment can be demanded, but the debt exists from the time of issuing the note. The maker has an undoubted right to waive this time and anticipate it by payment. Where a maker becomes insolvent and makes a general assignment for the benefit of his creditors, is it unreasonable to say that he waives further time upon his credit and, expressing his insolvency or inability to pay them at maturity, by such act matures all his debts? He has the power; do not his acts show its exercise? Time on his note is of no further importance to him, and his other creditors have no greater rights than he has granted them."