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Note and Comment

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NOTE AND COMMENT

THE DEATH OF PROFESSOR KNOWLTON.—The loss to the Law School and to his colleagues of the law faculty in the death of Jerome Cyril Knowlton cannot be expressed. For thirty-one years, the longest period of active service ever given by any man to this Law School, Mr. Knowlton was an effective factor in the development of the institution and in the moulding of the character and the legal ideas and ideals of the thousands of graduates who have passed through the Law School into the service of community and state and country, at the bar, upon the bench, in legislative halls, and indeed in all of the walks of life. Few if any men now living have been known to as many law students as was Mr. Knowlton. And few indeed are they whose influence has been as widely felt, for he made a vivid and lasting impression upon all who came in contact with him.

Wherever one goes among Michigan men or indeed among lawyers anywhere in the United States he finds affectionate friends of "Jerry" who inquire eagerly about his health and whether he still passes with ostensible ferocity, but with nevertheless obvious kindliness, from man to man in steady procession about the benches in the old rooms. He had a friendly interest in and about everyone, a pungent wit and an incisive and homely wisdom which were among the qualities which endeared him to all. The stories

exemplifying these qualities are many. Two or three of them may serve to recall the very atmosphere of his genial life to those who long ago passed out of the lecture rooms of this old building. The instance of the fiery young Southerner who in the old days threatened to shoot because of some fancied slight is in point. While the infuriated young man was surrounded by a group of half-frightened and half-angry students, and when the situation was very tense, "Jerry" proceeded from his office with the peculiar inimitable gait known to all who ever saw him, and remarked, "Young man, if you shoot you'll shoot a hole through your diploma," and walked away with the perfect assurance that he had punctured a situation laden with more of *grotesquerie* than of real danger.

The writer of this brief appreciation will never forget the amused embarrassment with which Mr. Knowlton asked his good offices in inducing the class in contracts two or three years ago to abstain from the old custom of presenting him with smoking material at Christmas-time. Each succeeding class in its affection for him had presented a larger supply of the Virginia flower until the quantity had become huge. And as "Jerry" humorously remarked he deeply appreciated the feeling of the boys but he did not know whether his reputation would stand any further augmentation of this annual inundation. On another occasion the present Secretary of War, Mr. Baker, was a speaker in the Law School and met the members of the law faculty prior to his address. When Mr. Knowlton's introduction came Mr. Baker looked at him quizzically and said, with his genial smile, "Are *you* Jerry?" Mr. Knowlton was pleased, and in his quick, staccato way said, "Yes, but have I ever met you before?" "No," said Mr. Baker, "but during all of my professional life I have met able lawyers who spoke affectionately of their old teacher, Jerry."

Mr. Knowlton's charm, his influence and the vivid impression he made upon all proceed from qualities which perhaps defy successful analysis. He had a remarkably keen legal mind, a wholesome common sense, a pleasing manner and a kindly and pleasant smile. But these may all be summed up in the one word "personality." This, of the most attractive and individual kind, he had in high degree, and it endeared him to us all. We shall miss him more than we can say.

The following resolutions were adopted by the faculty of the Law School at a meeting held after Professor Knowlton's death:

On Tuesday evening, December 12, 1916, Providence removed from our number the oldest member in point of service of our Law Faculty by the death of Jerome Cyril Knowlton. Mr. Knowlton began his connection with the Law School in 1885, serving as assistant professor of law until 1889, and from 1889 to 1916 as Marshall professor of law. He was elected acting dean in 1890 and dean of the School in 1891, serving in that capacity until 1895. He served the School continuously and actively longer than anyone who has heretofore been connected with it.

Be it Resolved, by us who remain

First, That there has been thus taken away from among us one of our most effective teachers, greatly and justly loved by many successive generations of students.

Second, That we have lost a most genial and gentle friend and co-worker.

Third, That the University has lost one who by the qualities of his mind and heart and the faithful and high character of his work and service added much to the reputation and esteem in which the University is held by great numbers of its alumni and friends.

Fourth, That the teaching and legal professions have both lost an unusually clear thinker, a very keen analyst, and an original, lucid and forceful expositor.

Fifth, That the community in which he lived and moved and worked so long has lost an upright and exemplary citizen.

Sixth, That a copy of these resolutions be entered in the minutes of the meetings of the Faculty of the Law School and copies be sent to the family, the President, and the Board of Regents.

THE LAW SCHOOL.—Although the effect of the increased requirements for admission to the Law School is still apparent in the lessened total enrollment, a marked increase in numbers in the entering class is to be noted this year, the present first year class being more than twenty per cent. larger than that of last year.

The total enrollment includes students from forty-one states and territories and two foreign countries; and ninety-three colleges and universities are represented, as follows:

University of Michigan, 221; Albion College, 6; Hope College, University of Wisconsin, 5; Kansas University, Leland Stanford University, State University of Iowa, University of Indiana, 4; Adrian College, Alma College, Bucknell University, Mt. Union College, Pennsylvania State College, State College of Washington, University of Arkansas, University of Illinois, Yale University, 3; Baker University, Colorado College, Cornell University, De Pauw University, Kalamazoo College, Marietta College, Ohio State University, Ohio Wesleyan University, Princeton University, University of Mississippi, University of Missouri, University of Oklahoma, Valparaiso University, Wabash College, 2; Allegheny College, Amherst College, Antioch College, Brown University, Central Michigan State Normal, Central University of Kentucky, Colgate College, College St. Xavier, Dartmouth College, Dickinson College, Drake University, Fisk University, Franklin & Marshall College, Georgia School of Technology, Gonzaga University, Grinnell College, Hanover College, Harvard University, Hillsdale College, Hiram College, Huron College, Illinois College, Jas. Milliken University, Juniata College, Lafayette College, Lake Forest University, Lawrence College, Lehigh University, Marion (Ind.) Normal, Mercer University, Miami College, Michigan State Normal, Muhlenberg College, Northwestern University, Oklahoma Normal, Olivet College, Pennsylvania State Normal, Pomona College, Reed Col-

lege, St. John's University, St. Mary's College, St. Viator's College, Silliman Institute, South Dakota State College, Trinity College, University of California, University of Chicago, University of Colorado, University of Detroit, University of Montana, University of South Carolina, University of South Dakota, University of Tennessee, University of Virginia, University of Washington, Washington & Jefferson College, Western Reserve University, Western (Mich.) State Normal, Whittier College, Williams College, Wm. Jewell College, William & Vashti College, 1.

THE PATENTABILITY OF A PRINCIPLE OF NATURE.—The extent to which courts will go in conceding patentability to a natural law, or principle of nature, is evidenced in the case of *Minerals Separation Co.* v. *Hyde*, 37 Sup. Ct. —, decided by the Supreme Court, December 11, 1916. It has always been more or less an axiom of patent law that the discovery of a principle of nature does not entitle the discoverer to a patent for it. The case usually thought of first as authority therefor, is that of *Morton* v. *New York Eye Infirmary*, 5 Blatch. 116, 2 Fisher 320. The patentees in that case had discovered that the inhalation of sulphuric ether would produce insensibility to pain. The ether itself was well known and the means by which the patentees induced it to the lungs was not new. It was the effect produced by its induction to the lungs which, alone, had been theretofore unknown. On this showing the court held the patent to be invalid, saying, "A discovery of a new principle, force, or law, operating, or which can be made to operate, on matter, will not entitle the discoverer to a patent." "The new force or principle brought to light must be embodied and set to work, and can be patented only in connection or combination with the means by which, or the medium through which, it operates." Another frequently cited case upon this proposition is that of *O'Reilly* v. *Morse*, 15 How. 62. The eighth claim of the patent involved in that case was for "the use of the motive power of the electric or galvanic current, which I call electro-magnetism, however, developed for marking or printing intelligible characters, signs or letters at any distances, being a new application of that power of which I claim to be the first inventor or discoverer." This claim was held invalid, on the ground that it was too broad and did not describe any means by which the force was to be utilized.

In the *Morton* case, patentability was denied the discovery despite the court's statement that a new force or principle could be patented in connection or combination with means through which it was made to operate. Two reasons for this denial are possible of deduction from the case—though no reason is explicitly stated. One is that the principle was not in reality a principle at all, but was itself the result, the end sought. It could not, in this view of it, be considered as operating "in connection with" any means. It must have been not a correlated "means," but the "effect" of some means. In this view, the statement of the court is sound, but quite irrelevant to the question before it. The other possibility is that the court believed the means in connection with which the principle was used ought itself to be new.

As the means of inducing the ether to the lungs used by Morton was old, the invalidity of the patent would follow.

This view of the law was accepted by the Supreme Court in the case of *LeRoy* v. *Tatham,* 14 How. 155. The patentees had discovered that lead would re-unite after separation, if under heat and great pressure even though not in a wholly fluid state. By this discovery they were enabled to make lead pipe much more economically and of better quality than had been possible. The apparatus they used, however, was apparently similar, except in size, to that which was used in other industries. The trial court, in an action at law, charged the jury that the invention "did not consist in the novelty of the machinery, but in bringing a newly discovered principle into practical application, by which a useful article of manufacture is produced." The patentees had not claimed as their invention any of the parts of the machinery, but only the combination thereof when used for the purpose of forming pipes of metal, under heat and pressure, in the manner set forth. The Supreme Court reversed the case for error in the trial court's instruction, on the ground that the machinery being old, the alleged invention was only, "at most, an old invention, or apparatus or machinery applied to a new purpose," and that, "if it is old and well known, and applied only to a new purpose, that does not make it patentable." The court does not seem to have considered that the invention could possibly have been what the patentee appeared to have claimed, namely, the *combination* of old substantial means and a new force of nature, to constitute, as a whole, a new idea of means.

This same case came before the court again, in equity, and the opinion was again delivered by Mr. Justice McLEAN. The court sustained the validity of the patent. It is impossible to ascertain from the opinion on just what grounds. It is said, "One new and operative agency in the production of the desired result would give novelty to the entire combination." This new agency might have been the newly discovered principle, but there is an intimation contextually that there was some new, but unnamed, substantial part in the particular combination used. (While this is the implication of the immediate context, the court had earlier said, "the machinery used was admitted to be old.")

The facts of the *Minerals Separation Co.* case were very closely analogous to those of *LeRoy* v. *Tatham.* The patent was for a process of separating mineral matter from the rock in which it had been born, after the latter had been crushed. Prior to the patent, this had been accomplished by the use of oil and water. The affinity of oil for mineral being greater than for the rocky matter, it caused an agglomeration of the former. Upon agitation of the whole mass in water, the buoyancy of the oil, if enough had been used, caused it to rise to the surface, bearing the mineral matter with it. It could then be floated off from the other matter. If less oil were used, its agglomeration of mineral matter caused it to stay at the bottom while agitation of the water bore upward and away the lighter particles of rock. Either of these methods required the use of a costly amount of oil. While the patentees were experimenting for a method of reducing the amount of oil necessary, they discovered that after a certain reduction the agglomera-

tion and separation of the mineral matter ceased, but that after a still further reduction, it apparently began again. This renewed separation was not due to the agglomerating and lifting force of the oil, but to the fact that the minute quantity of oil in the water caused bubbles of air, introduced by the agitation of the mass, to remain for a time undissipated from the surface. These bubbles attached themselves to the particles of mineral and caused such particles to float clear of the rocky material. A patent was granted for this process.

The process of the patentees was old in all respects except that of the principle involved. As the Circuit Court of Appeals said (214 Fed. 100, 109), "each step in their process is fully described in more than one of the patents of the prior art, with the single exception of the reduced quantity of oil which they use." That court, therefore, held the patent to be invalid. The Supreme Court reversed this decision, on the sole expressed ground that the "advance on the prior art and the resulting froth concentrate, so different from the product of other processes, make of it a patentable discovery as new and original as it has proved useful and economical." The invention must have lain in the reduction of the amount of oil, but this change, in itself, was too slight to have constituted a new process. The process was new because, by the reduction in amount of oil, it utilized a new principle, or principles, of nature. So many other cases have distinguished between apparently similar processes or machines because of a difference in their "principles of operation" that it is unnecessary to cite particular authority, but the case just discussed reveals the effect of the principle used with especial clearness. It is undoubtedly true that a principle of nature or a natural force can not by itself be monopolized by patenting, but it seems equally true that, like substantial wheels and levers, and other individually unpatentable things, a principle of nature, as the only new part of a novel combination, is often patented to the extent of its use in such combination or its equivalents.

J. B. W.

"OBTAINING PROPERTY BY FALSE PRETENSES" IN BANKRUPTCY.—When is "property"obtained by false pretenses or representations within the meaning of §17 of the BANKRUPTCY ACT? In the recent case of *In the Matter of Dunfee,* 114 N. E. 52, B had defaulted on a bond upon which, through B's false representations, A had become surety and by means of which bond B had obtained money from C; A was compelled to pay and recovered judgment against B, who then became a bankrupt and procured a discharge. On the ground that the guaranty on the bond was "property" within the meaning of § 17, which provides that liabilities for obtaining property by false pretenses or representations are not released by a discharge in bankruptcy, the New York Court of Appeals held that B remained liable.

The same conclusion was reached in *Gaddy* v. *Witt* (Tex. Civ. App. 1911), 142 S. W. 926, where the surety paid no money but merely executed a note to the original obligee, on the default of the principal; but the opposite was held in *In re Tanner,* 192 Fed. 572, 27 Am. Bank. R. 615. The former case throws no light on the question, since the court cited no authority and gave no reasons, but contented itself with the statement that "the statute * * *

should be liberally construed so as to prevent the discharge in bankruptcy from relieving against a liability which would not exist but for the fraudulent conduct of the defendant," thus assuming the answer to its problem. The latter decision, relied upon in the instant case in the lower court (*In re Dunfee*, 159 N. Y. Supp. 703, 94 Misc. Rep. 628), was decided under § 14b as it read before the amendment of 1910, providing that a discharge shall be given the bankrupt unless he has "obtained *property* on credit * * * upon a materially false statement in writing * * * ." By § 17, a discharge releases a bankrupt from all his provable debts except such as are "liabilities for obtaining *property* by false pretenses or false representations." The court places its decision on the ground that "by the insertion of the words 'money or' before the word 'property' in the amendment of 1910, Congress manifestly *doubted* whether the term 'property' as used in the amendment of 1903 was comprehensive enough to include money; and if it did not include money *most assuredly it did not include a contract or obligation such as this*." (192 Fed. at p. 574.)

In order to simplify the discussion it is assumed for the present that if the term "property" includes money the conclusion of the court as italicized, follows. If this argument—disregarding the italicized conclusion—is sound, then the decision in the principal case is clearly wrong, for in omitting to amend § 17, which is analogous to §14b, Congress would have intended that money should not be included in the term "property" within the meaning of § 17. But it had been decided in *In re Pfaffinger*, 154 Fed. 328 (C. C. A.), 19 Am. B. R. 309, and in *In re Gilpin*, 160 Fed. 171, 20 Am. B. R. 374, that "property" in § 14b included money. Justice LURTON (then Circuit Judge) said, in *Firestone* v. *Harvey*, 174 Fed. 574, 98 C. C. A. 420, that this ground for denying a discharge was evidently leveled particularly at the practice of making false statements of one's financial condition by a buyer or borrower for the purpose of obtaining from the person to whom such false statement is made * * * the articles or money desired." The court in the *Pfaffinger* case says, "One of the common crimes is obtaining property under false pretenses. It has never been restricted to the obtaining of property other than money, but to the obtaining of property including money. Money is property in its most available and efficient form." It would seem then, that Congress had little room to doubt that money was in § 14b included within the term "property," but even if (for the sake of argument) it is admitted that such a doubt existed as would warrant removal by amendment, it would indeed be an unusual method of reasoning by which one would reach the conclusion that thereby Congress, when it *enacted* this provision of the Bankruptcy Act (§ 14b), did not intend money to be included within the term "property."

It appears thus far that the arguments of the courts in the *Gaddy* and *Tanner* cases are not supportable. Are the decisions correct independent of such argument? If "property" in § 14b did not include money before the amendment of 1910, then it did not under § 17 and *In re Tanner* would be correct; but the decisions in the *Pfaffinger* and *Gilpin* cases negative this premise, and hence the conclusion in the *Tanner* case. If, before the amend-

ment, "property" in § 14b included money—and hence the added words "or money" are surplusage—then there are two possible effects of the amendment on the meaning of the word "property" in § 17; either Congress intended merely to dispel any uncertainty as to the interpretation to be placed on § 14 b, leaving the word "property" in § 17 unaffected, or it intended to make § 14b more certain and in addition to cut down the meaning of the word in § 17 so as to exclude money. Had the latter been its intention, it would more likely have made clear that intention by dealing directly with the term in § 17, rather than by leaving its meaning to be speculated upon, especially since Congress was at the time dealing with that very section of the act. It would seem then that the holding in the principal case that money is included in the term "property" is correct and the argument in the *Tanner* case incorrect. It is significant that in only one case other than the *Tanner* case (*Hallagan* v. *Dowell,* (Iowa 1913) 139 N. W. 883), has it ever been urged that "property" in § 17 did not include money, but the decision therein that money is "property" sheds no light on this discussion, because the court gives no argument and cites no authority other than Webster's dictionary.

Thus far we have considered only the nature of that which is ultimately obtained—money, goods, etc.—without reference to the question of remoteness—that is, as to how obtained, whether directly after the false pretenses or representations are made, or whether some intermediate legal obligation arises after the pretenses, but before the "property" is parted with, as in the present surety transaction. The point in the principal case that the money passed from the surety to the original obligee and not to the principal debtor seems in cases like the present to be immaterial and is met by the court with the statement from *Garr* v. *Martin,* 20 N. Y. 306, 309, that "where one person advances money for another in payment of the debt of the latter, it is deemed at the instant of its payment, to be the money of the party for whose benefit the payment is made; so that in the eye of the law the debt is satisfied not by the money of a third party, but by that of the debtor himself." *Musgrove* v. *State,* 133 Ind. 297, 32 N. E. 895, is to the same effect.

In *Gleason* v. *Thaw,* 185 Fed. 345, 25 Am. B. R. 782 (affirmed in 236 U. S. 558), it was held that obtaining a promise to perform legal services (and later the services themselves) by means of false pretenses and representations was not obtaining "property" within the meaning of § 17. The court, referring to the language under consideration, states that these words "refer to substantive things—a *res*—and in no case to which our attention has been called is anything included * * * which approaches in its description or definition, services rendered." The United States Supreme Court in that case says that "property" in § 17 denotes something which may be brought within the control of the court by some recognized process. The court in the principal case therefore holds that the *Thaw* decision is inapplicable, since here it is money which is obtained.

It is seen thus far that "property" within § 17 must be of a tangible nature —a *res*—such as goods or money. It now remains to be considered whether it makes a difference that the property is handed over immediately after the false pretenses or representations are made, or whether more remotely, as in

performance of a contract induced by such representations or pretenses, or as the result of a surety transaction likewise induced.

Criminal liability for the conduct condemned in § 17 dates back to the statute of 30 Geo. II, c. 24 (1757), which provided for the punishment of "all persons who knowingly and designedly, by false pretence or pretences, shall obtain from any person or persons, money, goods, wares or merchandizes * * *." The problem of determining what proximity is necessary between the pretense and obtaining the *res* has come up many times in criminal prosecutions under this and similar statutes. In *Queen* v. *Abbott*, 2 Cox C. C. 431, the defendant who had in a single transaction falsely represented the quality of certain cheese, induced a contract of sale, made delivery and received payment in money, was found guilty. The same conclusion was reached in *Reg.* v. *Martin*, 10 Cox C. C. 383, the defendant having obtained a wagon not in existence at the time the contract of manufacture and sale (induced by false pretenses) was made. It is therein stated that the "test is whether there is a direct connection between the delivery of the chattel and making the false pretenses, or in other words whether the false pretense is a continuing false pretense. In all cases that is a question for the jury." In *Wilkerson* v. *State*, 140 Ala. 155, obtaining goods two months after the mortgage for future advances was induced was not too remote. In *Reg.* v. *Larner*, 14 Cox C. C. 497, the defendant obtained his competitor's ticket for the race, obtained an undeserved handicap and won the prize; the pretense was held too remote: but in *Queen* v. *Button* [1900], 2 Q. B. 597, under identical facts, the contrary was held, and *Reg.* v. *Larner* disapproved. *Reg.* v. *Bryan*, 2 Fost. & F. 567, held the defendant not guilty who had obtained board by false pretenses and later borrowed money without making further pretenses. In *Reg.* v. *Gardner*, 2 D. & B. 41, 7 Cox C. C. 136, the same result was reached, the defendant having obtained lodging by false pretenses and later money without further pretenses. In *Commonwealth* v. *Harkens*, 128 Mass. 85, the court by a decision of four to three, held that obtaining money on a judgment upon which default had been induced by false pretenses was too remote, the three dissenting judges supporting the rule laid down in *Reg.* v. *Martin*, supra.

Were the rule laid down in *Reg.* v. *Martin* applied to these cases they would all be affirmed except *Reg.* v. *Larner*, (overruled by *Queen* v. *Button*), and *Commonwealth* v. *Harkins*, dissented from by three of the seven judges. The principal case would be affirmed and the *Tanner* case reversed. More definitely expressed, "property" is obtained by false pretenses within the meaning of § 17 when such pretenses are made with the intent that they should, or when the party making them might reasonably expect that they would, immediately or at some future time (proximately) result in the passing of a *res*, from the party to whom the pretenses are made to the party making them, or, as in the principal case, to a third party. No reason appears why, on the question of proximity, the rule in criminal cases as to obtaining property by false pretenses is not applicable to § 17 of the BANKRUPTCY ACT.

Is "property" obtained within the meaning of § 17 when through false

pretenses the surety assumes a contingent obligation or when, on the default of the principal debtor, the obligation becomes absolute, or only when the surety actually parts with the *res* (money)? In most cases, as in the principal one, the *res* actually passes before the discharge of the bankrupt and there is no doubt that "property" is obtained, but where all that is obtained is a promise to pay money if the principal debtor fails to pay, and at the time of the discharge in bankruptcy of the latter the surety has not parted with a *res,* but his obligation to do so has become absolute, it can at least be said, applying the rules laid down in the previous paragraph as to obtaining "property" by false pretenses and substituting the phrase "obligation to part with property" for the words "property" and *res,* that the obligation is obtained by false pretenses. Under the early statutes such phrases as "goods, wares, and merchandise" and "money or property" were not broad enough to include promissory notes and the like, and would not include this obligation. The operation of modern statutes has been extended by adding such words as "money, goods, chattels, things in action, and evidences of debt." *People* v. *Reed,* 70 Cal. 533; *State of Iowa* v. *Patty,* 97 Ia. 373. There is not such a difference in the nature, purpose, and language of the BANKRUPTCY ACT and of the section under discussion as to warrant a distinction, hence an additional requirement must therefore be added to the definition laid down in the previous paragraph, namely, that the *res* must actually be parted with by the person to whom the false pretenses are made. If the absolute obligation to pay is not "property," neither is the contingent or inchoate obligation.

It will be interesting to note the result if this precise problem is ever brought before a court, if it should be held that the *res* must actually pass and if the decision in *Williams, et al* v. *United States Fidelity and Guaranty Company,* 236 U. S. 549, 35 Sup. Ct. 289, in which no question of false pretenses is involved, is followed. In that case the principal had defaulted and had received a discharge in bankruptcy from his obligation to the principal, but the surety had not at that time paid the principal creditor. It was nevertheless held that the principal debtor's inchoate obligation to indemnify his surety was also discharged. But if the surety's inchoate obligation or even his absolute obligation, obtained by false pretenses, is not "property" within the meaning of § 17, and if the *Williams* case is followed, the surety, after the principal's discharge, will have no redress against him and will still be liable to the principal creditor. For a full discussion of *Williams et al.* v. *United States Fidelity and Guaranty Company* see 13 MICH. L. REV. 500.

S. D. F.

SET-OFFS AND PREFERENCES.—§ 68a of the BANKRUPTCY ACT provides that "in all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid." The courts are experiencing considerable difficulty in determining whether this provision makes it possible for a bank to retain as against the trustee in bankruptcy the amount of a depositor's check received by the bank within four months of the depositor's insolvency, and with reasonable cause to be-

lieve that he was insolvent, in satisfaction to that amount of a matured obligation due the bank from the depositor. Obviously, one of the incidental questions involved in the determination of this problem is whether the receipt of a check prevents the transaction from being denominated a "set-off." In a case decided in 1872 under the BANKRUPTCY ACT of 1867 (the provisions of which in reference to set-offs and preferences are identical with the existing act so far as the present discussion is concerned) the Supreme Court of the United States answered this question in the affirmative. *Traders' National Bank* v. *Campbell*, 14 Wall. (81 U. S.) 87. The court was of the opinion that the receipt of the check shows that the bank treats the deposit as the property of the depositor and is not relying upon its right of set-off. It was therefore held that the giving of the check constituted a payment which the assignee in bankruptcy was allowed to recover as a voidable preference; and the court intimates that if the bank had simply charged the depositor's account, the transaction would have amounted to a set-off. But this holding does not seem to have found favor with the inferior courts at that time. Two years later, a federal district court held that the receipt by the bank of the depositor's check constituted a set-off. On appeal to the circuit court, the state of the record was such that the question was not then open to review, but the circuit court ventured the dictum that the giving of the check did not prevent the transaction from being a set-off "unless the opinion of the Supreme Court in the case of *Traders' National Bank* v. *Campbell* decides differently * * * Whether the case cited holds otherwise it is not necessary nor indeed proper to inquire." *Blair* v. *Allen*, Fed. Cas. No. 1,483. In 1879, another circuit court reached a decision opposed to the views expressed by the Supreme Court. *Robinson* v. *Wisconsin M. & F. Ins. Co. Bank*, Fed. Cas. No. 11,969. In the course of its opinion the court says: "Upon the argument, the form of the transaction was dwelt upon, namely that a check was drawn and given for the amount of the note, and that the parties spoke of it in the course of their interview, as a payment. But we are not to sacrifice substance to form, but rather to go beyond the mere form and see what the substance and effect of the transaction was. And doing so, we find that it was in fact an adjustment of mutual debts." In reference to the *Traders' Bank* case, the following statement is made: "Taking the whole case together there was evidently a flagrant attempt on the part of the bank to obtain fraudulent preferences, and the several transactions between it and the bankrupts, which gave rise to the subsequent controversy, were so intermingled that the court seems to have found it necessary to condemn the whole as amounting to a fraudulent and unlawful proceeding." Since the *Traders' Bank* case appears to be the only express adjudication by the United States Supreme Court on the question involved it may not be amiss to notice those of its facts which are peculiar. The debtors of the bank in that case gave to the bank their demand note for the whole amount of their debt, with a power to confess judgment. On the next day the bank credited the note to the extent of the debtor's deposit and entered a judgment for the balance. The note was so credited because of the receipt of the debtor's check for the amount of the

deposit. After judgment, execution issued and a stock of goods belonging to the debtors was levied upon. In less than one month a petition in bankruptcy was filed against the debtors and they were adjudicated bankrupt. Later the debtor's stock of goods was sold under the execution of the bank and also a certain sum which the bank had received before bankruptcy by way of collections of drafts for the debtors. The amount received from the sale of the stock of goods was obviously a preference. But it is submitted that the court, had it been so disposed, could very easily have allowed a recovery either for this amount or for this amount plus the amount of the collections without having found it necessary to "condemn the whole." And if we are to determine the reason for the court's allowing the assignee to recover he amount of the check, it is therefore only fair to the court and in accord with the dictates of common sense, that we accept the reason the court has stated. It may be noted in passing that the amount of the collections was allowed to be recovered because, according to the court's statement, the bank in causing the sheriff to levy upon the fund collected, treated it as the property of the debtors and did not rely upon its "own right of set-off." Both of the two last-mentioned amounts were therefore recovered because of the same general reason

The *Traders' Bank* case stands practically alone among the cases decided under the BANKRUPTCY ACT of 1867. Before the decision of the *Traders' Bank* case, it was held in 1869 in *Hough* v. *First National Bank*, Fed. Cas. 6,721, that the giving of the check is in substance an adjustment of mutual debts and not a payment. In 1871, in *In re Warner et al.*, Fed. Cas. 17,177, it was thought that the giving of the check could constitute such fraudulent preference as to prevent the discharge of the bankrupt. But whatever importance might be accorded this holding, is seriously impaired by the fact that the court, in the course of its opinion, seems to be utterly oblivious of the set-off provision of the statute, and also seems to deny the general right to set-off mutual accounts independent of the BANKRUPTCY ACT.

The first intimation since the enactment of the present bankruptcy law as to whether the rule of the *Traders' Bank* case is to be followed, occurred in the course of the opinion of the United States Supreme Court in *New York County National Bank* v. *Massey*, 192 U. S. 138, 146. The court, in upholding the generally-accepted proposition that a set-off should be allowed between a bank and a bankrupt depositor, refers to the *Traders' Bank* case as not being an authority to the contrary because "the right of set-off was not relied upon, but a deposit was seized upon a judgment which was a preference." The court here, of course, fails to notice that a check drawn upon the deposit was given to the bank and that the execution was levied upon the amount the bank had received from collecting the bankrupt's drafts. But nevertheless the intimation is strong that the court in 1903 believed that the levying of an execution upon a deposit cannot constitute a set-off, although the transaction results in nothing more than the settlement of mutual debts; because the bank in so doing is treating the deposit as the property of the depositor. But as already noted in the *Traders' Bank* case, this reasoning applies equally as well to the transaction in which the bank receives a check

from the depositor drawn upon the deposit. This meager reference to its former decision therefore raised a strong presumption that the Supreme Court would still adhere to the doctrine of the *Traders' Bank* case.

But since *Studley* v. *Boylston National Bank,* 229 U. S. 523, the presumption lies very much in the opposite direction. In this case, the bank received the depositor's check without reasonable cause to believe that the depositor was insolvent. Therefore, even if the giving of the check constituted a preference, it did not here constitute a voidable preference. The court was not called upon to decide any question of set-off; and the following statement of the court, so far as the checks were concerned, might have disposed of the whole case: "But if * * * the bank had no reasonable cause to believe such transfers would effect a preference the payments by checks for $15,000 are as much protected as if on the same dates similar checks had been given in payment of like amounts due another bank with which the Collver Co. [the bankrupt] kept no account." The court, however, undertakes also to consider the case from the viewpoint of the question of set-off, and comes to the conclusion that whether a bank charges the depositor's account or whether the depositor gives the bank a check is immaterial; for in either event the transaction amounts to no more than a book entry "equivalent to the voluntary exercise by the parties of the right of set-off." *Dicta* to the same effect occur in the following cases based on similar facts: *Putnam* v. *U. S. Trust Co.,* 223 Mass. 199, 111 N. E. 969; *Walsh* v. *First National Bank,* 201 Fed. 522, 120 C. C. A. 30. Such a transaction was recognized as a set-off, by way of *obiter* also in *Chisholm* v. *First National Bank,* 269 Ill. 110 (see 14 MICH. L. REV. 147, 149), and by way of express adjudication in *Toof* v. *City National Bank,* 206 Fed. 250, 124 C. C. A. 118, and in *American Bank & Trust Co.* v. *Coppard,* 227 Fed. 597, 142 C. C. A. 229. Holdings to the contrary, however, may be found in *In re Scheizer,* 130 Fed. 631; *Ridge Ave. Bank* v. *Studheim,* 145 Fed. 798, 76 C. C. A. 362; *In re Starkweather & Albert,* 206 Fed. 797; *In re National Lumber Co.,* 212 Fed. 928, 129 C. C. A. 448; *Knoll* v. *Commercial Trust Co.,* 229 Pa. St. 197.

Those courts which refuse to treat the transaction in question as a set-off are probably influenced by a desire to construe § 68a strictly, since this section is inconsistent with one of the two main general purposes of the BANKRUPTCY ACT, viz.: the according of equal treatment to creditors. But after all, the distinction which these courts make is, as the early *Robinson* case points out, a distinction in form and not in substance. If the bank has the right to charge the depositor's account without his consent the bank should not be made to suffer merely because, by means of a check, it has received the depositor's consent. And general judicial recognition of this distinction would have no other effect than to cause banks always to charge the account without positive action on the part of the depositor, with the result that the general creditors will have been in no way benefited by the distinction.

It would seem that the transaction under consideration might be more vitally attacked by making a distinction between a set-off before bankruptcy

and a set-off after bankruptcy; since § 68a provides only for a set-off after bankruptcy. Yet all the cases cited *supra* which hold that the transaction amounts to a set-off also hold that it matters not that the set-off occurred within the four months before bankruptcy (except *Toof* v. *City National Bank,* in which case the check was given after the petition was filed). The *Studley* case also contains *dicta* to this effect. This view is further supported by an apparently unanimous line of authorities which allow a bank to charge the bona fide depositor's account within the four months' period when no check is given, although the bank had reasonable cause to believe the depositor was insolvent. Among the modern cases so holding may be cited: *Continental & Commercial Trust & Savings Co.* v. *Chicago Title & Trust Co.,* 229 U. S. 435; *Lowell* v. *International Trust Co.,* 158 Fed. 781, 86 C. C. A. 137; *Germania Savings Bank & Trust Co.* v. *Loeb,* 188 Fed. 285, 110 C. C. A. 263; *West* v. *Bank of Lakhoma,* 16 Okla. 328; *Habeggar* v. *First National Bank,* 94 Minn. 445; *Chisholm* v. *First National Bank,* supra; *Booth* v. *Prete,* 81 Conn. 636.

But to sustain the proposition that no set-off within the four-month period is protected by § 68, certain intimations will be found in the cases of *Ridge Ave. Bank* v. *Studheim* and in *In re National Lumber Co.* which have already been cited to the proposition that a transaction in which a check is given is not a set-off. And in the cases of *Putnam* v. *United States Trust Co.* and *Walsh* v. *First National Bank,* referred to above as containing *dicta* in favor of the proposition that the giving of a check does not prevent the transaction from being a set-off, will be found statements to the effect that if the check is received within the four months, it is to be treated as a preference and its amount recovered if the bank has reasonable cause to believe that the depositor was insolvent. The *Putnam* case in fact actually allowed upon this theory the recovery of the amount of certain checks. This decision is of particular importance in showing that the dictum of the United States Supreme Court in the *Studley* case and the court's actual holding—without consideration of the question—in the case of *Continental & Commercial Trust & Savings Co.* v. *Chicago Title & Trust Co.* have not settled the controversy.

The *Studley* case in its dictum expresses the reason for allowing a set-off in the four-month period, as follows: "There is nothing in § 68a which prevents the parties from voluntarily doing before the petition is filed what the law itself requires to be done after proceedings in bankruptcy are instituted." In *Booth* v. *Prete,* supra, the court states: "The fact that the set-off in the present case was made by the bank prior to the filing of the bankruptcy petition does not affect the question because it did only what the law would have done had the bank waited until the petition was filed." Thus the same reason is generally alluded to. But it is respectfully submitted that the effect of the set-off before bankruptcy does not necessarily produce the same effect as would a set-off after bankruptcy. If no set-off occurs before bankruptcy, the depositor might, so far as § 68a is concerned, draw on the deposit which would otherwise be set off; and the result of his so doing, would be that after bankruptcy, the bank would receive less and

the general creditors would probably receive more than had a set-off occurred before bankruptcy. It is also worthy of notice in this connection that the decision of the United States Supreme Court that the deposit in the *Massey* case supra was not a preference is based upon the fact that the depositor retained the right to draw out the money at any time before his bankruptcy. Further authority of some value contrary to the *Studley* dictum may be found in those cases which allow the recovery of the amount of the deposit that has been appropriated to the discharge of an unmatured obligation before bankruptcy with reasonable knowledge to believe that the depositor is insolvent, although such a set-off is legal after bankruptcy. *Heyman* v. *Third National Bank,* 216 Fed. 685; *Shale* v. *The Farmers Bank,* 82 Kans. 649; *Irish* v. *Citizens Trust Co.,* 163 Fed. 880. But it must be admitted that the recent *Putnam* case, which holds that a set-off before bankruptcy constitutes a preference, oddly enough upon the authority of the *Studley* dictum, accepts the view that an unmatured obligation is subject to set-off within the four-month period; but nevertheless, as already mentioned, the court in this case treats a set-off before bankruptcy as a payment, and allows recovery in accordance with § 60 if the bank, at the time of the set-off occurred, had reasonable cause to believe that the depositor was insolvent.

Though there is nothing in § 68a which justifies a setting off of mutual debts in the four-month period before bankruptcy, it does not necessarily follow that the many courts which accept this view, arrive at an erroneous result. As the *Studley* case states, there is nothing in this section which prevents such a transaction before bankruptcy. Before the enactment of the BANKRUPTCY ACT, the bank had the right to make a set-off at least whenever the depositor's obligation had matured. Therefore, if this right is affected by the ACT, it must be by virtue of some provision other than that contained in § 68a. And where are we to find such provision? § 60, of course, suggests itself immediately with its provision in regard to preferences. But one essential element for the recovery of preference according to § 60 is that the "bankrupt shall have made a transfer." A similar element is essential for recovery under § 67e. Although the courts wisely incline to construe these sections liberally, it would seem very difficult to bring within their terms a transaction in which the bank charges the account of a bankrupt depositor who remains passive or even objects. And perhaps, as before suggested in another connection, the fact that the depositor has consented should make no difference. At first thought, it does not seem plausible that the framers of the BANKRUPTCY ACT meant to allow creditor banks greater privileges than have other creditors within the four months preceding the debtor's bankruptcy. But it is plain that the framers meant to allow them greater privileges after bankruptcy. This is indicative of a general policy. And furthermore, the statements made in the *Studley* and other cases to the effect that to deny the right of set-off within the four-month period would "so interfere with the course of business as to produce evils of serious and far-reaching consequence," are worthy of consideration as tending to show that the failure of Congress to provide language that would declare such a set-off invalid, was not inadvertent. M. W.