Bank of Louisville v. Laughbridge

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Decision Date: 14 January 1892

Citation: Bank of Louisville v. Laughbridge, 92 Ky. 472, 18 S.W. 1 (Ky. Ct. App. 1892)

Parties: Bank of Louisville v. Laughbridge et al.

Court: Kentucky Court of Appeals

18 S.W. 1

92 Ky. 472

Bank of Louisville v. Laughbridge et al.

Court of Appeals of Kentucky.

January 14, 1892

Appeal from Louisville chancery court.

"To be officially reported."

Action by Charles Laughbridge and others against the **Bank** of Louisville to prevent a preference by a debtor of both parties. Judgment for plaintiffs. Defendant appeals. Affirmed.

Pryor, J.

S. **Caye**, Jr., & Co. borrowed divers sums of money from the **Bank** of Louisville, for which notes were executed, and to secure their payment various collaterals were pledged. **Caye** & Co. becoming insolvent, and the **bank** being desirous of making its debt more secure, obtained the pledge of other collaterals, when a creditor of the firm, Charles Laughbridge, instituted this action under the statute enacted to prevent preferences by debtors contemplating insolvency, and obtained a judgment determining that the pledge of the additional securities brought the case within the provisions of the statute. In distributing the assets the court further held that the general creditors must receive a dividend equal to the amount realized by the **bank** from its collaterals before the latter could share in the general distribution; in other words, the court adjudged the assets of an involuntary assignor must be distributed in the same manner as the assets of an insolvent decedent. It is contended by counsel for the **bank** that the same equitable rule of distribution should apply in the case of an assignment by operation of law as in the case of an assignment by the debtor himself, and the right of the lien creditor to share in the general distribution for his whole debt, where the assets are not sufficient to pay all the creditors, is not to be diminished by reason of any lien he may have obtained by contract on the debtor's estate; that when the lien fails to pay his debt the amount realized from it is not to be credited on the debt, and the *pro rata* given him on the balance, but it must be made on the entire amount due him. In cases of voluntary assignments, where a creditor has acquired a preference by lien, this rule of distribution has long since been adopted by this court. In Logan v. Anderson, reported in 18 B. Mon. 92, the rule was established, and it has been followed in several reported cases. ***Bank*** *v. Jefferson,* 10 Bush, 326; ***Bank*** *v. Patterson,* 78 Ky. 291; *Spratt's Ex'x v.* ***Bank***, 84 Ky. 85. It is said in Logan v. Anderson, if a creditor has a mortgage on property of the debtor sufficient to pay 50 cents on the dollar, and then makes a subsequent mortgage to the same creditor, including other

creditors, on other property sufficient to pay 50 cents on the dollar, the first mortgage creditor has the right to have his whole debt paid, while the second mortgage creditors get but 50 cents on the dollar, and for the reason that each mortgage is given to secure the whole debt of the first mortgagee; and the fact that the property last mortgaged fails to pay the last mortgagees is no reason for lessening the security of the first mortgagee, as he had the legal and equitable right to obtain both mortgages to secure his debt. So, if a creditor holds a mortgage on part of the debtor's estate, and the debtor then assigns his whole estate for the payment of all his debts, the debt of the mortgage creditor is embraced by the assignment,-not a part of it, but the whole,-and in the same manner and to the same extent as the debts of the creditors who have no liens. There are two funds, each of which is liable for the whole debt of the mortgage creditor, and where both are necessary for the payment of the debt equity refuses to interfere or marshal securities to the prejudice of the creditor entitled to the double fund. Should this doctrine apply to assignments made by operation of *2 law under a statute S.W. 2 enacted to prevent fraudulent preferences? is the question involved here. It is true, the law takes the estate from the debtor for creditors, but has the debtor given to the creditor this double fund as a security for his debt, and, if not, will a court of equity favor the creditor who is attempted to be preferred, so as at last to give him the preference over general creditors? His lien he has the right to enforce; but will the law step in and give him a double security, when at the same time it is attempting to prevent fraudulent preferences? It is argued that the equitable rule would be to credit the claim of the **bank** by the amount realized from the lien, and then give to the **bank** its *pro rata* share of the assets on the balance of its debt. This rule, if adopted, would present three modes of distributing the assets of an insolvent estate: (1) If a voluntary assignment, both funds would be liable if necessary to pay the whole debt; (2) if involuntary, the creditor would get a *pro rata* on the balance due him after satisfying his lien; (3) if the estate is insolvent, and the debtor dead, the creditor who has the lien must stand off until the general creditors are made equal with him. It seems to us that one of two modes of distribution must be followed in this case,-the assets must be distributed in the same manner as that of a decedent who dies insolvent, or as in the case of a voluntary assignment.

The thirty-fourth section of article 2, c. 39, Gen. St., provides the manner in which the estate of a debtor who dies insolvent shall be distributed, and is as follows: "But when any creditor has a lien, and the property subject to the lien is not sufficient to discharge the debt, he shall not be entitled to any portion of the residue of the estate until all the

creditors not having liens shall have received a sum equal *pro rata* with such lien creditor." The distribution as between creditors where the debtor dies insolvent is made plain by this statute, and the question arises: Did the legislature, in enacting the law to prevent fraudulent preferences, recognize or classify the estates of those passing by operation of law to creditors with the estates of insolvent decedents, as to the mode of distribution? All such estates are subject to the control of courts of equity, and some equitable rule for distribution must be ascertained. It is apparent that the law-making power when enacting the law in regard to sales, etc., in contemplation of insolvency, had in view the act regulating proceedings in the settlement of the estates of debtors who had died insolvent. Section 3 of article 2 of chapter 44 provides, where estates pass to creditors by operation of law, that "the action and proceedings as to the mode of proving claims and otherwise shall be conducted as actions and proceedings for the settlement of the estates of deceased persons are now required to be conducted, so far as the same are applicable," etc.; and by section 7 it is further provided that in the distribution of the assets of any debtor as provided debts due as guardian or administrator or executor shall have priority, as also debts due as trustee, if the trust be created by the deed or will, duly recorded in the proper clerk's office." The statute has designated the claims of those who, under this operation of law passing the estate to creditors, shall have prior liens, following the priority given to claimants against the estates of those dead, showing plainly that the legislature regarded the act of insolvency as placing the estate of the insolvent debtor in the same condition, and to be distributed in the same manner, as the estate of a decedent. While the third section of the act may apply to the mode of proceeding alone, such as filing the petition and proving claims, a careful reading of both sections indicates clearly that the legislature was attempting to regulate the mode of distribution, as well as the mode of proceeding, by the provisions of the statute with reference to the estates of deceased persons. It is the contract relation between the creditor and the debtor that gives to the former the right to resort to both funds to pay his debt when the lien is insufficient for that purpose. The rule springs from no equitable doctrine, but, on the contrary, a court of equity declines to interfere because the debtor by his voluntary assignment has placed every debt on the same footing, and it is to secure the whole debt to the extent the estate will pay, and not a part of it; but when the law seizes the estate for the purpose of preventing preferences, although for the benefit of creditors, equity must say, if the statute under which the proceeding is had has not already determined, how the assets shall be distributed. If left to the creditor and debtor under their contract by reason of which the estate has passed to creditors, the creditor would get all. But here is no contract, and we

find an equitable rule established by statute, by which the secured creditor is held off until the general creditors are made equal, and, when this is done, all share equally in the remaining assets. This rule is applied to a decedent's estate who is insolvent, and who has created a lien in favor of one creditor; and there is no reason why it should not apply to a case where the law has taken the debtor's estate from him, and holds it for equitable distribution between creditors. It is true that the creditor is not rewarded for his vigilance in obtaining a lien, but to prevent this where the debtor contemplated insolvency was the object of the statute, and in distributing the assets when by operation of law the creditors became entitled to the estate the law in regard to the distribution of the assets of a decedent's estate who dies insolvent should apply. The judgment below, conforming to these views, is affirmed.