

G.R. No. 20993. December 22, 1923

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the charges paid for storage and insurance, subject to the further orders of this court or of the Supreme Court in the premises." From this decision the Asia Banking Corporation appeals, specifying the following errors: "I. The trial court erred in failing to find and declare that the claimant bank held a valid title to the money and merchandise described in its supplemental claim and was entitled to preference with reference thereto over the assignee and all other creditors. "II. The trial court erred in finding that 'Umberto de Poli was at least suspected by the claimant bank of impending insolvency' on the 22d of November, 1920, when it obtained possession of the merchandise in question. "III. The trial court erred in failing to find that the negotiable neutral warehouse receipts issued on November 22, 1920, together with the previous letter pledges or promises to pledge, conveyed to the claimant bank absolute title to the said merchandise and that such title could only be defeated by proof of fraud on the part of the bank. "IV. The trial court erred in holding that the assignee was and is a third person with reference to the claimant bank. "V. The trial court erred in failing to order said assignee to return the money and merchandise surrendered to him by mistake." JOHNS, J.: Relying upon the decisions of this court in *Mitsui Bussan Kaisha vs. Hongkong & Shanghai Banking Corporation* (36 Phil., 27), and *Mahoney vs. Tuason* (39 Phil., 952), the attorneys for the bank vigorously contend that in this kind of a proceeding the assignee does not act for, or represent, general creditors of the insolvent estate, and that he represents the insolvent only; that De Poli could not personally question the legal force and effect of the "letter-warehouse receipts," and for such reason his assignee cannot question them. It must be conceded that the language used and the authorities cited in the *Mitsui Bussan Kaisha* case tend to support counsel's contention. As applied to the facts therein stated, the decision in the *Kaisha* case upon the point in question was more or less obiter dictum, as in legal effect the court held that the transaction there in question was valid even as against general creditors. The question here involved is squarely met and decided in the case of *Security Warehousing Co. vs. Hand* ([1907], 206 U. S., 415; 51 L. ed., 1117, 1122-1124), in which that court says: "There is, however, an important matter which has been raised by the appellants aside from the merits. That is, whether a trustee in bankruptcy can question the validity of these receipts, or the sufficiency of the alleged transfer of the property belonging to the bankrupt knitting company, to constitute a pledge of such property. The right is denied by the appellants, and it is contended that the transfers were valid between the parties; that the trustee in bankruptcy takes only the title and right of the bankrupt, and therefore he cannot assert a right not possessed by the knitting company. "It is no new doctrine that the assignee or trustee in bankruptcy stands in the shoes of the bankrupt, and that the property in his hands, unless otherwise provided in the bankrupt act, is subject to all of the equities impressed upon it in the hands of the bankrupt. This has been the rule under former acts and is now the rule. (*Hewit vs. Verlin Mach. Works*, 194 U. S./296; 48 L. ed., 986; 24 Sup. Ct. Rep., 690; *Thompson vs. Fairbanks*, 196 U. S., 516, 526; 49 L. ed., 577; 25 Sup. Ct. Rep., 306; *Humphrey vs. Tatman*, 198 U. S., 91; 49 L. ed., 956.; 25 Sup. Ct. Rep., 567; *York Mfg. Co. vs. Cassell*, 201 U. S., 344, 352; 50 L. ed., 782, 785; 26 Sup. Ct. Rep., 481.)" In analyzing its decision, that court quoted from its opinion in *Thompson vs. Fairbanks*, supra, where it is said: " 'Under the present bankrupt act, the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the act.' " Also from its opinion in the *York Mfg. Co. vs. Cassell*, supra, in which it is said: "This court had theretofore approved the remark in *Re New York Economical Printing Co.*, 49 C. C. A. 133; 110 Fed., 514, 518, that the present bankrupt act contemplates that a lien good as against the bankrupt and all of his creditors at the time of the filing of the petition in bankruptcy should remain undisturbed. *Hewit Case*, supra. Upon these facts it was reiterated that the trustee takes the property as the bankrupt held it. "The case at bar bears no resemblance in its facts to the cases just cited. There was no valid disposition of the property in the case before us, or any valid lien. The so-called warehouse receipts issued by the warehousing company to the knitting company, upon the facts of this case, gave no lien under the law in Wisconsin in which state they were issued. In such case this court follows the state court." The law is well stated in *Ruling Case Law*, vol. 3, page 231, where it is said: "63. Nature and incidents of trustee's title.—The trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or incumbrance of the property which is void as against the trustee by some positive provision of the Act. This was the rule under former bankruptcy acts and continues to be the rule under the present act.

He does not take the property of the bankrupt as a bona fide purchaser for value. It is only as to unlawful preferences and property fraudulently conveyed that the trustee has rights, in the interest of creditors, beyond those that the bankrupt himself could have enforced." In the notes, it is said: "The rule that the trustee takes the estate of the bankrupt in the same plight as the bankrupt held it is not applicable to liens which, although valid as to the bankrupt, are invalid as to creditors. *Baltimore First Nat. Bank vs. Staake*, 202 U. S., 141; 26 S. Ct., 580; 50 U. S. [L. ed.], 967, affirming 133 Fed., 717; 66 C. C. A., 547; *Fourth St. Nat. Bank vs. Millbourne Mills Co.'s Trustee*, 172 Fed., 177; 96 C. C. A., 629; 30 L. R. A. [N. S.], 552." *Corpus Juris*, vol. 7, page 224, says: "(Sec. 345) D. Representation of creditors by trustee.—The trustee is not the representative of the bankrupt, but of the creditors who are unsecured and who were such creditors at the time of the filing of the petition; and he holds title to the bankrupt's property in trust for the creditors and for the purpose of distribution among them. "A trustee in bankruptcy, as the representative of the creditors, may sue to recover property which has been transferred by the bankrupt with intent to hinder, delay, or defraud his creditors, or to give a preference, or money which has been paid to create a preference. (P. 247.) "(2) Avoidance of fraudulent transfer or preference.—The Bankruptcy Act in its present form expressly confers upon courts of bankruptcy jurisdiction of proceedings by the trustee to recover property transferred by the bankrupt in fraud of his creditors, or money or property paid or transferred with the intent to create a preference, where the payment or transfer occurred within four months prior to the filing of the petition in bankruptcy, regardless of the consent of the defendant; and an action by a trustee on behalf of creditors to avoid a transfer by the bankrupt which, under the state law, such creditors might have avoided, although not made within four months of the filing of the petition in bankruptcy, may now be brought in the court of bankruptcy without the consent of defendant. (P. 257.) "(1) By trustee—(a) To recover preference.—In an action to recover an alleged preference, the burden rests upon the trustee to establish the fact of a payment or transfer by the bankrupt, and that it was preferential and voidable rather than legal. He must therefore show that the payment or transfer took place within four months prior to the filing of the petition in bankruptcy; that the bankrupt was insolvent at the time thereof; that defendant knew of such insolvency and had reasonable cause to believe that a preference was intended, or, since the amendment of 1910, that the transfer would effect a preference; and that the effect of the payment or transfer would be to enable the recipient to obtain a greater portion of his claim than other creditors of the same class." (P. 270.) In legal effect, that was the decision of this court in *Te Pate vs. Ingersoll*, decided May 29, 1922, and reported in vol. 43, *Philippine Reports*, page 394, in which this court said: "When goods or merchandise have been pledged to secure the payment of a debt of a particular creditor, the other creditors of the pledgor are 'third persons' with relation to the pledge contract and the pledgor and pledgee. This is so because the insolvency proceedings operate to vest in the assignee all of the estate of the insolvent debtor not exempt by law from execution. This is true, also, because the assignee is the representative of the creditors and not of the bankrupt. (Civil Code, article 1865, in relation to articles 1863 and 1226; Bankruptcy and Insolvency Law, Act No. 1956, sec. 32; *Tec Bi & Co. vs. Chartered Bank of India, Australia and China* [1916], 41 Phil., 596; 12 *Manresa*, *Comentarios al Código Civil*, pp. 416, et seq.; *Ocejo, Perez & Co. vs. International Banking Corporation* [1918], 37 Phil., 631.)" We hold that in all actions or proceedings to set aside or nullify preferences or fraudulent transactions as void under the provisions of section 70 of Act No. 1956, known as the Insolvency Law, the assignee appears for, and represent, the general creditors, and that, in so far as the decision of this court in the *Kaisha* case is in conflict upon that point, it is hereby overruled. Section 70 of the Act provides: "If any debtor, being insolvent, or in contemplation of insolvency, within thirty days before the filing of a petition by or against him, with a view to giving a preference to any creditor or person having a claim against him or who is under any liability for him, procures any part of his property to be attached, sequestered, or seized on execution, or makes any payment, pledge, mortgage, assignment, transfer, sale, or conveyance of any part of his property, either directly or indirectly, absolutely or conditionally, to anyone, the person receiving such payment, pledge, mortgage, assignment, transfer, sale, or conveyance, or to be benefited thereby, or by such attachment or seizure, having reasonable cause to believe that such debtor is insolvent, and that such attachment, sequestration, seizure, payment, pledge, mortgage, conveyance, transfer, sale, or assignment is made with a view to prevent his property from coming to his assignee in insolvency, or to prevent the same from being distributed ratably among his creditors, or to defeat the object of, or in any way hinder, impede, or delay the operation of or to evade any of the provisions of this Act, such attachment, sequestration, seizure, payment, pledge, mortgage, transfer, sale, assignment, or conveyance is

void, and the assignee, or the receiver, may recover the property, or the value thereof, as assets of such insolvent debtor. If such payment, pledge, mortgage, conveyance, sale, assignment, or transfer is not made in the usual and ordinary course of business of the debtor, or if such seizure is made under a judgment which the debtor has confessed or offered to allow, that fact shall be prima facie evidence of fraud. Any payment, pledge, mortgage, conveyance, sale, assignment, or transfer of property of whatever character made by the insolvent within one month before the filing of a petition in insolvency by or against him, except for a valuable pecuniary consideration made in good faith, shall be void. All assignments, transfers, conveyances, mortgages, or incumbrances of real estate shall be deemed, under this section, to have been made at the time the instrument conveying or affecting such realty was filed for record in the office of the register of deeds of the province or city where the same is situated." The important question here is whether the transaction in question constitutes a valid lien in favor of the bank, or a preference which is void as to creditors. We do not agree with counsel for the bank that the letters of August 21st and 25th and September 4th are in legal force and effect warehouse receipts. It is very apparent that the bank itself did not treat or consider them in the form or nature of warehouse receipts. They recite: "In addition to security now in your hands covered by Quedanes, as collateral of my daily overdraft I hold in my godown of No. 209 Estero de Binondo: 11,780 Buntal hats valued P41,230.00 6,150 Balibuntal hats valued 46,125.00 _____ 87,355.00 ===== which bring my position to a total of P321,556.94." When the bank took the actual physical possession of the property in question, it was removed to the warehouses of Derham Bros., Inc., by which a warehouse receipt, with all of its legal formalities and in the usual and ordinary form, was issued to, and in favor of, the bank. Prior to that time the bank never had the actual control or physical possession of the property described in the August and September letters. Although when written the letters may have had some legal value as between the bank and De Poli, yet, standing alone and without possession, they did not create any vested rights in the bank as between it and the creditors of the insolvent estate. The record shows that the bank took the physical possession of the property in question on November 22, 1920, sixteen days prior to the time that De Poli was adjudged insolvent. Hence, the question becomes important as to how, why and in what capacity the bank took possession, and whether it then knew or had reasonable grounds to believe that De Poli was insolvent. Upon the question of knowledge, in its opinion the trial court says: "On November 22, 1920, when the said Umberto de Poli was at least suspected by the claimant bank of impending insolvency, the said bank obtained possession of the 22,920 Philippine hats described in the letters of August 21 and September 4, 1920, and of 42,046 meters of the 102,000 meters of sinamay described in the letter of August 25, 1920, and stored the same with the Derham Warehouse & Shipping Co., for which it received warehouse receipt No. 1701 in its own name." Upon that point, Mr. Brandt, the credit man of the bank, testified: "Q. And that was the first time that you knew that U. de Poli was about to be declared insolvent?—A. I had an intimation of it at the time of the delivery of the merchandise to us. "Q. Why was your attorney along with you ?—A. The depressed physical appearance of Mr. De Poli lead me to think he was in trouble. "Q. Why did you come to go down there and get that property on November 22d? Who told you to do that?—A. Manager Beldon. "Q. Did you ask him why?—A. He stated that he wished to obtain additional security to cover Mr. De Poli's overdraft with us, and that Mr. De Poli had agreed to turn over certain merchandise already pledged to us. "Q. Is it not a fact that these hats and this silk voile were taken from the U. de Poli bodega at night?—A. It started in the afternoon about four or five o'clock and continued until about eight o'clock possibly. "Q. Referring to your statement about the depressed condition of Mr. U. de Poli at the time you took delivery of these hats and this sinamay, how was that depression evidenced?—A. Mr. De Poli was very sad and depressed. "Q. Did he shed tears?—A. In the presence of me and Colonel Wolfson, he cried. "Q. And that lead you to suspect, for the first time as I understand it, that he was in financial difficulties, is that so?—A. Yes, sir." Mr. Schwarzkopf, who was then one of the attorneys for the bank, testified: "A. No, sir, my advice was based upon the fact that there was a rumor in the streets that the Philippine National Bank was about to take over the U. de Poli assets. "Q. Why were they about to do that?—A. I did not know. "Q. And when you gave the bank this advice you told them, did you not, to take possession of this merchandise immediately, working day and night if necessary, and to get all they could out of this bodega?—A. I told them to work quickly, and if necessary to work day and night." The reasons why, the time and manner in which the bank took possession clearly indicate that it knew, or that at least it had reasonable

grounds to believe, that De Poli was then insolvent. Again, it is very apparent from the time and manner of taking possession that it was not done "in the usual and ordinary course of business of the debtor." It clearly indicates that the bank thought and felt that an emergency existed, and that prompt action was required. The fact that the bank then surrendered two of the letters in question to the insolvent is conclusive proof that it then knew of the existence of the letters, and that it then at least thought and understood that the letters were of no legal value to the bank without possession of the property. In other words, it then took possession of it to further protect and secure its claim. Among other things section 70 provides: "Any payment, pledge, mortgage, conveyance, sale, assignment, or transfer of property of whatever character made by the insolvent within one month before the filing of a petition in insolvency by or against him, except for a valuable pecuniary consideration made in good faith, shall be void." On page 35 of its opinion in the Kaisha case, this court says: "There is no dispute about the facts between the Hongkong Bank and the intervener. Both agree that the title to the coal in question was in Chua Teng Chong. As above indicated, Chua Pue Tee, acting for Chua Teng Chong, attempted to pledge the coal to the bank on the 13th of April, 1914, by means of the private document, Exhibit 5. The bank, acting in good faith and without any knowledge of the insolvency of Chua Teng Chong, turned over to the latter's representative, Chua Pue Tee, the P30,000 in cash in consideration for the so-called pledge of April 13. On April 16 the bank, having in the meantime discovered that Chua Teng Chong was insolvent, secured a real pledge and took physical possession of the coal." (36 Phil., 35.) In other words, it is admitted there that, as a part of the transaction and concurrent with the making and delivery of the private document there in question, the Hongkong & Shanghai Bank parted with, and delivered to Chua Teng Chong, "the P30,000 in cash in consideration for the so-called pledge of April 13." That was a present loan as distinguished from a preexisting debt, in and by which the bank then and there parted with its money with the express understanding and agreement that it should have and receive a pledge of the property to secure the P30,000. Therein lies the important legal distinction between it and the instant case. Again, for aught that appears there, it was the only transaction between the parties. Here, De Poli was a customer of the bank with which he had numerous previous dealings and a large overdraft at the time the letters in question were written, and the transaction in question was one of many dealings which he previously had with the bank, and the testimony of Mr. Brandt above quoted is clear and convincing that the bank took possession "to obtain additional security to cover Mr. De Poli's overdraft with us." Assuming that to be true, it would follow that at the time the bank took possession it had other and different security for its claim against De Poli, and that possession was taken to secure a preexisting debt, and that the transaction in question was not a pledge or transfer of property for a valuable pecuniary consideration made in good faith within the meaning of that portion of section 70 above quoted. In his supplemental brief of December 17th, counsel for the bank points out that in one of his former briefs it is said: "That these promises to pledge 'may possibly have been executed to some extent in consideration of a preexisting debt.' " And " 'The bank in the present case was constantly advancing money to the debtor at the time of the execution of the private documents or promises to pledge as is sufficiently shown on the face of those documents and by the proofs offered in this case.' " He then points out that: "The balance of the daily overdraft on August 21, 1920, when the letter promise of that date was delivered to the bank was P321,556.94: On the delivery of the letter of August 25, 1920, P348,925.94, and on the delivery of the letter of September 4, 1920, P419,500.94. Thus it appears that the debtor U. de Poli overdrawed his current account to the extent of P97,944 from August 12, 1920, the date of the first letter, to September 4, 1920, the date of the third and last letter promise to pledge; that is to say, the debtor drew and the bank parted with that amount as a present or subsequent advancement against the security represented by those two letter promises, and whatever other security may have been deposited with the bank during the same period. "Subsequent to the execution and delivery of the letter promise of September 4, 1920, the claimant bank, through the same current account thus secured by the three letter promises, advanced additional sums against all the securities deposited until the total overdraft amounted to over seven hundred thousand pesos * * *. This total overdraft, together with the list of the securities held by the bank, shows conclusively that the latter, after the deposit of such securities, including the three letter promises to pledge, advanced against such securities sums largely in excess of their value." From which it is contended that the bank relied upon the letters for any advances which it made after September 4th. That position is not tenable and is not sustained by the proof. With all due respect to learned counsel for the bank, there is no financial statement of the bank in the record before us which shows the condition of De Poli's account with the bank between those dates. The first entry in Exhibit

GG is December 16, 1921. Exhibit A shows the condition of his account as of December 15, 1921, and neither exhibit shows the condition of his bank account at any time during the year, 1920. It is true that in his letter of August 21st De Poli says: "Which bring my position to a total of P321,556.94." And in the one of August 25th, he says: "Which bring my today's position to a total of P348,925.94." And in the one of September 4th, he says: "Will bring my today's position to a total of P419,500.94." But this court has no legal right to accept De Poli's statements in the letters as to the amount of his overdraft in the bank as of those dates. Accepting his statement of P348,925.94 as of August 25th, and adding to it the P14,645, the value of the merchandise stated in the letter of September 4th, you have a total of P363,570.94, and in the letter of September 4th De Poli says: "Will bring my today's position to a total of P419,500.94" showing an unexplained difference of P55,930. If it be a fact that the letters in question were written under an agreement with the bank that it would loan De Poli a specific amount on the merchandise evidenced by each letter, and that the bank made him the loan under such an agreement and later took possession of the merchandise described in the letters, another and a different question would be presented, and the decision in the Kaisha case would then be in point. But, here, the evidence tends to show that the letters in question were written and possession of the property taken to secure an open current account in the form of an overdraft evidencing a preexisting debt as distinguished from a present loan, and there is a failure of proof to show that the letters were written under an agreement to secure a present loan, or that the bank made a present loan and parted with its money under any such an agreement. Again, it will be noted that the letters in question are not public instruments, and that neither of them is acknowledged or filed of record. Article 1865 of the Civil Code says; "No pledge shall be effective as against a third person unless evidence of its date appears in a public instrument." In the case of *Te Pate vs. Ingersoll*, above quoted, it is further said: "A pledge, to be valid against third persons, must be evidenced by a public instrument. This is a mandatory condition prescribed by article 1865 of the Civil Code, which must be met in order to constitute the contract of pledge. An assignee is a 'third person' within the meaning of this article of the Civil Code." Upon the facts in the record here, the assignee represents the creditors, and is a third person within the meaning of article 1865. From what has been said, it follows that the judgment of the lower court on the merits must be affirmed. The assignee did not appeal. Hence, many of the questions discussed in his brief are not legally before this court. Suffice it to say that, upon the question of value, we agree with the findings and conclusions of the trial court as to the good faith of the bank and the disposition which it made of the property, the accounting which it should make, and the basis for its liability. In their respective briefs and oral arguments, there is more or less criticism of each other by opposing counsel, which is wholly immaterial and of no value to the court. Suffice it to say that no attorney ought to be criticized for the making of an honest legal effort to protect the interest of his client. The judgment of the lower court is affirmed, without costs to either party, and the case is remanded for an accounting and such further proceedings as are not inconsistent with this opinion. So ordered. Malcolm, Avanceña, Villamor, Ostrand, and Romualdez, JJ., concur. CONCURRING STREET, J.

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STATEMENT

As a supplemental statement of its claim against the estate of U. de Poli, an insolvent, the Asia Banking Corporation alleges that, in addition to its security mentioned in its claim presented December 20, 1920, and as amended October 18, 1921, it held, as further security, three warehouse receipts in the form of letters issued to it by the debtor as of August 21, 25, and September 4, 1920, of which the following is a copy of the first:

"MANILA, August 21, 1920.

"Messrs. ASIA BANKING CORPORATION,

"Manila, P. I.

"Dear Sirs: In addition to security now in your hands covered by Quedanes, as collateral of my daily overdraft I hold in my godown of No. 209 Estero de Binondo:

11,780 Buntal hats valued

P41,230.00

6,150 Balibuntal hats valued

46,125.00

87,355.00

=====

which bring my position to a total of

P321,556.94."

The other two letters are of the same tenor describing property of the value of P42,015.

It is then alleged that of the property described in the letters, on November 22, 1920, De Poli delivered possession to the bank of sixty-eight cases of sinamay and 22,920 Philippine hats; that at the time of such delivery, the receipts of August 21st and September 4th were returned to De Poli, who promised to deliver the remainder of the property, which he failed to do; that of the property which was delivered and stored in neutral warehouses 18,518 of the hats were sold for P31,457.53; that the remaining 4,349, for the purposes of sale, were forwarded to New York City; that their probable value is P4,511; that due to a change in the management of the bank, the facts with reference to the said warehouse receipts were lost, and that the present management had no knowledge of such receipts, and for want thereof, and upon the advice of its present counsel, the bank delivered to the assignee the proceeds of the sale of the hats, together with 42,046 meters of sinamay of the value of P12,420.24; that such delivery was made through the error of both parties and in ignorance of the existence of the "letter-warehouse receipts;" that, acting upon information, which it received from the assignee, on November 23, 1921, the bank found the letters in question.

Wherefore, it prays that the assignee be ordered and directed to return to the bank the money and merchandise, which were erroneously delivered to him, and to also deliver the remaining 59,954 meters of sinamay, or the proceeds in the event the property has been sold.

For answer, the assignee makes a general and specific denial of all of the material allegations of the petition, and, as a further and special defense, alleges that the bank has no valid security, or preference whatever, by virtue of the "letter-warehouse receipts," for the reason that they are null and void as against the general creditors of the insolvent estate. First, because they are not valid warehouse receipts under the law, and are not evidenced by any public document, and that the property was never delivered to the bank, and, as a second special defense, alleges that the money and the property were voluntarily surrendered by the bank to the assignee with the full knowledge of all the facts and upon the advice of its present and former counsel, and, as a counterclaim, the assignee alleges that, without any legal right, the bank took and appropriated to its own use the property described in the letters, and that it was then of the value of P142,500; that, giving the bank credit for the money which it refunded to the assignee, there is a balance due and owing from the bank to the assignee of P98,622.23, for which he prays judgment against the bank.

The trial court denied the supplemental claim of the bank, and rendered judgment to the effect that the assignee should "have and recover of and from said Asia Banking Corporation the goods, wares, and merchandise hereinbefore described and mentioned as having been taken into the possession of the Asia Banking Corporation on November 22, 1920, and stored on said date with the Derham Warehouse & Shipping Company, or, in the event of sales thereof, the proceeds of all of said property which has or shall have been sold, less the charges paid for storage and insurance, subject to the further orders of this court or of the Supreme Court in the premises."

From this decision the Asia Banking Corporation appeals, specifying the following errors:

"I. The trial court erred in failing to find and declare that the claimant bank held a valid title to the money and merchandise described in its supplemental claim and was entitled to preference with reference thereto over the assignee and all other creditors.

"II. The trial court erred in finding that 'Umberto de Poli was at least suspected by the claimant bank of impending insolvency' on the 22d of November, 1920, when it obtained possession of the merchandise in question.

"III. The trial court erred in failing to find that the negotiable neutral warehouse receipts issued on November 22, 1920, together with the previous letter pledges or promises to pledge, conveyed to the claimant bank absolute title to the said merchandise and that such title could only be defeated by proof of fraud on the part of the bank.

"IV. The trial court erred in holding that the assignee was and is a third person with reference to the claimant bank.

"V. The trial court erred in failing to order said assignee to return the money and merchandise surrendered to him by mistake."

JOHNS, J.:

Relying upon the decisions of this court in *Mitsui Bussan Kaisha vs. Hongkong & Shanghai Banking Corporation* (36 Phil., 27), and *Mahoney vs. Tuason* (39 Phil., 952), the attorneys for the bank vigorously contend that in this kind of a proceeding the assignee does not act for, or represent, general creditors of the insolvent estate, and that he represents the insolvent only; that De Poli could not personally question the legal force and effect of the "letter-warehouse receipts," and for such reason his assignee cannot question them. It must be conceded that the

language used and the authorities cited in the Mitsui Bussan Kaisha case tend to support counsel's contention. As applied to the facts therein stated, the decision in the Kaisha case upon the point in question was more or less obiter dictum, as in legal effect the court held that the transaction there in question was valid even as against general creditors. The question here involved is squarely met and decided in the case of *Security Warehousing Co. vs. Hand* ([1907], 206 U. S., 415; 51 L. ed., 1117, 1122-1124), in which that court says:

"There is, however, an important matter which has been raised by the appellants aside from the merits. That is, whether a trustee in bankruptcy can question the validity of these receipts, or the sufficiency of the alleged transfer of the property belonging to the bankrupt knitting company, to constitute a pledge of such property. The right is denied by the appellants, and it is contended that the transfers were valid between the parties; that the trustee in bankruptcy takes only the title and right of the bankrupt, and therefore he cannot assert a right not possessed by the knitting company.

"It is no new doctrine that the assignee or trustee in bankruptcy stands in the shoes of the bankrupt, and that the property in his hands, unless otherwise provided in the bankrupt act, is subject to all of the equities impressed upon it in the hands of the bankrupt. This has been the rule under former acts and is now the rule. (*Hewit vs. Verlin Mach. Works*, 194 U. S./296; 48 L. ed., 986; 24 Sup. Ct. Rep., 690; *Thompson vs. Fairbanks*, 196 U. S., 516, 526; 49 L. ed., 577; 25 Sup. Ct. Rep., 306; *Humphrey vs. Tatman*, 198 U. S., 91; 49 L. ed., 956; 25 Sup. Ct. Rep., 567; *York Mfg. Co. vs. Cassell*, 201 U. S., 344, 352; 50 L. ed., 782, 785; 26 Sup. Ct. Rep., 481.)"

In analyzing its decision, that court quoted from its opinion in *Thompson vs. Fairbanks*, *supra*, where it is said:

" 'Under the present bankrupt act, the trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it, and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or encumbrance of the property which is void as against the trustee by some positive provision of the act.' "

Also from its opinion in the *York Mfg. Co. vs. Cassell*, *supra*, in which it is said:

"This court had theretofore approved the remark in *Re New York Economical Printing Co.*, 49 C. C. A. 133; 110 Fed., 514, 518, that the present bankrupt act contemplates that a lien good as against the bankrupt and all of his creditors at the time of the filing of the petition in bankruptcy should remain undisturbed. *Hewit Case*, *supra*. Upon these facts it was reiterated that the trustee takes the property as the bankrupt held it.

"The case at bar bears no resemblance in its facts to the cases just cited. There was no valid disposition of the property in the case before us, or any valid lien. The so-called warehouse receipts issued by the warehousing company to the knitting company, upon the facts of this case, gave no lien under the law in Wisconsin in which state they were issued. In such case this court follows the state court."

The law is well stated in *Ruling Case Law*, vol. 3, page 231, where it is said:

"63. Nature and incidents of trustee's title.—The trustee takes the property of the bankrupt, in cases unaffected by fraud, in the same plight and condition that the bankrupt himself held it and subject to all the equities impressed upon it in the hands of the bankrupt, except in cases where there has been a conveyance or incumbrance of the property which is void as against the trustee by some positive provision of the Act. This was the rule under former bankruptcy acts and continues to be the rule under the present act. He does not take the property of the bankrupt as a bona fide purchaser for value. It is only as to unlawful preferences and property fraudulently conveyed that the trustee has rights, in the interest of creditors, beyond those that the bankrupt himself could have enforced."

In the notes, it is said:

"The rule that the trustee takes the estate of the bankrupt in the same plight as the bankrupt held it is not applicable to liens which, although valid as to the bankrupt, are invalid as to creditors. *Baltimore First Nat.*

Bank vs. Staake, 202 U. S., 141; 26 S. Ct., 580; 50 U. S. [L. ed.], 967, affirming 133 Fed., 717; 66 C. C. A., 547; Fourth St. Nat. Bank vs. Millbourne Mills Co.'s Trustee, 172 Fed., 177; 96 C. C. A., 629; 30 L. R. A. [N. S.], 552."

Corpus Juris, vol. 7, page 224, says:

"(Sec. 345) D. Representation of creditors by trustee.—The trustee is not the representative of the bankrupt, but of the creditors who are unsecured and who were such creditors at the time of the filing of the petition; and he holds title to the bankrupt's property in trust for the creditors and for the purpose of distribution among them.

"A trustee in bankruptcy, as the representative of the creditors, may sue to recover property which has been transferred by the bankrupt with intent to hinder, delay, or defraud his creditors, or to give a preference, or money which has been paid to create a preference. (P. 247.)

"(2) Avoidance of fraudulent transfer or preference.—The Bankruptcy Act in its present form expressly confers upon courts of bankruptcy jurisdiction of proceedings by the trustee to recover property transferred by the bankrupt in fraud of his creditors, or money or property paid or transferred with the intent to create a preference, where the payment or transfer occurred within four months prior to the filing of the petition in bankruptcy, regardless of the consent of the defendant; and an action by a trustee on behalf of creditors to avoid a transfer by the bankrupt which, under the state law, such creditors might have avoided, although not made within four months of the filing of the petition in bankruptcy, may now be brought in the court of bankruptcy without the consent of defendant. (P. 257.)

"(1) By trustee—(a) To recover preference.—In an action to recover an alleged preference, the burden rests upon the trustee to establish the fact of a payment or transfer by the bankrupt, and that it was preferential and voidable rather than legal. He must therefore show that the payment or transfer took place within four months prior to the filing of the petition in bankruptcy; that the bankrupt was insolvent at the time thereof; that defendant knew of such insolvency and had reasonable cause to believe that a preference was intended, or, since the amendment of 1910, that the transfer would effect a preference; and that the effect of the payment or transfer would be to enable the recipient to obtain a greater portion of his claim than other creditors of the same class." (P. 270.)

In legal effect, that was the decision of this court in *Te Pate vs. Ingersoll*, decided May 29, 1922, and reported in vol. 43, *Philippine Reports*, page 394, in which this court said:

"When goods or merchandise have been pledged to secure the payment of a debt of a particular creditor, the other creditors of the pledgor are 'third persons' with relation to the pledge contract and the pledgor and pledgee. This is so because the insolvency proceedings operate to vest in the assignee all of the estate of the insolvent debtor not exempt by law from execution. This is true, also, because the assignee is the representative of the creditors and not of the bankrupt. (Civil Code, article 1865, in relation to articles 1863 and 1226; Bankruptcy and Insolvency Law, Act No. 1956, sec. 32; *Tec Bi & Co. vs. Chartered Bank of India, Australia and China* [1916], 41 Phil., 596; 12 *Manresa, Comentarios alCodigo Civil*, pp. 416, et seq.; *Ocejo, Perez & Co. vs. International Banking Corporation* [1918], 37 Phil., 631.)"

We hold that in all actions or proceedings to set aside or nullify preferences or fraudulent transactions as void under the provisions of section 70 of Act No. 1956, known as the Insolvency Law, the assignee appears for, and represent, the general creditors, and that, in so far as the decision of this court in the *Kaisha* case is in conflict upon that point, it is hereby overruled.

Section 70 of the Act provides:

"If any debtor, being insolvent, or in contemplation of insolvency, within thirty days before the filing of a petition by or against him, with a view to giving a preference to any creditor or person having a claim against

him or who is under any liability for him, procures any part of his property to be attached, sequestered, or seized on execution, or makes any payment, pledge, mortgage, assignment, transfer, sale, or conveyance of any part of his property, either directly or indirectly, absolutely or conditionally, to anyone, the person receiving such payment, pledge, mortgage, assignment, transfer, sale, or conveyance, or to be benefited thereby, or by such attachment or seizure, having reasonable cause to believe that such debtor is insolvent, and that such attachment, sequestration, seizure, payment, pledge, mortgage, conveyance, transfer, sale, or assignment is made with a view to prevent his property from coming to his assignee in insolvency, or to prevent the same from being distributed ratably among his creditors, or to defeat the object of, or in any way hinder, impede, or delay the operation of or to evade any of the provisions of this Act, such attachment, sequestration, seizure, payment, pledge, mortgage, transfer, sale, assignment, or conveyance is void, and the assignee, or the receiver, may recover the property, or the value thereof, as assets of such insolvent debtor. If such payment, pledge, mortgage, conveyance, sale, assignment, or transfer is not made in the usual and ordinary course of business of the debtor, or if such seizure is made under a judgment which the debtor has confessed or offered to allow, that fact shall be prima facie evidence of fraud. Any payment, pledge, mortgage, conveyance, sale, assignment, or transfer of property of whatever character made by the insolvent within one month before the filing of a petition in insolvency by or against him, except for a valuable pecuniary consideration made in good faith, shall be void. All assignments, transfers, conveyances, mortgages, or incumbrances of real estate shall be deemed, under this section, to have been made at the time the instrument conveying or affecting such realty was filed for record in the office of the register of deeds of the province or city where the same is situated."

The important question here is whether the transaction in question constitutes a valid lien in favor of the bank, or a preference which is void as to creditors.

We do not agree with counsel for the bank that the letters of August 21st and 25th and September 4th are in legal force and effect warehouse receipts. It is very apparent that the bank itself did not treat or consider them in the form or nature of warehouse receipts. They recite:

"In addition to security now in your hands covered by Quedanes, as collateral of my daily overdraft I hold in my godown of No. 209 Estero de Binondo:

11,780 Buntal hats valued

P41,230.00

6,150 Balibuntal hats valued

46,125.00

87,355.00

=====

which bring my position to a total of

P321,556.94."

When the bank took the actual physical possession of the property in question, it was removed to the warehouses of Derham Bros., Inc., by which a warehouse receipt, with all of its legal formalities and in the usual and ordinary form, was issued to, and in favor of, the bank.

Prior to that time the bank never had the actual control or physical possession of the property described in the August and September letters. Although when written the letters may have had some legal value as between the bank and De Poli, yet, standing alone and without possession, they did not create any vested rights in the bank as between it and the creditors of the insolvent estate. The record shows that the bank took the physical possession of the property in question on November 22, 1920, sixteen days prior to the time that De Poli was adjudged insolvent. Hence, the question becomes important as to how, why and in what capacity the bank took possession, and whether it then knew or had reasonable grounds to believe that De Poli was insolvent.

Upon the question of knowledge, in its opinion the trial court says:

"On November 22, 1920, when the said Umberto de Poli was at least suspected by the claimant bank of impending insolvency, the said bank obtained possession of the 22,920 Philippine hats described in the letters of August 21 and September 4, 1920, and of 42,046 meters of the 102,000 meters of sinamay described in the letter of August 25, 1920, and stored the same with the Derham Warehouse & Shipping Co., for which it received warehouse receipt No. 1701 in its own name."

Upon that point, Mr. Brandt, the credit man of the bank, testified:

"Q. And that was the first time that you knew that U. de Poli was about to be declared insolvent?—A. I had an intimation of it at the time of the delivery of the merchandise to us.

"Q. Why was your attorney along with you ?—A. The depressed physical appearance of Mr. De Poli lead me to think he was in trouble.

"Q. Why did you come to go down there and get that property on November 22d? Who told you to do that?—A. Manager Beldon.

"Q. Did you ask him why?—A. He stated that he wished to obtain additional security to cover Mr. De Poli's overdraft with us, and that Mr. De Poli had agreed to turn over certain merchandise already pledged to us.

"Q. Is it not a fact that these hats and this silk voile were taken from the U. de Poli bodega at night?—A. It started in the afternoon about four or five o'clock and continued until about eight o'clock possibly.

"Q. Referring to your statement about the depressed condition of Mr. U. de Poli at the time you took delivery of these hats and this sinamay, how was that depression evidenced?—A. Mr. De Poli was very sad and depressed.

"Q. Did he shed tears?—A. In the presence of me and Colonel Wolfson, he cried.

"Q. And that lead you to suspect, for the first time as I understand it, that he was in financial difficulties, is that so?—A. Yes, sir."

Mr. Schwarzkopf, who was then one of the attorneys for the bank, testified:

"A. No, sir, my advice was based upon the fact that there was a rumor in the streets that the Philippine National Bank was about to take over the U. de Poli assets.

"Q. Why were they about to do that?—A. I did not know.

"Q. And when you gave the bank this advice you told them, did you not, to take possession of this merchandise immediately, working day and night if necessary, and to get all they could out of this bodega?—A. I told them to work quickly, and if necessary to work day and night."

The reasons why, the time and manner in which the bank took possession clearly indicate that it knew, or that at least it had reasonable grounds to believe, that De Poli was then insolvent.

Again, it is very apparent from the time and manner of taking possession that it was not done "in the usual and ordinary course of business of the debtor." It clearly indicates that the bank thought and felt that an emergency existed, and that prompt action was required. The fact that the bank then surrendered two of the letters in question to the insolvent is conclusive proof that it then knew of the existence of the letters, and that it then at least thought and understood that the letters were of no legal value to the bank without possession of the property. In other words, it then took possession of it to further protect and secure its claim.

Among other things section 70 provides:

"Any payment, pledge, mortgage, conveyance, sale, assignment, or transfer of property of whatever character made by the insolvent within one month before the filing of a petition in insolvency by or against him, except for a valuable pecuniary consideration made in good faith, shall be void."

On page 35 of its opinion in the Kaisha case, this court says:

"There is no dispute about the facts between the Hongkong Bank and the intervener. Both agree that the title to the coal in question was in Chua Teng Chong. As above indicated, Chua Pue Tee, acting for Chua Teng Chong, attempted to pledge the coal to the bank on the 13th of April, 1914, by means of the private document, Exhibit 5. The bank, acting in good faith and without any knowledge of the insolvency of Chua Teng Chong, turned over to the latter's representative, Chua Pue Tee, the P30,000 in cash in consideration for the so-called pledge of April 13. On April 16 the bank, having in the meantime discovered that Chua Teng Chong was insolvent, secured a real pledge and took physical possession of the coal." (36 Phil., 35.)

In other words, it is admitted there that, as a part of the transaction and concurrent with the making and delivery of the private document there in question, the Hongkong & Shanghai Bank parted with, and delivered to Chua Teng Chong, "the P30,000 in cash in consideration for the so-called pledge of April 13." That was a present loan as distinguished from a preexisting debt, in and by which the bank then and there parted with its money with the express understanding and agreement that it should have and receive a pledge of the property to secure the P30,000. Therein lies the important legal distinction between it and the instant case. Again, for aught that appears there, it was the only transaction between the parties.

Here, De Poli was a customer of the bank with which he had numerous previous dealings and a large overdraft at the time the letters in question were written, and the transaction in question was one of many dealings which he previously had with the bank, and the testimony of Mr. Brandt above quoted is clear and convincing that the bank took possession "to obtain additional security to cover Mr. De Poli's overdraft with us." Assuming that to be true, it would follow that at the time the bank took possession it had other and different security for its claim against De Poli, and that possession was taken to secure a preexisting debt, and that the transaction in question was not a pledge or transfer of property for a valuable pecuniary consideration made in good faith within the meaning of that portion of section 70 above quoted.

In his supplemental brief of December 17th, counsel for the bank points out that in one of his former briefs it is said:

"That these promises to pledge 'may possibly have been executed to some extent in consideration of a preexisting debt.' " And

" 'The bank in the present case was constantly advancing money to the debtor at the time of the execution of the private documents or promises to pledge as is sufficiently shown on the face of those documents and by the proofs offered in this case.' "

He then points out that:

"The balance of the daily overdraft on August 21, 1920, when the letter promise of that date was delivered to the bank was P321,556.94: On the delivery of the letter of August 25, 1920, P348,925.94, and on the delivery of the letter of September 4, 1920, P419,500.94. Thus it appears that the debtor U. de Poli overdrew his current account to the extent of P97,944 from August 12, 1920, the date of the first letter, to September 4, 1920, the date of the third and last letter promise to pledge; that is to say, the debtor drew and the bank parted with that amount as a present or subsequent advancement against the security represented by those two letter promises, and whatever other security may have been deposited with the bank during the same period.

"Subsequent to the execution and delivery of the letter promise of September 4, 1920, the claimant bank, through the same current account thus secured by the three letter promises, advanced additional sums against all the securities deposited until the total overdraft amounted to over seven hundred thousand pesos * * *. This total overdraft, together with the list of the securities held by the bank, shows conclusively that the latter, after the deposit of such securities, including the three letter promises to pledge, advanced against such securities sums largely in excess of their value."

From which it is contended that the bank relied upon the letters for any advances which it made after September 4th. That position is not tenable and is not sustained by the proof.

With all due respect to learned counsel for the bank, there is no financial statement of the bank in the record before us which shows the condition of De Poli's account with the bank between those dates. The first entry in Exhibit GG is December 16, 1921. Exhibit A shows the condition of his account as of December 15, 1921, and neither exhibit shows the condition of his bank account at any time during the year, 1920. It is true that in his letter of August 21st De Poli says:

"Which bring my position to a total of P321,556.94." And in the one of August 25th, he says:

"Which bring my today's position to a total of P348,925.94."

And in the one of September 4th, he says:

"Will bring my today's position to a total of P419,500.94."

But this court has no legal right to accept De Poli's statements in the letters as to the amount of his overdraft in the bank as of those dates. Accepting his statement of P348,925.94 as of August 25th, and adding to it the P14,645, the value of the merchandise stated in the letter of September 4th, you have a total of P363,570.94, and in the letter of September 4th De Poli says:

"Will bring my today's position to a total of P419,500.94"

showing an unexplained difference of P55,930.

If it be a fact that the letters in question were written under an agreement with the bank that it would loan De Poli

a specific amount on the merchandise evidenced by each letter, and that the bank made him the loan under such an agreement and later took possession of the merchandise described in the letters, another and a different question would be presented, and the decision in the Kaisha case would then be in point. But, here, the evidence tends to show that the letters in question were written and possession of the property taken to secure an open current account in the form of an overdraft evidencing a preexisting debt as distinguished from a present loan, and there is a failure of proof to show that the letters were written under an agreement to secure a present loan, or that the bank made a present loan and parted with its money under any such an agreement.

Again, it will be noted that the letters in question are not public instruments, and that neither of them is acknowledged or filed of record.

Article 1865 of the Civil Code says;

"No pledge shall be effective as against a third person unless evidence of its date appears in a public instrument."

In the case of *Te Pate vs. Ingersoll*, above quoted, it is further said:

"A pledge, to be valid against third persons, must be evidenced by a public instrument. This is a mandatory condition prescribed by article 1865 of the Civil Code, which must be met in order to constitute the contract of pledge. An assignee is a 'third person' within the meaning of this article of the Civil Code."

Upon the facts in the record here, the assignee represents the creditors, and is a third person within the meaning of article 1865.

From what has been said, it follows that the judgment of the lower court on the merits must be affirmed.

The assignee did not appeal. Hence, many of the questions discussed in his brief are not legally before this court. Suffice it to say that, upon the question of value, we agree with the findings and conclusions of the trial court as to the good faith of the bank and the disposition which it made of the property, the accounting which it should make, and the basis for its liability.

In their respective briefs and oral arguments, there is more or less criticism of each other by opposing counsel, which is wholly immaterial and of no value to the court. Suffice it to say that no attorney ought to be criticized for the making of an honest legal effort to protect the interest of his client.

The judgment of the lower court is affirmed, without costs to either party, and the case is remanded for an accounting and such further proceedings as are not inconsistent with this opinion. So ordered.

Malcolm, Avanceña, Villamor, Ostrand, and Romualdez, JJ., concur.

CONCURRING

STREET, J.:

I concur in the conclusion reached in this case but am unable to assent to the proposition that the decision in *Mitsui Bussan Kaisha vs. Hongkong & Shanghai Banking Corporation* (36 Phil., 27), contains anything that must be overruled. A careful examination of that decision will show I think that it rests upon the indisputable fact that the Hongkong & Shanghai Bank was pledgee in due course and for a valuable pecuniary consideration paid in good faith. The pledge was therefore in all respects valid and could not be impeached by anybody, whether the

pledgor, the vendor of the coal, or the assignee in bankruptcy. It must be confessed that the true ratio decidendi of that decision is not expressed with absolute clarity; and at one point the court might seem to have accepted the contention, advanced by the attorneys for the Mitsui Bussan Kaisha, that "the assignee in bankruptcy is not a third person, but stands in the shoes of the bankrupt." But it cannot be fairly stated that the court intended to adopt the proposition thus broadly stated. The pledge there effected was undoubtedly binding on everybody, including the pledgor, the assignee in bankruptcy, and on the Mitsui Bussan Kaisha, who claimed in a right hostile to both. But this was because of the bona fide character of the pledge. Approaching insolvency, it must be remembered, does not discapacitate a merchant from making transfers or pledges in ordinary course, and a person who acquires rights by a bona fide purchase, or pledge, for value paid down, acquires an indefeasible right even though the transaction should be made on the very eve of insolvency.

In the case before us the pledge which was finally perfected by the delivery to the Asia Banking Corporation of the warehouse receipts issued by the Derham Company, was clearly not made "in the usual and ordinary course of business of the debtor." It was therefore prima facie invalid by the express provision of section 70 of Act No. 1956; and it was incumbent on the pledgee to show that the pledge was in fact made in good faith for a valuable pecuniary consideration. Now, assuming that this requirement could have been met by proof showing that the pledgee had advanced money in reliance upon the agreement to pledge contained in the letters of August 21, August 25, and September 4, 1920, yet we cannot discover that the bank did actually advance anything contemporaneously with or subsequent to the writing of those letters, upon the faith of the security therein pledged. On the contrary it would seem that the imperfect pledge thereby attempted was made for the purpose of securing advances that had already been made. We note in this connection that in each of those letters De Poli uses an expression which, it is suggested, indicates the extent of his overdraft and that this overdraft was increasing *pari passu* with the increase in the amount of merchandise thereby agreed to be pledged. The expression referred to is that in which De Poli speaks of his "position;" but "my to-day's position" as there used by him evidently refers, not to the extent of his existing overdraft, but to the amount of merchandise intended to be pledged. This is clearly shown by a comparison of the letters of August 21 and August 25, from which it will be seen that he is stating the total of the merchandise pledged, or intended to be pledged. It results that those letters show nothing with reference to the state of the contemporary overdraft. It therefore cannot be inferred, even remotely, that the bank advanced anything additional upon the faith of the increase in the amount of the intended collateral.

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