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SOME PROBLEMS OF PREFERENTIAL TRANSFERS IN WEST VIRGINIA

ROBERT EVANS STEALEY*

In West Virginia prior to 1891 unless a preference fell within the classification of a fraudulent or voluntary transfer or conveyance it was not inhibited. There is a vast difference, historically and actually, between a fraudulent conveyance and a preference, and the consequences to the parties involved that may flow from each. The condemnation of fraudulent conveyances by statute is ancient; that of preferential transfers a modern development of the law. It is not the purpose here to deal with fraudulent or voluntary transfers or conveyances, but only with certain aspects of preferences, involving principally those effected by a sale or conveyance to a third person or by a direct or indirect payment in money.

The common law not only condoned but encouraged the obtaining of preferences by diligent creditors. The race was to the swift. As it was put by Judge Brannon in *Herold v. Barlow*:

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1 Fraudulent and voluntary conveyances by an insolvent debtor are regulated by W. Va. Code c. 40, art. 1, §§1, 2, 3 and 4 (1931). Except for the inclusion in §§3 by the Revisers of that Code of a definition, partial or complete, of the terms transfer or charge, §§1 and 2 retain almost the literal language of Va. Code c. 118, §§1 and 2 (1849), and are the same as §§5184 and §5185 of the present (1942) Virginia Code. Said §§1, 2 and 3 of the W. Va. Code are as follows: Section (1) "Every gift, conveyance, assignment, or transfer of, or charge upon any estate, real or personal, every suit commenced, or decree, judgment, or execution suffered or obtained, and every bond or other writing given, with intent to delay, hinder, or defraud creditors, purchasers, or other persons, of or from what they are or may be lawfully entitled to, shall as to such creditors, purchasers, or other persons, their representatives or assigns, be void. This section shall not affect the title of a purchaser for valuable consideration, unless it appear that he had notice of the fraudulent intent of his immediate grantor, or of the fraud rendering void the title of such grantor."

Section (2) "In sections three, four and five of this article the word 'transfer' shall be taken to include every gift, sale, conveyance or assignment; and the word 'charge' shall be taken to include every confessed judgment, trust deed, mortgage, lien or encumbrance."

Section (3) "Every transfer or charge which is not upon consideration deemed valuable in law shall be void as to creditors whose debts shall have been contracted at the time it was made; but shall not, upon that account merely, be void as to creditors whose debts shall have been contracted, or as to purchasers who shall have purchased, after it was made; and though it be decreed to be void as to a prior creditor because voluntary, it shall not for that cause be decreed to be void as to subsequent creditors or purchasers."

2 13 Eliz. c. 5; 27 Eliz. c. 4, in force in Virginia prior to the revolution, and enacted by the General Assembly in 1785, c. 64, effective from Jan. 1, 1787. See Va. Rev. Code c. 101 (1819).

3 47 W. Va. 750, 755, 36 S. E. 8 (1901).
“By the common law it is perfectly lawful in a creditor to obtain, and in a debtor to give a creditor, preference over other creditors, if the intent is merely to prefer a creditor, and not to hinder or defraud other creditors. Such preferences may injure, but it does not defraud, other creditors. . . . It makes no difference about the secret motives of the creditor, as the law takes no cognizance of such motives, and cannot assign a bad motive to an act not wrong either in itself or in its consequences, because, in law, a motive having a lawful end in view, and resulting in proper action, not condemned by law, cannot be called a bad motive. Here self-preservation is regarded as the law of nature. It makes no difference that the creditor knows that the party is insolvent when he gets his preference. . . . He defeats other creditors lawfully to save his own honest debt. He simply uses diligence to save himself, and the law rewards that diligence by giving him its fruits. It is immaterial how such lawful preference is accomplished, whether by absolute conveyance of the fee, or by mere mortgage of judgment.”

Except as modified by the Bankruptcy Act⁴ this is yet the law of Virginia. There the only transfers or charges made by an insolvent debtor which can be attacked by a creditor are those without consideration or fraudulent in fact.⁵ And the Virginia rule is the prevalent state of the law in the vast majority of the states, as Ohio appears to be the only state other than West Virginia having a general preference act.⁶ The original West Virginia

⁵ VA. CODE §§5184, 5185 (1942). See note 1, supra. In Surratt v. Eskridge, 131 Va. 325, 108 S. E. 677 (1921), the Virginia law is summed up thus: “Now at common law and under the Virginia statute against fraudulent conveyances it is well settled, and is unquestioned before us, that an insolvent debtor, known by himself at the time to be insolvent, may make a valid conveyance of a portion or the whole of his assets to a bona fide creditor or creditors, in satisfaction of an account of existing indebtedness if, that is the sole purpose of the debtor, and the transfer is for full value, although such conveyance may and is intended by the grantor and grantee or grantees to give such creditor or creditors a preference to the exclusion of others in the distribution of the assets of the debtor. In such case other creditors are not lawfully entitled to any share in the assets transferred to the preferred creditor or creditors. What the law sanctions cannot be regarded as unlawful. In such case it is only where the transfer is not made with the sole purpose on the part of the debtor of making a bona fide preference among his creditors, and where that is merely an incident of the transactions, used as a cloak for some other purpose which is fraudulent in actual intent, that the transfer is regarded as unlawful.”
⁶ OHIO GEN. CODE §1104 (1938). Several other states have statutes regulating assignments for the benefit of creditors and conveyances or transfers by insolvent corporations. The Uniform Fraudulent Conveyances Act, which has been adopted in twenty states, does not affect preferences, §§3 thereof providing that an antecedent debt shall constitute fair consideration for a conveyance by an insolvent debtor.
section substitution. In 1895 it was revised and amended in certain particulars which will be hereafter noted. The Revisers of the 1891 Code transferred to another section the definitions of transfer as including every "gift, sale, conveyance or assignment" and charge as including every "confessed judgment, trust deed, mortgage, lien or encumbrance," and placed the remainder of the 1895 act, without amendment, as c. 40, art. 1, §§5, where it yet remains, without change.

7 W. Va. Acts 1891, c. 123, amending W. VA. CODE c. 74, §2 (1868), derived from VA. CODE c. 118, §2 (1849). The act added the following after the original language of the section which declared void voluntary transfers: ". . . and every gift, sale, conveyance, assignment, transfer or charge, made by an insolvent debtor to a trustee, assignee, or otherwise, giving or attempting to give a priority or preference to a creditor or creditors of such insolvent debtor, or which provides or attempts to provide for the payment, in whole or in part, of a creditor or creditors of such insolvent debtor, to the exclusion or prejudice of other creditors, shall be void as to such priority, preference or payment so made or attempted to be made; and all such gifts, sales, conveyances, assignments, transfers and charges, shall be deemed void as to such priority, preference or payment; and every such gift, sale, conveyance, assignment, transfer or charge shall be deemed, taken and held to be made for the benefit of all the creditors of such debtor except as hereinafter provided; and all the estate, property and assets given, sold, conveyed, assigned, transferred or charged as aforesaid, shall be applied upon the debts and paid to the creditors of such insolvent debtor, pro rata; Provided, That nothing in this section shall be taken or construed to change, impair or affect any prior lien, priority or incumbrance acquired by a creditor on the real estate of such debtor in any manner now prescribed by law; Provided further, That nothing in this act contained shall be taken or construed to change or impair or affect the transfer, sale or assignment of bonds, notes, stocks, securities or other evidences of debt in payment of, or as collateral security for, the payment of a bona fide debt or to secure any endorser or surety, whether said transfer, sale or assignment is made at the time said debt is contracted or endorsement made, or for the payment or security of a pre-existing debt.”

8 W. Va. Acts 1895, c. 4. The text is the same as the present act (note 10, infra), except that the definition of transfer or charge was placed in another section. (See note 9, infra).

9"W. VA. CODE c. 40, art. 1, §3 (1981).

10 "Every transfer or charge made by an insolvent debtor attempting to prefer any creditor of such insolvent debtor, or to secure such a creditor or any surety or endorser for a debt to the exclusion or prejudice of any other creditor, shall be void as to such preference or security, but shall be taken to be for the benefit of all creditors of such debtor, and all the property so attempted to be transferred or charged shall be applied and paid pro rata upon all the debts owned by such debtor at the time such transfer or charge is made. Provided, That any such transfer or charge by an insolvent debtor shall be valid as to such preference or priority unless a creditor of such insolvent debtor shall institute a suit in chancery within one year after such transfer or charge was made to set aside and avoid the same and cause the property so transferred or charged to be applied toward the payment pro rata of all the debts of such insolvent debtor existing at the time such transfer or charge is made, subject, however, to the provisions hereinafter contained with reference to creditors uniting in such suit and contributing to the expenses thereof. But if such transfer or charge be admitted to record within eight months after it is made, then such
It might have been expected that a statute so in derogation of the common law, and constituting such an innovation, would receive a strict construction by the court. But in the first case decided under it a contrary intention appeared. In Wolf v. McGugin,\(^{11}\) decided January 28, 1893, under the original 1891 act, it was held that insolvency meant an insufficiency of all the debtor's property to pay all his debts,\(^{12}\) and that whether the preferred creditor had notice or knowledge of the fact of insolvency was immaterial.\(^{13}\) And in Baer Sons Grocer Co. v. Williams\(^{14}\) the court held that a deed of trust to secure a bona fide present loan of money, executed when the grantor was insolvent, was a preference, because the statute made no exception in such case. Also, there being no period of limitation provided for the bringing of suits to set aside suit to be availing must be brought within four months after such transfer or charge was admitted to record. Every such suit shall be deemed to be brought in behalf of the plaintiff and all other creditors of such insolvent debtor, but the creditor instituting such suit or proceeding, together with all creditors of such insolvent debtor who shall come into the suit and unite with the plaintiff before final decree and agree to contribute to the costs and expenses of such suit, shall be entitled to have their claims first paid in full pro rata out of the property so transferred or charged, in preference to any creditor of such debtor who shall before final decree decline or fail so to unite and agree to contribute to the costs and expenses of such suit, but not in preference to such creditor as may attempt to sustain the preference given him by such transfer or charge: Provided further, That nothing in this section shall be taken to prevent the making of a preference as security for the payment of purchase money or a bona fide loan of money or other bona fide debt contracted at the time such transfer or charge was made, or as security for one who at the time of such transfer or charge becomes an indorser or surety for the payment of money then borrowed; And provided further, That nothing in this section contained shall be taken to affect any transfer of bonds, notes, stocks, securities or other evidences of debt in payment of or as collateral security for the payment of, a bona fide debt, or to secure any indorser or surety, whether such transfer is made at the time such debt is contracted or indorsement made or for the payment or security of a preexisting debt.”

\(^{11}\) 57 W. Va. 552, 16 S. E. 797 (1899).

\(^{12}\) This definition has been consistently followed, except as to banks, Ream's Drug Store v. Bank, 115 W. Va. 66, 174 S. E. 788 (1934); Carr v. Summerfield, 47 W. Va. 115, 34 S. E. 804 (1901).

\(^{13}\) The Bankruptcy Act has always required on the part of the creditor reasonable cause to believe the debtor insolvent, or that a preference would be effected at the time of the transfer, to constitute a voidable preference. 30 Stat. 562 (1898), as amended, 11 U. S. C. §96 (1946). Any such preference may be avoided by the trustee if the creditor receiving it or to be benefited thereby or his agent acting with reference thereto has, at the time when the transfer is made, reasonable cause to believe that the debtor is insolvent.” Section 60 (b) of Act of 1898 (30 Stat. 562) used the test “shall have had reasonable cause to believe that it was intended thereby to give a preference.”

\(^{14}\) 43 W. Va. 323, 27 S. E. 345, decided January 19, 1897, involving a transfer under the original 1891 Act.
preferences, it was held that only the equitable doctrine of laches would restrict the time.\textsuperscript{15}

The latter two holdings pointed up inadvertencies of the 1891 act which probably caused the 1895 revision, although the cases were decided after the amendment. A limitation of one year, or four months after the recordation of a recordable instrument, was provided. Any suit by a creditor was to be a "class" suit and not, as in the case of a suit to set aside a transfer as fraudulent in fact, for the prior benefit of the first plaintiff. And preferences given for a present consideration were excluded.\textsuperscript{16}

As amended, apart from the proviso excepting a transfer of "bonds, notes, stocks, securities or other evidences of debt" from its operation, the statute would seem well designed to attain its evident object—a fair distribution of the estate of an insolvent debtor among his creditors.\textsuperscript{17} The reason for the proviso is not apparent. It would appear necessary in order to protect the free negotiability of such paper as subsequent bona fide purchasers for value, without notice, would be protected under other principles of law, and the proviso could have been expressly so limited, if thought needful.\textsuperscript{18} The Bankruptcy Act contains no such exception. It specifically covers the transfer of "any property" of the bankrupt.\textsuperscript{19} There being no logical reason for the exception in the West Virginia statute, as long as it remains there it should be construed as narrowly as possible so that it will conform as nearly as can be to the coverage of the Bankruptcy Act. But subsequent interpretation apparently expanded its scope. The court first held that transfers of paper within the exception were governed by the common law,\textsuperscript{20} and, shortly thereafter, that an "evidence of debt"

\textsuperscript{15} Herold v. Barlow, 47 W. Va. 750, 36 S. E. 8 (1900), holding that a delay of four years and four months constituted laches; Casto v. Greer, 44 W. Va. 332, 33 S. E. 110 (1897), holding that the limitation period in the 1895 amendment operated prospectively only.

\textsuperscript{16} See notes 8, 10, supra.

\textsuperscript{17} As it was succinctly put in Baer & Sons v. Williams, note 14, supra, by Dent, J.: "In other words, the insolvent debtor's property being limited, the design of the law is to prevent his disposition thereof in such manner as to have the same applied on some of his debts, to the exclusion of others, and to cause the same to be divided pro rata, that all may share alike."

\textsuperscript{18} For example, see the proviso protecting holders in due course of negotiable paper from the lien of an execution duly docketed in W. Va. Code c. 98, art. 4, §10 (1931).


\textsuperscript{20} Frank v. Zeigler, 46 W. Va. 614, 33 S. E. 761 (1899). In this case the transferees of the notes failed to benefit by the exception. Z, insolvent, sold a stock of goods to S, his son-in-law, who gave promissory notes for the purchase price to Z, who transferred the same to three banks to which he was indebted.
included an assignment of an open account, although the language would seem to include only evidence of debt executed at the time of the creation of the debt, and intended to be evidence thereof, such as bonds or notes.

Concurrently and mixed with the problem as to the scope of the proviso arose the question as to whether the statute covered indirect as well as direct transfers whereby a creditor was preferred.

In several cases the debtor sold to a third person, sometimes a creditor and sometimes not, who thereupon gave his notes for the purchase price, or a part thereof, to designated creditors of the debtor, or directly paid named creditors in money. In such situation are the creditors thus preferred compelled to account to the attacking creditor for the preference thus received by them, or are they protected by the exception, or some other principle of law? There are two lines of cases which cannot be reconciled.

In *Wolf v. McGugin*, one M sold to A and B a stock of goods for which they agreed to discharge certain notes payable to

Certain attaching creditors brought suit to set the sale aside as fraudulent. The court held it to be fraudulent in fact and void in toto, whereby the attaching creditors have priority over the bank. Although the facts are basically the same, the problem involved in *Merchants & Co. v. Whitescarver*, note 28, infra, and similar cases as to whether the giving of notes in such circumstances constituted a transfer within the proviso was not discussed, the finding of fraud in esse making it unnecessary.

21 *Carr v. Summerfield*, 47 W. Va. 155, 34 S. E. 804 (1899). In *Small Ferrer, Inc. v. Ware*, 68 F.2d 366 (4th Cir. 1934), where certain creditors claimed that an assignment of funds due from certain fire insurance companies was good because made more than four months prior to bankruptcy, under 30 STAT. 562 (1898), as amended, 11 U. S. C. §96 (1946), the court held that it was nevertheless void because covered by W. VA. CODE c. 40, art. 1, §5 (1931) and not within the exception, the court confining the meaning of the exception to “stocks, bonds, notes, etc., the physical possession of which would be transferred to the pledgee in accordance with ordinary commercial practice, not to shield a transfer by way of assignment of incorporeal assets, made with a view of granting a preference to certain favored creditors.” *Carr v. Summerfield* was not cited. In view of *Erie R. R. v. Tomkins*, 304 U. S. 64, 114 A. L. R. 1487 (1937), holding that federal courts must follow the decisions of state courts of last resort in matters of local law, the case seems valueless as a precedent, although it certainly expresses the better view.

22 If the purchaser was a creditor, he would be permitted to share pro rata for the amount of his debt with the attacking creditors, *Wilson v. Carrico*, 50 W. Va. 336, 40 S. E. 439 (1901); *Westinghouse Lamp Co. v. Ingram*, 70 W. Va. 664, 74 S. E. 941 (1912); or, if part cash was paid the purchasing creditor would be entitled to preference for the cash paid the debtor, *Moore v. Thorn*, 112 W. Va. 37, 163 S. E. 617 (1932); *Herold v. Barlow*, 47 W. Va. 750, 36 S. E. 8 (1901). So that the core of the problem is the right of attacking creditors to reach the cash or notes in the hands of other preferred creditors to whom they may have been delivered, and declare the notes void or require the creditor who has been paid in cash to refund.

23 37 W. Va. 552, 16 S. E. 797 (1893). This sale would not be voidable under the Bulk Sales Law, W. VA. CODE c. 40, art. 2 (1931), first enacted by W. VA. Acts 1909, c. 78, §1.
It means any act done by an insolvent debtor devoting any part of his property in any way, so that its legal effect is to give preference to one creditor over another. No matter about the form of the instrument . . . where as in this case, the sale is to an absolute purchaser, with a provision that he devote the purchase money to preferred creditors, we ought to regard the transfer valid to pass title, and hold only the purchase-money liable to all creditors . . . if a person purchase property of an insolvent debtor, not for cash, but agree as a part of the transaction to devote the consideration to pay certain creditors of the seller to the exclusion of others, that is an act falling under the bar of the statute.”

This came very close to the theory that any transfer which diminishes the insolvent debtor’s estate to the benefit of an existing creditor is preferential and void. It was, and is, obviously the theory which would most nearly effectuate the purpose of the act. Otherwise, through the indirect means of a sale, with the purchaser as a conduit, a preference could be effected which would be voidable if made directly.

The judicial climate soon changed, however, and in three cases beginning with Merchants & Co. v. Whitescarver, which involved a factual situation almost indistinguishable from the Wolf case, the court, without citing that case, in effect overruled it, holding that the making of the purchase money notes by the purchaser directly to creditors was a transfer within the exception and that, even without the exception, the giving of the notes would have been good as a “payment” of creditors by the debtor, saying, “if the sale to [M] had been made for cash, the firm could have taken the money and paid off these debts, and neither the plaintiffs nor any other of their creditors could have recovered it.” This is the first intimation that a payment in money would not con-
Three months later the court decided Armstrong v. Oil-Well Supply Co., a suit which grew out of the Wolf case in which the liability of the purchaser to a creditor on notes given for a part of the purchase price was involved. The creditor was not a party to the Wolf suit at the time of its appeal and defended on the ground that the note was given in consideration of the release of an attachment. The court not only held that this was sufficient to furnish a present consideration for the note and remove it from the status of a pre-existing debt, the soundness of which seems questionable, but held that the decision in Merchants & Co. was directly in point and governed. This, to all practical purpose, would seem to overrule the Wolf case.

At almost the same time Herold v. Barlow was decided. Here the insolvent had sold certain real estate for a consideration which included (a) payment by the purchaser of liens binding on the land, (b) payment by the purchaser of certain general creditors of the insolvent in cash and (c) credit to the purchaser on account of antecedent debts due from the insolvent. As the case arose prior to the amendment of 1895 there was no applicable statute of limitations and it was dismissed for laches in delaying the suit for four years and four months. But the opinion expresses the view that the purchaser would be protected for amounts expended under (a) and (b), although as to (c) the conveyance was a preference. The discharge of valid liens was certainly not a preference as the creditors holding same received nothing they were not already entitled to receive, the property having a value in excess of the liens. But the other creditors who were paid by the purchaser clearly received cash instead of the unsecured obligation of the insolvent. The proceeds of the insolvent's estate were used to pay them and the transaction was no different, in effect, than if the insolvent had conveyed directly to them and they had sold the

26 This case also followed the erroneous doctrine of Mack v. Prince, 40 W. Va. 328, 21 S. E. 1014 (1895), to the effect that the motives of the debtor were material in determining whether transfer was voidable as a preference. Certainly in the case of a conveyance fraudulent in fact, the intent of the debtor is a determining factor, but the only inquiry regarding a preference should be the effect of the transfer, i.e., whether it secures to the creditor transferee an unfair share of the estate of the insolvent. First National Bank v. Parsons, 42 W. Va. 197, 24 S. E. 554 (1896), which had held that the fraudulent intent of the grantor was immaterial, was ignored, but Warren Refining Co. v. Dyer, 101 W. Va. 452, 132 S. E. 877 (1926), now seems to firmly establish the principle that a transfer may be voidable as a preference in the absence of any fraudulent intent.

27 47 W. Va. 455, 35 S. E. 967 (March 24, 1900).

28 47 W. Va. 750, 36 S. E. 8 (April 7, 1900).
property. The opinion assigns no reason why a payment in cash would not constitute a preference but simply says that the purchaser should be preferred because the insolvent could lawfully have paid the unsecured creditors in cash.\textsuperscript{29} This begs the question.

While a court might be reluctant to force a purchaser, even though a creditor, to lose actual cash paid to acquire the debtor's property, this result could be avoided by impleading the creditors who were preferred by payment from the purchaser, forcing them to disgorge, and allowing the purchaser credit for the money paid. And this is exactly what the court did in the next case decided involving a similar situation. In \textit{Powers-Taylor Drug Co. v. Faulconer},\textsuperscript{30} the insolvent sold his stock of goods and drug store fixtures to a bank cashier, individually. The cashier assumed a lien against the fixtures, paid off several execution lien creditors and a note of the insolvent to the bank of which he was an officer. This note appeared to be well secured by accommodation endorsers. Immediately afterwards the purchaser sold a half interest in the goods and fixtures for the amount of his original purchase. The transaction was attacked both as a preference and as fraudulent in fact. The trial chancellor set it aside on the latter ground, requiring the purchaser to account to the attacking creditor for the full purchase price.

Upon appeal the transaction was held a preference but not a fraudulent transfer. The bank was required to account and pay to the attacking creditor its pro rata share of the money it received from the purchaser. Although the opinion relies upon \textit{Wolf v. McGugin} as authority for the proposition that a sale is a transfer within the statute,\textsuperscript{31} it is evident from its context that some of the

\textsuperscript{29} \textit{Id.} at 763. "I think too that as the Barlows paid to Hevner and others, who were general creditors of Lockridge, valid debts, the Barlows would get the benefit of them over other creditors even. Why? Because those creditors could lawfully receive cash in payment of their debts, and also because the Barlows furnished cash to pay them; and this is just the same as it would be if paid to Lockridge."

\textsuperscript{30} 52 W. Va. 581, 44 S. E. 204. Submitted January 23, 1902. Decided March 28, 1903.

\textsuperscript{31} Note 23, \textit{supra}. Poffenbarger says, 52 W. Va. 581, 589, 44 S. E. 204 (1903), "The word sale, as used in this statute, is not expressly limited to a sale to the creditor. Whether it is to be so limited, is a matter of construction, and the construction of the statute ought to be such as to give it the effect intended by the legislature, so far as that intent is made plainly manifest by the statute. The force and effect of the statute ought not to be frittered away by refinement and technicality. Certainly not, by mere play upon words. This statute is in derogation of the common law, it is true, and ought not to be so construed as to be carried beyond the purpose for which it was passed. But it ought to be liberally expounded for the accomplishment of that salutary purpose, the
court concurred only because they perceived a design and conspiracy among the debtor, the purchaser and the bank to prefer the latter. The soundness of Merchants & Co. v. Whitescarver was questioned but it was not overruled.\(^{32}\) And the Armstrong and Barlow cases were not mentioned.

But in Garner v. Martin,\(^{33}\) decided ten years after Powers-Taylor Drug Co. v. Faulconer, the court returned to the principles of the Wolf case and applied them without equivocation. Here the insolvent purchased a house and lot but the seller neglected to secure and record a lien for the unpaid purchase money. The debtor later sold to a third party, who, as a part of the consideration, paid the original seller his debt. The object of the suit was to require the seller thus preferred to distribute the money received as a preference pro rata among the debtor's creditors. This relief was allowed as against the contention that the statute did not embrace the payment of a bona fide debt. As to this, the court said:

"Yet it does, when the payment is brought about through the force of a transfer constituting an unlawful preference. The statute directly prohibits the securing of a pre-existing debt through any transfer by an insolvent debtor if the same operates as a preference over other creditors."

The Wolf and Drug Co. cases were cited but the Merchants & Co. and companion decisions were ignored. This appears to be the last decision upon a comparable state of facts.

If the Garner case is to be accepted as the present law, then it follows that (a) Merchants & Co. and companion cases are, in effect, overruled, (b) preferences accomplished through sales, whether to a creditor or an innocent third party, are under the ban of the statute and creditors thus preferred may be required to account to those left out of the distribution, and (c) a payment of a debt by a purchaser as a part of the sales price is a preferential transfer.

But is a payment of a debt in money, made by an insolvent debtor directly to the creditor, a preference? In the Herold\(^{34}\) and

\(^{32}\) 52 W. Va. 581, 586, 44 S. E. 204 (1903): "For the appellants, it is insisted that the case is within the principle announced in Merchants & Co. v. Whitescarver, 47 W. Va. 36 . . . . If the facts disclosed by the evidence placed this case on the footing of the one just referred to, and made it necessary to pass upon the soundness of that decision, I should be inclined to question it. It enables an insolvent debtor to do indirectly what he is forbidden to do directly by the plain and express language of the statute, namely, to turn his property over to a part of his creditors to the exclusion of others."

\(^{33}\) 73 W. Va. 407, 80 S. E. 495 (1913).

\(^{34}\) Note 26, supra.
cases a bald assumption that it was not was used as a premise to rebut the proposition later expressly propounded by the Garner case, that a payment in money by indirection was a preference. No authority was ever cited to support the assumption, and unless there is sound logic and reason to the contrary, a transfer in money ought to be as much a preference as a transfer of any other property. Certainly it diminishes the estate of the insolvent no less, and this is the test under the Bankruptcy Act. While the application of the rule under that act has sometimes occasioned difficulty because of the seeming unfairness of its application to particular situations, it is now unquestioned that a payment in money is a preferential transfer by a bankrupt if the other necessary elements are present. Thus, unless there is an impediment in the West Virginia statute itself, those creditors who receive payment in money ought to be as liable to account as those who receive real estate or other tangible property.

Does the proviso which excepts a transfer of “bonds, notes, stocks, securities or other evidences of debt,” embrace a direct payment in money? The payment may be either in currency or by check. If by the latter, no evidence of debt would change hands as a check is a mere order on the drawee bank to pay, and is not an

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35 Note 22, supra.


37 For example, the problems involved in the allowance of set-offs particularly as to bank deposits against notes held by a bank against the bankrupt are illustrative. This set-off is allowed, unless the bank had “active” knowledge of insolvency or “procured” the deposit. This peculiar rule is justified by Glenn on the theory of the bank’s duty as a public servant to accept deposits in the ordinary course of business, although all the authorities deny that a bank is a public utility. See Glenn, Fraudulent Conveyances §407. Also the problem concerning the status of payments on a running account, where many courts have followed the “net-result” theory of diminution of the bankrupt estate. See the discussion of Glenn, at §411. Under the present act no distinction as to running accounts seems to be recognized. Campanella v. Liebowitz, 103 F.2d 252 (9d Cir. 1939), 39 Am. B. R. (N.S.) 655 (1939). Likewise the question of payment of “running expenses” of the business. This seems to hark back to the original exception from a “fraudulent preference” of a payment in due course made by Lord Mansfield in Rust v. Cooper, 2 Cowp. 269 (1777). Glenn, §411 places the nonpreferential character of such payments on the ground that they constitute a fair exchange of values and preserve the business as a going concern. The present extent of the exception, if any, is doubtful.

38 See also, in general, Remington, Bankruptcy §1663 et seq. (5th ed. 1940).

39 Notes 7, 10, supra.
assignment pro tanto of the bank's deposit liability to the drawer;\textsuperscript{40} but if the payment be by currency, a more difficult problem is presented.

A considerable part of what passed for money in this country was formerly in the form of demand notes. Bank notes, at one time the chief form of this medium of exchange, were simply promises to pay on demand. All of this circulation, except that of national banks, was effectively curtailed in 1865 by the imposition of a confiscatory tax of ten per cent.\textsuperscript{41} And such circulation by national banks ceased about 1935 when the government redeemed the only bonds eligible by law as security for the notes.\textsuperscript{42}

The currency\textsuperscript{43} presently in circulation consists of gold certificates,\textsuperscript{44} silver certificates,\textsuperscript{45} United States notes,\textsuperscript{46} and Federal Reserve notes.\textsuperscript{47} All are equally legal tender.\textsuperscript{48} As such none of them can be said to be an "evidence of debt" since, by legislative fiat, their value as currency is independent of any obligation to pay. They are themselves the medium in which any debt must be paid. So that a transfer of currency cannot be a transfer of an "evidence of debt" within the West Virginia statute.

The Garner opinion, although it does not mention the earlier decisions to the contrary, and does not expressly consider whether

\textsuperscript{40} W. Va. Code c. 46, art. 16, §6 (1931); Negotiable Instruments Law §189. "A check of itself does not operate as an assignment of any part of the funds to the credit of the drawer with the bank, and the bank is not liable to the holder, unless and until it accepts or certifies a check."

\textsuperscript{41} 13 Stat. 484 (1865), as amended 26 U. S. C. §1900 (b) (1946).

\textsuperscript{42} The statutory provisions governing the issue of circulating notes by national banks were not repealed. See 12 U. S. C. §§101 et seq. (1946). In effect Federal Reserve notes were substituted therefor. Act of March 9, 1933, c. 1, §401, 48 Stat. 6 (1933), amended 12 U. S. C. §445 (1946) so that the Federal Reserve banks could substitute their own notes for the bonds retired and which secured the outstanding national bank notes. Having served its purpose it was repealed by act of June 12, 1945, c. 186, §3, 59 Stat. 238 (1945).

\textsuperscript{43} 48 Stat. 344 (1934), 31 U. S. C. §444 (1946) defines "currency of the United States" as "currency which is legal tender in the United States, and includes United States notes, Treasury notes of 1890, gold certificates, silver certificates, Federal Reserve notes, and circulating notes of the Federal Reserve banks and national banking associations."


\textsuperscript{45} 31 U. S. C. §§405, 405a, 406 (1946).

\textsuperscript{46} 31 U. S. C. §§401-404 (1946). Issue limited to $382,000,000,00


\textsuperscript{48} 48 Stat. 52 (1933), 31 U. S. C. §462 (1946), as amended, 48 Stat. 113 (1933), 31 U. S. C. §462 (1946). Prior to this act some were legal tender for certain purposes only.
a payment in money is within the statute, the case being considered as if the property transferred itself was the medium of payment, necessarily raises an inference that not only a preference created through the indirect medium of a sale is within the ban, but that a payment in money must be also because the property was converted into money. Nevertheless, legislative clarification of the West Virginia statute in order to assure an equitable distribution of the property of an insolvent among his creditors, and in order to eliminate any doubt as to its application to the situations discussed herein would seem desirable.

Certainly the proviso excepting transfers of bonds, notes, etc., ought to be eliminated. There is no basis for it in principle. And if this loophole be plugged, it would seem fair to add the requirement of the Bankruptcy Act⁴⁹ that the creditor must, at the time of the transfer, have reasonable cause to believe the debtor insolvent. This would seem enough to protect all "good faith" situations, and we would then have a preference statute, roughly comparable to the Bankruptcy Act in its scope and usefulness in state practice.

⁴⁹ See note 13, supra.