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SECTION 4 OF THE BANKRUPTCY ACT:  
THE EXCLUDED CORPORATIONS  

MICHAEL I. SOVERN*

Section 4 of the Bankruptcy Act excludes from both voluntary and involuntary bankruptcy municipal, railroad, insurance and banking corporations and building and loan associations, and excludes from involuntary bankruptcy corporations that are not "moneyed, business or commercial."1 The exclusion of railroad and municipal corporations lost much of its significance when special reorganization provisions were enacted for those corporations.2 Insurance and banking corporations and building and loan associations, on the other hand, are excluded from the Bankruptcy Act's

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1. 30 Stat. 547 (1898), as amended, 11 U.S.C § 22 (1952). The full text of this section is as follows:
   
   (a) Any person, except a municipal, railroad, insurance, or banking corporation or a building and loan association, shall be entitled to the benefits of this title as a voluntary bankrupt.

   (b) Any natural person, except a wage earner or farmer, and any moneyed, business, or commercial corporation, except a building and loan association, a municipal, railroad, insurance, or banking corporation, owing debts to the amount of $1,000 or over, may be adjudged an involuntary bankrupt upon default or an impartial trial and shall be subject to the provisions and entitled to the benefits of this title. The bankruptcy of a corporation shall not release its officers, the members of its board of directors or trustees or of other similar controlling bodies, or its stockholders or members, as such, from any liability under the laws of a State or of the United States. The status of an alleged bankrupt as a wage earner or farmer shall be determined as of the time of the commission of the act of bankruptcy.

corporate reorganization chapters as well as from straight bankruptcy; and creditors can no more compel a corporation that is not moneyed, business or commercial to reorganize than they can compel it to liquidate.⁶

This article will be concerned with several questions raised by section 4. First, how have bankruptcy courts defined banks, insurance corporations, building and loan associations and corporations that are not moneyed, business or commercial?⁴ Second, how should these terms be defined? And, third, should all, or any, of these exclusions be retained? We shall preface our discussion of these questions with a summary of the legislative history of section 4 since corporations were first made amenable to bankruptcy in 1867.

I. LEGISLATIVE HISTORY

As originally drafted, the Act of 1867 would have made all corporations amenable to both voluntary and involuntary bankruptcy.⁵ Fear was expressed in the Senate that "[U]nder the involuntary system proceedings would be instituted against religious and educational and eleemosynary corporations and they would be wound up."⁶ To avoid this danger, the bill's floor manager offered to limit the statute to "moneied and business" corporations. This dialogue ensued:

Mr. Howard. Let me suggest as a substitute for the word "busi-

3. Corporate reorganization under Chap. X of the Bankruptcy Act is possible only for a corporation "which could be adjudged a bankrupt under this Act, and any railroad corporation excepting a railroad corporation authorized to file a petition under section 77 of this Act." Bankruptcy Act §§ 106(3), 526, 52 Stat. 883, 885 (1938), 11 U.S.C. §§ 506(3), 526 (1952). This has been interpreted to mean that a voluntary petition for reorganization may be filed only by a corporation which could file a voluntary petition in bankruptcy, and an involuntary petition for reorganization may be filed only against a corporation which could be filed against in bankruptcy. See 6 Collier, Bankruptcy §§ 2.07, 4.05, 4.06 (14th ed. 1943), and authorities there cited. An arrangement under Chap. XI of the Bankruptcy Act is available only to "a person who could become a bankrupt under section 4 of this Act and who files a petition under this chapter." Bankruptcy Act §§ 306(3), 321, 322, 52 Stat. 906, 907 (1938), 11 U.S.C. §§ 706(3), 721, 722 (1952). Consequently, a corporation which cannot file a voluntary petition in bankruptcy cannot file a petition for an arrangement. See 8 Collier, Bankruptcy §§ 2.09, 4.02 (14th ed. 1943), and authorities there cited.

4. We will not consider the questions raised by the Bankruptcy Act's peculiar definition of "corporation." See Bankruptcy Act § 1(8), 30 Stat. 544 (1898), as amended, 11 U.S.C. § 1(8) (1952). They have been ably treated elsewhere. See, e.g., McLaughlin, Amendment of the Bankruptcy Act, 40 Harv. L. Rev. 341, 355 (1927); Tondel, Corporations Eligible for Relief under Section 77B, 21 Minn. L. Rev. 144 (1937); Weinstein, Corporations Amenable to Section 77B, 83 U. of Pa. L. Rev. 853 (1935). The question with which we are concerned is: assuming that a particular entity is a corporation within the meaning of the Bankruptcy Act, what must be shown to bring it within one of the excluded classes?


6. Id. at 989.
ness" the word "commercial." It seems to me that the word "business" is a little more comprehensive than the word "commercial," and may be construed to include all corporations to carry on any kind of business, even the business of distributing charities or the business of employing teachers in schools, or of conducting religious exercises. Certainly the Senator from Vermont does not design to include such corporations. . . .

Mr. Poland. I desire to obtain precisely the same result by this amendment that the Senator from Michigan desires, if we can only agree upon the exact word. My amendment proposes to limit this section to moneyed and business corporations, and the Senator from Michigan proposes the word "commercial" instead of the word "business."

Mr. Howard. Then I will suggest to the Senator to add the word "commercial," so that it will read, "moneyed, business, or commercial corporations."

Mr. Poland. I accept that.

And so did the rest of Congress, notwithstanding the fact that by limiting voluntary as well as involuntary proceedings to "moneyed, business, or commercial corporations" the amendment went considerably further than the fear expressed required.

The bill which, substantially overhauled, was to become the Bankruptcy Act of 1898 employed a different approach to the subject of corporate bankruptcy. Voluntary bankruptcy was closed to all corporations; involuntary was open to all corporations except national banks. In response to the objection that the latter provision would permit municipalities and other governmental corporations to be involuntarily adjudicated, the bill's definition of corporation was amended on the Senate floor to read, "[A] body doing business as a merchant, broker, banker, trader, manufacturer, or miner . . . ." However, largely because of anti-corporation sentiment, corporations were entirely excluded from involuntary as well as from voluntary bankruptcy before the bill passed the Senate.

The bill reported by the House Judiciary Committee reverted to the original Senate provision on corporations, subjecting all corporations except national banks to involuntary bankruptcy and excluding all corporations from voluntary bankruptcy. The same objections to the involuntary provision that had been raised in the

7. Id. at 1002.
10. See id. at 787.
11. Id. at 789.
12. See ibid.
13. See id. at 801.
Senate were again brought up in the House,\textsuperscript{16} but they did not prevail. The statement of Congressman Bodine, one of the opponents of the corporate provision, was unique and rather significant in view of the form section 4 was to take in 1910:

This bill is the first one of its kind to include corporations at all.\textsuperscript{16} It may be that there is a certain class of corporations that are as appropriately made subject to its provisions as are natural persons. I refer to those engaged in mining, manufacturing, merchandising, trading, and the buying and selling of property of any kind, and, in fine, engage in any business of the same kind as that usually carried on by individuals. But this bill goes much further than this. It embraces insurance companies...; it embraces building and loan associations, trust companies, savings banks, and all other State banks.

Now, in nearly every State in the Union there are chapters on chapters of the statutes regulating to the smallest minutia the proceedings in case of the insolvency of any of those classes of corporations. It is made the duty of designated officials to make critical and periodical examination of their affairs, to proceed against them when insolvent, and to take charge of their property, including the securities deposited for the protection of the beneficiaries... and, in fine, to do and perform all the duties of a trustee in bankruptcy.

Under this bill a trustee in bankruptcy becomes the insurance commissioner, the railroad commissioner, the bank examiner and commissioner, and the building and loan commissioner of the several States...[N]ot content with invading the domain of the State, not content with its jurisdiction over every kind of corporation organized for business purposes, it invades the domain of charity and religion.

If a church is a corporation and is guilty of an act of insolvency—which it can be under this bill without violating a single precept of the Master—it can be thrown into bankruptcy, and the trustee can take into his possession and sell the bread and wine and the cup and plate which contain them and the sacred book itself \textsuperscript{[laughter]}, and leave its members nothing except their hope of salvation in another world...\textsuperscript{17}

Mr. Bodine's statement was not to influence the House's action, for the Committee's bill passed,\textsuperscript{18} nor can it be ascertained whether the conference committee appointed to settle the differences between the House and Senate bills took any notice of what he said, but by 1932 all save one of the exclusions suggested by him have

\textsuperscript{15} See id. at 1794.
\textsuperscript{16} This, of course, is an error. See text at notes 5-8 supra and authorities there cited.
\textsuperscript{17} 31 Cong. Rec. 1939 (1898).
\textsuperscript{18} See id. at 1947.
found their way into the Bankruptcy Act. Further, when the courts are called upon to divine the reason for the exclusion of banks, insurance corporations and building and loan associations, Mr. Bodine's thoughts appear in the opinions with surprising frequency, although no reference to him is ever made.\(^{19}\)

The conference committee's bill, which became the Bankruptcy Act of 1898, retained the bar against voluntary bankruptcy for corporations, supplemented the exclusion of national banks from involuntary bankruptcy by excluding banks incorporated under state or territorial law as well, and limited involuntary bankruptcy in general to corporations "engaged principally in manufacturing, trading, printing, publishing, or mercantile pursuits."\(^{20}\) This list of corporations subject to involuntary bankruptcy bears a strong resemblance to the list originally inserted on the Senate floor,\(^{21}\) but it is improbable that the conference committee, like the Senate, adopted the list merely to avoid the involuntary adjudication of governmental corporations. The committee's explanation for excluding from involuntary bankruptcy banks and all corporations not enumerated appears in a statement accompanying the conference report: "The great railroad and transportation companies and banks incorporated under any law are left to be dealt with by the laws of the State creating them. It would lead to much confusion and hardship and many complications should we undertake to subject the great railroad and transportation corporations to the provisions of this act. It is believed that they can be better dealt with under other laws."\(^{22}\) No effort is made to explain why it is desirable to leave certain corporations "to be dealt with by the laws of the states creating them." The Senate bill's exclusion of national banks had been justified by the Senator in charge of the bill on this basis: "There is already in existence a satisfactory law for the control and liquidation of national banks. Since the Government is responsible for the bank notes issued by these banks in the event of their failure, there is good reason why it should have control of their liquidation."\(^{23}\) The conference committee's rather vague statement leaves us to conjecture whether these factors were at all influential in the committee's thinking.

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21. See text supra at note 11.
22. 31 Cong. Rec. 6427 (1898).
23. 30 Cong. Rec. 606 (1897).
To a considerable extent the 1910 amendment of section 424 was a throwback to the Act of 1867. Corporations, with the exception of municipal, railroad, insurance and banking corporations, were readmitted to voluntary bankruptcy, and "any moneyed, business, or commercial corporation, except a municipal, railroad, insurance, or banking corporation," could be adjudicated an involuntary bankrupt. The House Report, which is quoted without more by the Senate Report, indicates that one of the reasons for the change from the 1898 formulation was a need for clarification, but Congress probably did not think it was merely tinkering with the existing statute. The House Report goes on to say:

The words substituted ["moneyed, business, or commercial corporation"] are taken from the bankruptcy law of 1867, and their meaning has long since been settled by the courts. The reason for exempting the quasi-public corporations will be apparent. Banks are excepted from the operation of the law at present. Other business entities having similar responsibilities to the public are now also excepted.

That something different from the 1898 Act was being done is also indicated by the statement of the manager of the bill: "The changes here are intended to broaden the present law so far as it affects corporations. As the law now stands only corporations 'engaged principally in manufacturing, trading, printing, publishing, mining, or mercantile pursuits' can be proceeded against by creditors. There is no good reason for these distinctions."

The business corporations completely excluded from bankruptcy by the amendment are essentially those suggested by Congressman Bodine during the House debate on the Act of 1898. Was his reason for differentiating between those corporations and others the reason for the distinctions made by the amendment? Are railroad, insurance and banking corporations different from others because, "it is made the duty of designated officials to make critical and periodical examination of their affairs, to proceed against them when insolvent, and to take charge of their property...."? The committee report says only that corporations having "responsibilities to the public" similar to those of banks are excepted.

25. See text at notes 5-8 supra.
28. 45 Cong. Rec. 2276 (1910). Mining corporations had been added to the list of corporations that might be adjudicated involuntary bankrupts in 1903. Act of February 5, 1903, c. 487, 32 Stat. 797.
29. See text at note 17 supra.
The next step with which we are concerned occurred in 1932, when building and loan associations were added to the cluster of excluded corporations. Only trust companies were now lacking to complete Congressman Bodine's list. Why this new exclusion? The House Report tells us first that, "Every reason which obtains for exempting [banks, etc.] obtains in so far as building and loan associations are concerned." Consequently, when the Report goes on to give the reasons for the new exception, we might expect to find the committee's view of the reasons for the exceptions created by the 1910 amendment.

"It has been suggested that by reason of the fact that in two States in the Union no law exists controlling building and loan associations that this might be a reason for not exempting these associations from the operation of the bankruptcy law. It will be remembered that if the bankruptcy law is not invoked in connection with building and loan associations that this in no way interferes with the State equity laws, and whether a State has supervisory control over building and loan associations or not those interested may at all times take advantage of State insolvency laws. Building and loan associations are of a peculiar nature, associations functioning almost exclusively in local communities. The deposits received are from local depositors and the securities taken are local securities. Therefore, it seems the part of wisdom to leave the administration of these matters in the local courts."

The first two quoted sentences are interesting for their implication about the committee's position on Congressman Bodine's rationale. State supervision is apparently not the controlling factor, for "whether a State has supervisory control over building and loan associations or not those interested may at all times take advantage of State insolvency laws." The Report rather clearly rests the exception of building and loan associations on the ground that they are local institutions. Obviously, then, the reason for exempting building and loan associations cannot have been the reason for at least two of the other exceptions; the exclusion of railroad and insurance corporations could not conceivably have been based on the ground that they were local institutions. The locality point was also made on the floor of Congress, but Mr. Bodine's theory fared better there than it did with the committee, one congressman stating:

I have had some experience in the management of these building and loan associations. They are entirely under the management of State laws. Nearly all of them have State inspectors to check

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32. Ibid.
up on their books and securities. They are subject to the State law respecting voluntary assignments and receiverships, and there is every reason why they should be taken out from under the Federal Bankruptcy law and be allowed the usual course taken under State management and State law.\textsuperscript{33}

The next significant action on this subject is the enactment in 1934 of section 77B which declared eligible for corporate reorganization "Any corporation which could become a bankrupt under section 4 of this Act."\textsuperscript{34} Congress thus adopted for its new remedy of reorganization the exclusions it had worked out earlier for liquidation.\textsuperscript{35} Counsel to a special committee set up to study bankruptcy and receivership later said, "It is doubtful whether the draftsmen gave any real consideration to the problem, it being more probable that they chose the easier method of adopting a standard already set up in section 4 of the Bankruptcy Act."\textsuperscript{36}

Whatever mysterious attraction the standard of section 4 held

\textsuperscript{33} 75 Cong. Rec. 3041 (1932), Sen. Rep. No. 120, Ser. No. 9487, 72d Cong., 1st Sess. (1932), the Senate Judiciary Committee's Report on the bill exempting building and loan associations from bankruptcy, offers no reasons in support of its recommendation that the bill be enacted into law.

\textsuperscript{34} Act of June 7, 1934, c. 424, 48 Stat. 911.

\textsuperscript{35} The statement in the text is subject to the qualification that corporate reorganization was possible to a limited extent under § 12 of the Bankruptcy Act even before the adoption of 77B. Section 12 permitted a debtor to propose a composition to his creditors after a petition in bankruptcy had been filed. Obviously, since a petition could not be filed by or against a corporation excluded by § 4, the § 4 exclusions were applicable to this limited form of reorganization as well as to liquidation. For a summary of the various inadequacies of § 12 as a reorganization device, see 6 Collier, Bankruptcy § 0.03 (14th ed. 1943). Because of these inadequacies, § 12 was a little-used and insignificant provision of the Bankruptcy Act, and was repealed in 1938 by the Chandler Act. 52 Stat. 840 (1938), 11 U.S.C. § 30 (1952). It remains true, then, that the primary function of the Bankruptcy Act before the adoption of 77B was liquidation, and there is little doubt that the § 4 exclusions were adopted with an eye to that function rather than to reorganization.

\textsuperscript{36} Report of the Counsel to the Special Committee to the Chairman of the Special Committee to Investigate Receivership and Bankruptcy Proceedings and Administration of Justice in United States Courts, Sen. Doc. No. 268, 74th Cong., 2d Sess. 43 (1936). However, after section 77B was enacted, Congressman Tom McKeown, chairman of the Subcommittee on Bankruptcy of the House Judiciary Committee, stated that the problem was considered by the conference committee on the bill that was to become 77B:

While the bill was pending in the Senate for passage, a great urge came to make eligible for relief banks, insurance companies, and building and loan associations which had ceased functioning as such, but the request came too late to put the amendment in the bill in the Senate. When the conference met, an amendment was offered to take care of the situation. The difficulty that faced the conference committee was the fact that the language defining what corporations could avail themselves of the privileges of the bill had passed the Senate just as it came from the House, so that the conference committee under the rules could not change the first part of section 77B. McKeown and Langeluttig, Federal Debtor Relief Laws 4 (1935).

The Senate had, however, added to the House provision permitting a petition for reorganization after a proceeding in bankruptcy has been commenced, the
for the original draftsmen of section 77B apparently manifested itself to the authors of Chapter X, the Chandler Act's replacement for section 77B, for section 106(3) provides that "'corporation' shall mean a corporation, as defined in this Act, which could be adjudged a bankrupt under this Act..." The section 4 exclusions were also adopted for Chapter XI, under which corporations and individuals may adjust their unsecured debts without suffering liquidation. The legislative history contains no clues to why the liquidation standard was adopted for reorganization provisions.

clause, "whether or not the corporation has been adjudicated a bankrupt." The conference committee was free, therefore, to amend this provision, and, according to Mr. McKeown, took advantage of this to make defunct banks, insurance companies and building and loan associations eligible for reorganization by adding, "provided the present operations of such corporation do not exclude it hereunder." Id. at 5, 109-111. As a result, the section permitted "Any corporation which could become a bankrupt under section 4 of this Act" to seek corporate reorganization either by original petition or by petition "in any proceeding pending in bankruptcy, whether filed before or after this section becomes effective, provided the present operations of such corporations do not exclude it hereunder, and whether or not the corporation has been adjudicated a bankrupt..." Act of June 7, 1934, c. 424, 48 Stat. 911. Mr. McKeown's account explains why the language he claims made defunct banks, insurance companies and building and loan associations eligible for reorganization does not appear where one would expect to find it, but it hardly explains the singular lack of relation between what this language seems to say and what Mr. McKeown claims for it. All that language seems to do is deny to a corporation by or against whom a bankruptcy proceeding has been begun the right to petition for reorganization if its present operations would make it ineligible for bankruptcy. It says nothing about making corporations excluded by section 4 eligible for reorganization if they have ceased doing business. Nothing in the legislative history of 77B indicates that the rest of Congress shared Mr. McKeown's understanding of the conference committee's amendment. In fact, neither the committee reports, the Congressional Record, nor the reported hearings on section 77B reflect the "great urge" to which Mr. McKeown refers. The only indication of concern appearing in these materials is the insertion in the Congressional Record of a speech by the superintendent of insurance of New York before a convention of insurance commissioners in which he suggests that one possible way of dealing with some of the difficulties of insurance company liquidation would be to bring insurance corporations under the Bankruptcy Act. 77 Cong. Rec. 5222 (1933). A number of cases expressly rejected the contention that the "present operations" clause rendered defunct banks, insurance corporations and building and loan associations eligible for reorganization. E.g., In re Union Guarantee & Mortgage Co., 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935); In re Peoria Life Ins. Co., 75 F.2d 777 (7th Cir.), cert. denied, 296 U.S. 594 (1935). Finally, the "present operations" clause was omitted from Chapter X of the Bankruptcy Act, the Chandler Act's replacement for 77B, and nothing in the legislative history of Chapter X suggests that Congress thought that this omission changed the law on the eligibility for reorganization of corporations excluded by section 4.

What conclusions can we draw from these various expressions of Congress as to what is meant by a banking or insurance corporation, a building and loan association, or a corporation that is not moneyed, business or commercial? Congress' intent with respect to the content of "moneyed, business or commercial" is fairly clear. The phrase first appears in the Act of 1867 as a response to the objection that unless bankruptcy is restricted to such corporations, religious, educational and eleemosynary institutions might be involuntarily adjudicated. And, as we shall see, the cases decided under the Act of 1867 faithfully excluded religious, educational and eleemosynary corporations from the scope of "moneyed, business or commercial corporations," and confined that term to corporations engaged in the pursuit of financial gain. When the language is adopted again in the amendment of 1910, the House and Senate Reports refer specifically to the judicial interpretation: "The words substituted [moneyed, business or commercial corporation] are taken from the bankruptcy law of 1867, and their meaning has long since been settled by the courts." We can expect to find, then, that the delimitation of corporations that are not moneyed, business or commercial has proved to be a relatively easy chore for the courts.

How much guidance does the legislative history give in defining the other excluded corporations? For example, is there anything to help a court decide whether a fraternal benefit society is an insurance corporation because it pays death benefits to the beneficiaries of its members? It might be argued that Congress left the insolvency administration of banking and insurance corporations and building and loan associations to state law for the reason suggested by Mr. Bodine, that "[I]n nearly every State in the Union there are chapters on chapters of the statutes regulating to the smallest minutia the proceedings in case of the insolvency of any of those classes of corporations." Therefore, the argument would run, a fraternal benefit society should not be deemed an insurance corporation unless the statutes of the state of incorporation specifically provide for close regulation of such societies by officials who are to take charge of the corporation in the event of insolvency. The argument suffers badly from the lack of evidence in the history of section 4 that the rest of Congress shared Mr. Bodine's views. There is slight support

39. See text at notes 5-8 supra.
40. See text at note 199 infra.
42. See text at note 17 supra.
in the deliberations preceding the passage of the Act of 1898, and in the debate preceding the exemption of building and loan associations, but hardly enough to sustain the proposition that Congress excluded banks, insurance corporations and building and loan associations primarily because they were so extensively regulated by the states. 43 The argument suffers, too, from Congress' failure to exclude all closely regulated enterprises from bankruptcy.

Another argument might draw upon the House Report on the amendment of 1910 which justified the exclusion of railroad and insurance corporations on the ground that their "responsibilities to the public" were similar to those of banks: 44 since a fraternal benefit society has extensive responsibilities to the public, it should be deemed an insurance corporation and held ineligible for bankruptcy. But even if the legislative history contained additional support for a "responsibilities to the public" test, it would have to be rejected as too vague to be helpful in the resolution of a close case.

Finally, we have the possibility of an argument based on the House Report which emphasized the local operation of building and loan associations as the reason for exempting such corporations from bankruptcy: 45 if a fraternal benefit society's activities are not confined to one community, it should be eligible for bankruptcy and hence should not be characterized as an insurance corporation. The argument is easily refuted by the fact that many companies which are concededly insurance corporations conduct their business on an interstate scale. Therefore, Congress certainly did not exclude insurance corporations from bankruptcy because they were local enterprises, and the geographical scope of a debtor's activities should not be used to determine whether or not it is an insurance corporation.

It is, of course, possible, perhaps even probable, that banks, insurance corporations and building and loan associations were not all excluded from bankruptcy for the same reasons. It is possible, too, that Congress had no more definite reason than a reluctance to bring such crucial financial institutions within the purview of a statute aimed primarily at liquidation, but preferred to leave them under the aegis of the states and to courts of equity, where rehabilitation would at least be a possibility. However, the failure of the Chandler Act to make reorganization available to the excluded

43. The support offered by the debate on the bill exempting building and loan associations is more than offset by the implication in the House Report on that bill that state supervision is not crucial. See text at note 32 supra.
44. See text at note 27 supra.
45. See text at note 32 supra.
corporations indicates that, whatever the earlier view of Congress, it was not moved by this consideration in 1938. It is also possible that the members of Congress had no particular alternative remedy in mind, but simply did not wish to include corporations so important to our economy under a statute which permitted liquidation, and later reorganization, to be compelled in the event of insolvency by so unrepresentative a group as three creditors. In that event, though, it would not have been necessary to exclude them from voluntary as well as from involuntary bankruptcy.

Whatever purposes Congress may have intended to achieve by excluding banking and insurance corporations and building and loan associations from bankruptcy, the legislative history of section 4 does not clearly reveal them. Consequently, we can expect to find more judicial floundering when these exceptions are dealt with than when courts are obliged to construe the exemption from involuntary bankruptcy of corporations that are not "moneyed, business or commercial." In addition to being clearer, the legislative history of the moneyed, business or commercial clause indicates that the reasons for this exclusion are probably different from the reasons for the total exclusions. We shall, therefore, deal with these two different types of exclusion separately, considering first the more difficult problems presented by the exclusion of banks, insurance corporations and building and loan associations.

II. DEFINING BANKING AND INSURANCE CORPORATIONS AND BUILDING AND LOAN ASSOCIATIONS

A. The State Classification Test.

Three kinds of state action have been urged upon the courts as warranting a holding that a given corporation is exempt from bankruptcy, and hence to be left to the state of incorporation for liquidation or reorganization. These are: (1) that the state of incorporation has provided for liquidation or reorganization of corporations of this type;46 (2) that the state of incorporation has declared that corporations of this type shall not be subject to the Bankruptcy Act;47 and (3) that the state of incorporation has classified corporations of this type as banking or insurance corporations or building and loan associations.48 The first and second points are usually raised to bolster the third.

46. See, e.g., In re Prudence Co., 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935); Woolsey v. Security Trust Co., 74 F.2d 334 (5th Cir. 1934).
47. See In re Prudence Co., supra note 46.
Obviously, if these arguments are to be effective, it must be on the theory that Congress wished the state indication to control. Absent such a Congressional intent, the Bankruptcy Act would override any state expressions on the amenability of corporations to bankruptcy. The cases have not found this necessary intent when only the first two kinds of state action listed above are involved. In other words, the fact that the state of incorporation has provided for liquidation or reorganization of some corporations or that it has declared that those corporations shall not be subject to the Bankruptcy Act is not by itself sufficient to except them from bankruptcy.40

However, a number of cases have accepted as controlling the state of incorporation's classification of a particular corporation as a banking or insurance corporation or a building and loan association.50 The operation of the state classification test in a rather extreme form is illustrated by a comparison of two Second Circuit cases decided four months apart, In re Union Guarantee & Mortgage Co.51 and In re Prudence Co.52 The debtors in these two cases were in the business of "making mortgage loans on real estate and selling the mortgages to the public with [their] guaranty of payment."53 The Union Guarantee & Mortgage Company was held to be an insurance corporation and hence ineligible for reorganization under section 77B, but the Prudence Company was held to be neither a bank nor an insurance corporation and hence eligible for 77B reorganization.

In the Union Guarantee case, the court first decided that the purpose of excluding some corporations from bankruptcy was not self-evident and that the purpose had to be inferred "from such similarity as exists between the excepted groups."54 It found that the corporations excluded were "affected with a public interest" and required public supervision and control. From this the court reasoned that,

49. E.g., In re Prudence Co., 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935) (corporation held subject to Bankruptcy Act notwithstanding both state provision for liquidation and state declaration that corporations of this type shall not be subject to the Bankruptcy Act); Gamble v. Daniel, 39 F.2d 447 (8th Cir.), appeal dismissed, 281 U.S. 705, cert. denied, 282 U.S. 848 (1930) (corporation held subject to Bankruptcy Act notwithstanding state provision for liquidation).

50. E.g., In re Union Guarantee & Mortgage Co., 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935); Security Bldg. & Loan Ass'n v. Spurlock, 65 F.2d 768 (9th Cir.), cert. denied, 290 U.S. 678 (1933).

51. 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935).

52. 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1933).

53. Id. at 78; see 75 F.2d at 984.

54. 75 F.2d at 984.
The most natural inference is that Congress meant to leave to local winding up statutes the liquidation of such companies; that, since the states commonly kept supervision over them during their lives, it was reasonable that they should take charge upon their demise. If a state enacts that companies having powers of a prescribed kind must be regulated, that is of course authoritative; and, if in addition it classes the company as a bank or a railroad or an insurer, that too should be authoritative. This is true, not because Congress was bound to yield in such cases, but because otherwise its apparent purpose to leave the winding up of such companies to the state would not be effected; for the will of the state is no clearer to supervise the company than to class it as it does. When Congress excepted not all companies affected with a public interest, but specified kinds of such company, presumably it intended the states to define the kinds.

Thus we have no occasion to decide whether the debtor at bar ought not to have been incorporated under the New York Insurance Law and regulated as such, whatever such a statement could mean. Assuming that it should not, it was in fact so subject and so incorporated. The state has chosen to regard it so, and that is all we may ask.55

Unlike the Union Guarantee & Mortgage Co., the Prudence Co. was organized under the Banking Law of New York. Relying upon *In re Union Guarantee & Mortgage Co.*, the superintendent of banks argued that New York had classified the debtor as a banking corporation by allowing it to be incorporated under the Banking Law, subjecting it to the supervision of the superintendent of banks and providing a procedure for its liquidation. The argument was rejected on the basis of an extensive consideration of the New York Banking Law: New York had not classified this corporation as a bank because the Banking Law expressly contemplated the incorporation of several other types of corporation, in addition to banks, under that statute. In the course of rejecting the superintendent's argument the court also did some defining of banking independently of state classification,56 but it rallied back to the state classification test in its treatment of the contention that if the debtor was not a bank, it must have been an insurance corporation. "[T]he appellees reply that the state has not classified the debtor as an insurance company, since it was not organized under the Insurance law, and consequently we cannot, consistently with *In re Union

55. *Ibid.*

56. "Hence the debtor does not possess the power to receive deposits, which is generally recognized as the essential characteristic of a banking business." 79 F.2d at 79. See text at notes 76 to 86 *infra* for a consideration of the problems of characterizing banking corporations independently of state classification.
Guarantee & Mortgage Co. . . . hold the debtor exempt from bankruptcy as an insurer. We think this answer is sound."

Certainly any test is suspect when its application results in only one of two corporations empowered to engage in and actually engaging in the same business being held subject to bankruptcy. Putting aside for the present the question whether this apparent contradiction can be justified, the reasoning employed by the Second Circuit to arrive at the state classification standard is still subject to criticism. If Congress had excluded banking and insurance corporations and building and loan associations from bankruptcy primarily because they were extensively regulated by the states, then perhaps a finding of exclusion might properly follow from a finding that a debtor's state of incorporation subjected it to strict regulation as a member of one of the excluded classes. But since there is little evidence in the legislative history to support the proposition that close state regulation was the principal reason for Congress' action, and since Congress, instead of excepting from bankruptcy all corporations which the states may strictly regulate, excepted only a handful of such companies, the ultimate responsibility for distinguishing those companies from all others rests on the federal courts. And, of course, in the absence of some indication to the contrary, the definition of terms in a federal statute is a matter of federal law and not to be supplied by the states.

Neither the Prudence nor the Union Guarantee opinion contains any further justification for the state classification test, nor do most of the other cases which accept this standard. An exception is Security Building and Loan Association v. Spurlock, which supported the use of the state classification test for building and loan associations in this way:

[A]t the time this amendment [excepting building and loan associations] was passed many, if not all, of the states of the union had theretofore authorized the formation of building and loan associations described and characterized as such in the legislation authorizing the incorporation thereof. . . . It follows that when Congress enacted this legislation without any attempt to define the characteristics of the building and loan associations intended to be excluded from the operation of the Bankruptcy Act, it necessarily recognized the various definitions thereof in the statutes of the several states as indicating what constitutes a building and loan association in the respective states. To attempt by judicial construction to incorporate into the federal

57. Id. at 80.
58. See section 1, supra, of this article.
59. 65 F.2d 768 (9th Cir.), cert. denied, 290 U.S. 678 (1933).
law some definition of a building and loan association would be in effect to legislate upon that subject. Congress was satisfied to take the state statutes as they found them and we must do so.\textsuperscript{69}

This reasoning, too, is subject to criticism. That state definitions of building and loan association existed when building and loan associations were added to the list of excluded corporations is undoubtedly true. It could be argued that if a particular corporation would qualify as a building and loan association under all or most of the state statutes in existence in 1932, Congress must have intended it to be excluded, because that corporation is a building and loan association according to the generally accepted contemporaneous definition. But it does not follow that by failing to define the term, Congress intended to accept the definition of whatever state happened to be the state of incorporation of a particular debtor. The argument of the \textit{Spurlock} opinion would have greater force if, at the time of the amendment, the federal courts had definitely adopted the state classification test, but at that time the weight of authority favored independent characterization over acceptance of a state classification.\textsuperscript{61} As likely as the court's assumption is that the United States Building and Loan League, the sponsor of the amendment, felt that it would be tactically unsound to include a definition of building and loan association when one of the arguments to be used by the proponents of the amendments was the similarity of building and loan associations to the already excluded corporations,\textsuperscript{62} none of which was expressly defined by the Bankruptcy Act. In short, there is nothing in the legislative history of the 1932 amendment to indicate that Congress had any intent one way or the other on where the definition of building and loan associations was to be found in a close case.

Is there anything to be said on behalf of the state classification test? The preponderance of authority had shifted towards it between 1932 and 1938, but the use of the section 4 exclusions in Chapter X, enacted in 1938, cannot be regarded as an implied legislative adoption.

\textsuperscript{60} \textit{Id.} at 771.


\textsuperscript{62} See text at note 31 \textit{supra}.
of state classification because it was still not favored by all circuits and nothing in the legislative history indicates whether or not Congress was aware of its existence. If the state classification test offers a simple guide to lawyers attempting to predict whether a particular corporation will be held subject to bankruptcy, it can make some claim to legitimacy, for precise knowledge of available remedies will reduce litigation and help business managers and creditors to choose the most appropriate remedy. Wasted litigation can be especially harmful to a tottering corporation and its creditors, since, in addition to the expense involved, the corporation's position

63. See note 61 supra. Independent characterization was also employed in Clemons v. Liberty Savings & Real Estate Corp., 61 F.2d 448 (5th Cir. 1932), and in In re New York Title & Mortgage Co., 9 F. Supp. 319 (N.D. N.Y. 1934). However, insofar as the latter decision relies on independent characterization, it is presumably overruled by Prudence and Union Guarantee. Both state classification and independent characterization were relied upon in Capital Endowment Co. v. Kroeger, 86 F.2d 976 (6th Cir. 1936) (semble), Woolsey v. Security Trust Co., 74 F.2d 334 (5th Cir. 1934), and Kansas ex rel. Boynton v. Hayes, 62 F.2d 897 (10th Cir. 1932). Grand Lodge, Knights of Pythias v. McKee, 95 F.2d 474 (5th Cir. 1938), and In re Nat'l Mortgage Corp., 17 F. Supp. 54 (D. N.J. 1935), relied entirely on the state classification test.

Consequently, if Congress had attempted to ascertain the extent to which the state classification test was the law in 1938, it would have found: that the question had not been passed upon by the Supreme Court nor the First, Seventh and District of Columbia Circuits; that the Second and Ninth Circuits regarded state classification as controlling; that the most recent decision of the Fifth Circuit was in accord, although there were earlier indications to the contrary; that the state classification test had been regarded as controlling by a district court in the Third Circuit, but that the Court of Appeals for that circuit had not yet spoken clearly, see In re Order of Sparta, 242 Fed. 235 (3d Cir. 1917); that the Fourth and Eighth Circuits seemed to favor independent characterization; and that the Sixth and Tenth Circuits had given roughly equal weight to state classification and independent characterization.

While the preponderance of authority thus shifted towards the state classification test between 1932 and 1938, the test still was not sufficiently established to sustain the argument that by adopting the § 4 exclusions for Chapter X, Congress intended to ratify this judicial creation. Furthermore, even two of the leading cases espousing state classification contain language which smacks of independent characterization. Thus, in Security Bldg. & Loan Ass'n v. Spurlock, 65 F.2d 768, 772 (9th Cir.), cert. denied, 290 U.S. 678 (1933), the court looks beyond state classification, saying, "No one would dispute, and it is not disputed here, that the definition of a building and loan association contained in the Arizona statute is in accord with the general conception of such organization throughout the United States." And In re Prudence Co., 79 F.2d 77, 79 (2d Cir.), cert. denied, 296 U.S. 646 (1935), contains this statement: "Hence the debtor does not possess the power to receive deposits, which is generally recognized as the essential characteristic of a banking business. . . . And all of the cases, so far as we are advised, which have construed the words 'banking corporation' as used in the Bankruptcy Act, have regarded the legal power to receive deposits as the essential thing." On the question whether the debtor is an insurance corporation, the court concludes, "Since neither in common parlance nor by the terms of state legislation is the debtor regarded as an 'insurance company,' it cannot be exempt from bankruptcy under that phrase." (Italics supplied.) Id. at 80.
is apt to continue to deteriorate while it awaits its fate, and these additional losses may make the difference between liquidation and a successful reorganization.

In order to determine whether the state classification test produces substantial predictability, we must look further into how this standard has been applied by the courts. How is the state of incorporation's classification of a given enterprise ascertained? Obviously, when a bankruptcy court searches for a state classification, its inquiry must be translated into: What has some governmental organ of the state of incorporation said or done about this corporation or one like it? Any one of the three principal branches of government can conceivably be looked to for help, and, at one time or another, all have been.64

Legislative characterizations are most consistently invoked. For example, one court refused to hold the debtor before it an insurance corporation when the debtor was expressly exempted by statute from "all provisions of the insurance laws of this State, not only in governmental relations with the State, but for every other purpose."65 Another, rejecting the contention that the debtor was a bank, noted the failure of the legislature to impose double liability on the stockholders of corporations like the debtor when the state constitution required such liability to be imposed on the stockholders of banks.66 Several cases compared the debtor with an express definition of, say, "banking" found in the state statutes.67 The most common technique for discovering the legislature's classification is an examination of the statute under which the debtor was organized to determine what sort of enterprise the legislature contemplated should be incorporated under that statute.68 Thus, the fact that the debtor was organized under the state insurance law is highly

64. The usual caveat about blindly accepting a characterization of a term rendered in one context when the meaning of that term is at issue in a different context is probably not pertinent here. The rationale of the state classification test—which asks how the state of incorporation regards corporations of this type—necessarily requires a bankruptcy court to see how corporations of this type have been treated in non-bankruptcy contexts.

65. Grand Lodge, Knights of Pythias v. McKee, 95 F.2d 474, 476 (5th Cir. 1938).


persuasive evidence that the debtor is an insurance corporation, while incorporation under a statute other than the insurance law is virtually conclusive that the debtor is not an insurance corporation. In fact, according to the Prudence case, failure to incorporate under the insurance law prevents a debtor from being an insurance corporation even though it possesses the very same powers it would have obtained by incorporation under that statute. While this theory produced the different results in Prudence and Union Guarantee & Mortgage, it is consistent with the judicial rationale for the state classification test. The states are permitted to define insurance corporations because Congress' primary purpose in excluding them from bankruptcy was to avoid interference with the extensive regulatory schemes of the states, but if a debtor is not organized under the state insurance law, it probably will not be regulated as an insurance corporation, and so there is no reason to exclude it from bankruptcy. If we treat predictability, rather than the usual judicial rationale, as the basis for the state classification test, the different results in Prudence and Union Guarantee & Mortgage can still be justified. The status of a corporation will be easier to predict if the statute under which it was incorporated is controlling than if its activities and attributes must be compared with those of other corporations that have been adjudicated or denied adjudication as a bankrupt.

An administrative classification is often relied upon in conjunction with a legislative characterization. Every case which holds that a debtor’s state classified it as one of the excluded corporations contains some indication that the state administrative official in charge of such corporations treated the debtor as subject to his jurisdiction. Action or inaction by a state official is accorded less

69. In re Union Guarantee & Mortgage Co., 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935). In re Prudence Co., 70 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935), is not in genuine conflict with the proposition set forth in the text, even though it was held not to be a bank in spite of incorporation under the New York Banking Law. The New York Banking Law clearly contemplated that corporations other than banks would be organized under it. The title of that statute was “An Act in relation to banking corporations ... and corporations under the supervision of the banking department,” and the statute was subdivided into articles providing for the incorporation of banks, trust companies, safe deposit companies, and investment companies. Consequently, whether the debtor was organized under the Banking Law was only a preliminary question, the real question being whether the debtor was incorporated under the article of that statute dealing with banking corporations, and it wasn’t.

70. Capital Endowment Co. v. Kroeger, 86 F.2d 976 (6th Cir. 1936); In re Prudence Co., supra note 69.

71. See, e.g., Sims v. Fidelity Assur. Ass’n, 129 F.2d 442 (4th Cir. 1942), aff’d, 318 U.S. 608 (1943); Republic Underwriters v. Ford, 100 F.2d 511 (5th Cir. 1938); Kansas ex rel. Boynton v. Hayes, 62 F.2d 597 (10th Cir. 1932).
significance by the cases holding that the debtor's state did not classify it as one of the excluded corporations. Where, for example, a debtor is held to fall outside a state's classification of insurance corporation, the court's opinion may not refer to the state insurance commissioner at all. In such cases the insurance commissioner probably never took any action with respect to the debtor, since he is not likely to supervise a corporation unless it was organized under the insurance law. Nevertheless, the failure of the opinions to mention the absence of administrative action tends to indicate that this factor is not given as much weight as the statute under which the debtor is incorporated. The significance of administrative action or inaction is further diminished by the practice in some states of conferring jurisdiction on a particular official over more than one type of corporation. Thus, the fact that the New York Banking Law charged the department of banks with supervision of several businesses other than banks persuaded the court in the Prudence case not to attach great weight to the fact that the debtor was supervised by the department of banking. Consequently, while supervision of a debtor by, say, the state banking commissioner may be a sine qua non to a finding that the state has classified the debtor as a bank, the banking commissioner's supervision does not by itself insure such a finding.

Judicial characterizations have been least referred to. This does not, of course, necessarily mean that bankruptcy courts are indifferent to what the courts of a debtor's state of incorporation have had to say about corporations like the debtor. It may be that the courts of the relevant state have not had occasion to pass upon the question.

In sum, under the state classification test, an attorney consulted

72. See Hoile v. Unity Life Ins. Co., 136 F.2d 133 (4th Cir. 1943); Grand Lodge, Knights of Pythias v. McKee, 95 F.2d 474 (5th Cir. 1938); In re Grand Lodge A.O.U.W., 232 Fed. 199 (N.D. Cal. 1916).
73. See In re Bay Cities Guaranty Bldg.-Loan Ass'n, 48 F.2d 623 (S.D. Cal. 1931), where the question was whether a building and loan association was a banking corporation within the meaning of § 4. The court was impressed by the fact that, "Building and loan associations under the laws of California are not under the supervision of the banking department of the state . . . ; they are not inspected by the superintendent of banks; there is a separate supervising official who examines into their business affairs and who checks improper or unsafe transactions and who may cause them to be liquidated." Id. at 624.
75. Judicial constructions were referred to in Republic Underwriters v. Ford, 100 F.2d 511 (5th Cir. 1938); Grand Lodge, Knights of Pythias v. McKee, 95 F.2d 474 (5th Cir. 1938).
to determine the eligibility of a corporation for bankruptcy can make a rather accurate prediction by merely studying the legislation under which the debtor is incorporated; he can come quite close to certainty if administrative and judicial characterizations concur with that yielded by his study of the state statutes. Predictability alone may be sufficient to justify the state classification test. We will be in a better position to decide that after examining the other choices.

B. Characterization by Bankruptcy Courts.

If a bankruptcy court rejects the state classification test, it is faced with several problems that do not trouble the court which elects to abide by the characterization of the state of incorporation. It must, of course, provide its own definition of banking, insurance or building and loan association. Furthermore, if the debtor whose status is at issue is doing something different from what its charter empowers it to do, the court must decide whether to regard the debtor's powers or activities as controlling. We will consider first the simpler situation in which the debtor is merely exercising the powers conferred on it by its charter.

1. Activities Identical to Powers

a. Banking Corporations.

A corporation cannot be a banking corporation within the meaning of section 4 of the Bankruptcy Act unless it has the power to receive deposits. The leading statement on the subject appears in Gamble v. Daniel:

When Congress spoke of "banking corporations" it spoke as of 1910. It used the words in no technical nor special sense, but as they were then ordinarily understood. As (sic) that time, the ordinary conception of a bank was of a business which was based primarily on the receipt of deposits (general or special), which deposits were used by the bank for loans, discounts, buying and selling commercial paper, and other business purposes.

. . . The prime incentive in engaging in the business was the profit to be made, directly or indirectly, from use of deposits.

76. Compare Woolsey v. Security Trust Co., 74 F.2d 334 (5th Cir. 1934) (debtor had power to receive deposits and was held a bank), and Kansas ex rel. Boynton v. Hayes, 62 F.2d 597 (10th Cir. 1932) (debtor had power to receive deposits and was held a bank), with In re Prudence Co., 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935) (debtor lacked power to receive deposits and was held not a bank), and Gamble v. Daniel, 39 F.2d 447 (8th Cir.), appeal dismissed, 281 U.S. 705, cert. denied, 282 U.S. 848 (1930) (debtor lacked power to receive deposits and was held not a bank).

For a discussion of some problems in defining "deposits," see Note, Insured Deposits under the Federal Deposit Insurance Law, 42 Colum. L. Rev. 1030 (1942). These problems have not caused any difficulty in the bankruptcy cases.
Most of the then existing state legislation concerning banks had as its principal purpose the protection of such depositors. Much of the right to regulate banks was the public interest in protecting depositors. . . . Other businesses might and did, and still do, deal in commercial paper, make loans or borrow money without any one thinking of them as banks. When a business takes deposits and then does the above or related things, every one knows it is doing a banking business. . . . In short, while there may be other attributes which a bank may possess, yet a necessary one is the receipt of deposits which it may use in its business.77

While the power to receive deposits is undoubtedly an indispensable prerequisite to a finding of banking, it does not follow that any corporation with that power is a bank. What more is needed and the extent to which non-banking activities carried on in conjunction with the receipt of deposits will prevent a finding of banking are not clear.

Before building and loan associations were expressly excluded from bankruptcy, the question whether such organizations were banks was raised. Notwithstanding the fact that building and loan associations normally receive and repay deposits much like a savings bank, In re Bay Cities Guaranty Building-Loan Ass'n held that a building and loan association was not a bank.78 The court pointed out the debtor's lack of power to "have or carry upon its books . . . any demand, commercial or checking account or any credit to be withdrawn upon the presentation of any negotiable check or draft."79

In Clemons v. Liberty Savings & Real Estate Corp., the Fifth Circuit held that the debtor was not a bank even though it was empowered "to conduct a savings department . . . with the right to receive deposits not subject to check, and to pay interest thereon."80 The debtor's other powers included "the right to buy, sell, rent, lease, hire, develop, improve, own, control, and manage improved and unimproved real estate; to make contracts for constructing buildings; to buy, sell, and deal in stocks, bonds, promissory notes, and all kinds of choses in action; to advance or lend money to its stockholders or other persons, and to adopt a system of loans, advances, terms, and payments in installments in like manner, as to its interest charges and computations as may be done by building and loan associations. . . ."81 The opinion does not even intimate that these powers were incompatible with a finding of banking. On the con-

77. 39 F.2d at 450.
78. 48 F.2d 623 (S.D. Cal. 1931).
79. Id. at 624.
80. 61 F.2d 448, 450 (5th Cir. 1932).
81. Ibid.
trary, the Liberty Savings & Real Estate Corporation was not a bank because it lacked something essential to a finding of banking. The court said, "It is evident that appellee was organized to do a general savings and loan business, something less than either a bank or a building and loan association." 82 What was lacking was not stated, although the opinion seems to suggest that the case for a finding of banking would have been aided by the presence of power to permit depositors to make withdrawals by check. 83

Since both Clemons v. Liberty Savings & Real Estate Corp. and In re Bay Cities Guaranty Building-Loan Ass'n leaned in part on state classification as well as independent characterization, the significance of their conclusion that the power to receive deposits is not enough to sustain a holding of banking is somewhat lessened. Nevertheless, the two cases leave little doubt that something more is needed. Whether a corporation would be a bank if its depositors could draw checks upon it is not at all certain, but it is clear at least that no corporation whose depositors could not draw upon it by check has ever been held a bank within the meaning of the Bankruptcy Act.

While the decisions offer some information on the sine qua non of banking—there must be deposits and these probably must be subject to withdrawal by check—they give little help on the extent to which non-banking activities carried on in conjunction with a banking business will prevent a finding that the debtor is a bank. The failure of Clemons v. Liberty Savings & Real Estate Corp. to rest its holding that the debtor was not a bank in part on the ground that it had too many non-banking powers barely tends to indicate that, if the essential elements of banking are present, a corporation can have a good many auxiliary powers or activities and still be a bank. And it has been held that a corporation engaged in banking does not lose its exempt status by also carrying on the business of a trust company. 84 Beyond that the bankruptcy courts have been spared the problem of characterizing a corporation engaged in banking and other lines of endeavor.

Banking has been defined in many contexts outside of bank-

82. Ibid.
83. "A clear preponderance of the evidence shows that appellee did no banking business other than receiving savings accounts, for which they issued either pass books or certificates of deposit; that the depositors on the pass books were permitted to draw out portions of the deposit from time to time on checks. This it could not do under its charter.... If it occasionally engaged in banking transactions, those acts were ultra vires and could not operate to make it a bank within the meaning of the Bankruptcy Law...." Ibid.
84. Woolsey v. Security Trust Co., 74 F.2d 334 (5th Cir. 1934) ; Kansas ex rel. Boynton v. Hayes, 62 F.2d 597 (10th Cir. 1932).
ruptcy, and some of these definitions are occasionally referred to by bankruptcy courts. The usual caveat about importing definitions established in one area into an unrelated field is obviously applicable. That a department store may be deemed for purposes of state law to be unlawfully engaged in banking if it permits its customers to deposit money to be drawn upon for future purchases does not mean that such a store would be a banking corporation within the meaning of the Bankruptcy Act. Nor is a definition established for a term in a revenue statute much help in applying a bankruptcy statute. In any event, the general definitions customarily offered have little resolving power in a close bankruptcy case. One example should suffice:

Strictly speaking, the term bank implies a place for the deposit of money, as that is the most obvious purpose of such an institution. Originally the business of banking consisted only in receiving deposits, such as bullion, plate, and the like for safekeeping, until the depositor should see fit to draw it out for use, but the business . . . was extended, and bankers assumed to discount bills and notes and to loan money upon mortgage, bond, or other security, and at a still later period to issue notes of their own intended as a circulating currency and a medium of exchange. . . . Modern bankers frequently exercise any two or even all three of those functions, but it is still true that an institution prohibited from exercising any more than one of those functions is a bank in the strictest commercial sense.

b. Insurance Corporations.

Whereas the banking corporation cases occasionally postulate a definition of banking and then see whether the debtor fits, the insurance corporation cases typically avoid any attempt at a general definition of insurance. The decisions which characterize an insurance corporation independently of state classification can best be discussed by considering the approaches they employ and how they deal with certain activities.

One court has tackled the problem by asking: Would most states have classified this corporation as an insurance corporation at the time the exclusion of insurance corporations was adopted?

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87. See Sims v. Fidelity Assur. Ass'n, 129 F.2d 442, 451 (4th Cir. 1942), aff'd, 318 U.S. 608 (1943), in which the debtor had been selling annuities and had, shortly before it attempted bankruptcy reorganization, begun selling life insurance; the court pointed out that the business of the debtor was such that it "would have been classed as an insurance company under the laws of the majority of the states as they existed in 1910. . . . At that time, the laws
To the extent that this inquiry is premised on the common judicial assumption that Congress' primary purpose was to leave liquidation of an insurance corporation to the same authority that regulated it during its life, the inquiry is only a variant of the state classification test. Such an inquiry might be justified, however, without reference to any assumption about legislative intent, on the theory that Congress' understanding in 1910 of the meaning of insurance must be discovered in contemporaneous legal usage, and the usage of state legislators, officials and judges is the best available evidence of that. Even on this theory, though, the inquiry is open to the objection that it freezes the meaning of the Bankruptcy Act as of 1910 regardless of changes in business conditions and regulatory practices. If the actions of the states are to be looked to for help in fashioning a bankruptcy definition of insurance corporation, it would be better to find out what they are doing currently.

The best reasoned approach to the problem is probably still *In re Supreme Lodge of the Masons Annuity*, now presumably overruled. The Supreme Lodge had been issuing certificates "in nearly all the forms of modern life and accident insurance, to persons selected and chosen under the usual standards of insurance regulations, with premiums calculated and fixed by insurance rules." The court said:

No reasons for making these exceptions were assigned by the committees of Congress, but they may be surmised to lie in the public or quasi public nature of the business, involving other interests than those of creditors, in the desirability of unarrested operation, the completeness of state regulation, including provisions for insolvency, and the inappropriateness of the bankruptcy machinery to their affairs. . . . The affairs of an embarrassed or insolvent insurance company often require much technical skill and judgment and time for their adjustment and a carrying forward of the business, to prevent lapses and to permit reinsurance to simplify them. And considering the variety of insurance obligations assumed and the various statuses thereof, a chief practical difficulty is the ascertainment of who are really to be considered creditors and in what amounts, often requiring much time and elaborate accounting for its solution. Under such
circumstances even the election of a trustee in bankruptcy would
be difficult, and a creditors' meeting could hardly prosecute any
business, owing to conflicting interests of the various classes of
claims.

All these reasons apply with full force to a modern fraternal ben-
et insurance organization, and argue the inclusion of corpora-
tions doing such business within the broad terms used by
Congress.90

The court thus considered the drawbacks of bankruptcy liquidation
for insurance corporations and soundly concluded that since those
same drawbacks would be applicable to the debtor it should be held
an insurance corporation. Some of the disadvantages mentioned in
the opinion undoubtedly ended with the adoption of comprehensive
procedures for corporate reorganization, but those that do remain
would still be as applicable to the Supreme Lodge of the Masons
Annuity as to any conceded insurance corporation.

The status of fraternal benevolent orders under the insurance
corporation exclusion has come before bankruptcy courts on a num-
ber of occasions. In re Supreme Lodge of the Masons Annuity is
very nearly alone in regarding such an organization as an insurance
corporation.91 The powers and activities of such organizations may,
of course, vary substantially from one fraternal order to another.
Contrast, for example, the operations of the Supreme Lodge of the
Masons Annuity with this description of the debtor in In re Grand
Lodge A.O.U.W.:

The bankrupt is not, in my opinion, an insurance corporation
within the meaning of the bankrupt law. As a matter of fact it
did not insure. Its only obligation was to collect, from such of
its members as were willing to contribute, funds with which, if
and when collected, it would pay certain amounts to the benefi-
ciaries of deceased members. There was not other obligation
on the bankrupt than that of a collector. There was no obli-

90. Id. at 184.
91. Square holdings on the question whether a fraternal order is an
insurance corporation are rare because involuntary proceedings must be
dismissed if the debtor is either an insurance corporation or is not moneyed,
business or commercial. Thus, In re Supreme Lodge of the Masons Annuity,
286 Fed. 180, 188 (N.D. Ga. 1923), concludes: "According to its charter,
therefore, [the debtor] is a benevolent, and not a business or moneyed,
corporation. According to its principal object and business at the time of its failure,
it was an insurance corporation. Under either view of it, it is not subject to
involuntary bankruptcy." Notwithstanding this kind of hedging, it is rather
clear that almost all courts which have considered whether a fraternal
benevolent order is eligible for bankruptcy have viewed such organizations as
something other than insurance corporations. See, e.g., Holle v. Unity Life
Ins. Co., 136 F.2d 133 (4th Cir. 1943). Additional authorities on this subject
are collected in Annot., 148 A.L.R. 714 (1944).
gation on the part of any of the members to pay unless they were willing to do so . . . . This is not insurance.92

The variety of fraternal orders should make the approach exemplified by In re Supreme Lodge of the Masons Annuity extremely attractive and yet it has been stated that,

[C]orporations of this character had been in existence very many years at the time of the enactment of the bankrupt law, and of the provision excepting insurance corporations from its benefits, and were technically known as fraternal benevolent societies or associations, and not as insurance corporations. If Congress intended to place them among the excepted corporations, there was a well-known name by which they could have been designated.93

The answer, of course, is that Congress did not wish to except all fraternal benefit societies from bankruptcy; it wished to exclude only those which were insurance corporations.

Since fraternal benefit societies normally engage in a number of activities in addition to providing death and disability benefits, we might expect the cases involving those societies to consider whether non-insurance functions carried on in conjunction with an insurance business will prevent a debtor from being held an insurance corporation, but the problem is never approached in these terms. Nevertheless, it may be that the courts which have held such societies not to be insurance corporations were influenced to some extent by their non-insurance activities. If the question had been expressly put to the court that decided In re Supreme Lodge of the Masons Annuity, it might well have said that no amount of auxiliary activity could remove the disadvantages of bankruptcy administration for this debtor, and it should, therefore, be deemed an insurance corporation. The question was expressly considered in In re New York Title & Mortgage Co.,94 a case involving a guaranteed mortgage company, but gave little difficulty because the court characterized the overwhelming proportion of the debtor's business as insurance. In sum, the insurance cases on this problem provide no more information than the banking cases.

Another business that has presented the problem of insurance corporation or not on several occasions is the guaranteed mortgage company. Only two cases essay an independent characterization of such an enterprise, and they reach opposite conclusions,95 which

93. Id. at 200.
94. 9 F. Supp. 319 (N.D. N.Y. 1934).
95. In re Prudence Co., 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935), indicated that independent characterization of the guaranteed mortgage company before it would accord with the state's classification of the
may help to explain the enthusiasm for the state classification test manifested by the circuit in which they arose.

The last approach to be found in the cases is the inevitable reliance on insurance decisions in other contexts. For example,

[T]he record puts this case in close analogy with U. S. v. Home Title Insurance Company . . . in which the Supreme Court held that the company was an insurance corporation within the meaning of the tax law and that the tax law used the term "insurance company" in its ordinary sense. So it must be held here.

c. Building and Loan Associations.

Few cases have been concerned with the meaning of building and loan association since that type of corporation was added to the list of section 4 exclusions twenty-five years ago. None gives much aid in defining building and loan association independently of state classification. Clemen v. Liberty Savings & Real Estate Corporation\(^9\) presented a fact situation that offered an opportunity for helpful analysis, but counsel apparently contended that the debtor was a building and loan association for the first time in argument before the Court of Appeals, which dismissed the contention briefly, concluding that, "It is evident that appellee was organized to do a general savings and loan business, something less than either a bank or a building and loan association."\(^8\)

This conclusion is curious because "savings and loan association" is generally regarded as a synonym for "building and loan association."\(^9\) The court was apparently using the phrase, "savings debtor as something other than an insurance corporation. In re New York Title & Mortgage Co., 9 F. Supp. 319 (N.D. N.Y. 1934), held the business of selling guaranteed mortgages to be insurance. To the extent that In re New York Title & Mortgage Co. relies on independent characterization, it is presumably overruled by In re Union Guarantee & Mortgage Co., 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935), in which a guaranteed mortgage company was held an insurance corporation solely on the basis of state classification. Union Guarantee & Mortgage was followed in In re National Mortgage Corp., 17 F. Supp. 54 (D. N.J. 1935). To the extent that independent characterization resulted in a finding of insurance in In re New York Title & Mortgage Co., it is presumably overruled by the Prudence case's indication that the guaranteed mortgage business cannot be characterized as insurance.

96. In re New York Title & Mortgage Co., supra note 95, at 325.
97. 61 F.2d 448 (5th Cir. 1932).
98. Id. at 450.
99. See, e.g., Cal. Fin. Code Ann. § 5025 (West Supp. 1956) ("Whenever in the laws of this State the words 'Building and Loan Association Law,' 'Division of Building and Loan,' 'Building and Loan Commissioner,' 'Building and Loan Inspection Fund,' 'building and loan association,' and 'building and loan business' appear, they shall mean 'Savings and Loan Association Law,' 'Division of Savings and Loan,' 'Savings and Loan Commissioner,' 'Savings and Loan Inspection Fund,' 'savings and loan association,' and 'savings and loan business,' respectively.") ; Russell, Savings and Loan Associations e. 3 (1956).
and loan business," not in any technical sense, but merely to refer to some kind of limbo into which it would consign corporations which receive deposits but which do not meet the qualifications of a bank or building and loan association.\(^{100}\) We are not told, though, nor are sufficient facts set forth to infer, what essential characteristic of a building and loan association was missing from the debtor's makeup.

In the absence of any helpful case authority, it may be worthwhile to speculate on what characteristics are likely to be regarded as essential to a building and loan association. The history of building and loan associations, now more commonly known as savings and loan associations, indicates that these terms have always been used to refer to a corporation that is both a savings and home financing institution.\(^{101}\) The form of the savings contract may vary — the saver is sometimes referred to as a shareholder; his funds may be available on demand or only on notice — but in essence the relationship is similar to that of a depositor to a savings bank.\(^{102}\) The funds on deposit with a building and loan association are used primarily for first mortgage loans on private homes.\(^{103}\) Perhaps a corporation would be held a building and loan association if home mortgage loans made up less than a substantial majority of its portfolio, but probably not unless home financing was at least the company's predominant investment outlet.

Several other characteristics are quite common among corporations calling themselves building and loan associations, but do not seem indispensable. While most building and loan associations are mutual organizations,\(^{104}\) a corporation engaging in the requisite savings and investment activities would probably be held a building and loan association even though it issued capital stock.\(^{105}\) Similarly, the fact that building and loan associations typically lend only to their members would not prevent a corporation pursuing a different practice from being held a building and loan association. This dis-
tinction may have been impoi-tant once, but it probably persists only because of certain tax advantages accruing to associations which so limit their lending, and, in fact, is now only a meaningless for-
mality. For example, the charters of federal savings and loan asso-
ciations customarily provide that all borrowers automatically be-
come members, and some state associations have similar provi-
sions. Another common but not indispensable characteristic is
local operation; because of the nature of their lending activities,
building and loan associations can apparently police their securi-
ties more efficiently if they operate only within the community in
which they are located. Nevertheless, it seems unlikely that a
 corporation would cease to be a building and loan association by
doing business in a wider area.

2. Activities Differing from Powers.

If the activities of a corporation differ in some respect from the
powers conferred by its charter, a bankruptcy court undertaking to
determine, independently of state classification, whether that corpo-
ratio is excluded from bankruptcy may have to decide whether the
corporation's powers or activities, or some combination of these,
should control. Gamble v. Daniel presented one aspect of this
problem. There the debtor's activities apparently would have classi-
ified it as a bank, but it lacked an essential banking power. The
court held that corporate powers should control, saying:

First, it would be strange if Congress would permit the classifi-
cation under section 4 (and, therefore, the application of the
entire Act) to be controlled by the exercise of ultra vires powers
by a corporation. Second, a comparison of the Amendment of
1910 (the present section) with similar sections in previous
bankruptcy legislation shows a deliberate departure from the

106. For example, Int. Rev. Code of 1954, § 591 provides that, "In the
case of mutual savings banks, cooperative banks, and domestic building and
loan associations, there shall be allowed as deductions in computing taxable
income amounts paid to, or credited to the accounts of, depositors or holders
of accounts as dividends on their deposits or withdrawable accounts, if such
amounts paid or credited are withdrawable on demand subject only to cus-
tomary notice of intention to withdraw." "Domestic building and loan asso-
ciation" is defined by Int. Rev. Code of 1954, § 7701(19) as "a domestic
building and loan association, a domestic savings and loan association, and a
Federal savings and loan association, substantially all the business of which
is confined to making loans to members." (Italics supplied.)

107. See Russell, op. cit. supra note 99, c. 21 and authorities there cited.


109. 39 F.2d 447 (8th Cir.), appeal dismissed, 281 U.S. 705, cert. denied,
282 U.S. 848 (1930).
"business carried on" criterion. Third, the reason for the amendment of section 4, in 1910 was stated by its author to be to escape the confusion which had arisen in decisions as to construction and application of the words "engaged principally" in the 1898 act. . . . It was to escape this confusion and uncertainty that the amendment "adopted the scientific way of declaring a class and then stating exceptions to the class." Cong. Rec. vol. 45 p. 2275. We have no doubt that when Congress used the words "banking corporations" it meant corporations which were authorized by the laws of their creation to do a banking business.110

Is it true, as the court argues in its second and third points, that the legislative history of section 4 compels the conclusion that Congress intended a corporation's powers, rather than its activities, to control? That section 4 was once phrased in terms of the business principally engaged in, and is no longer so phrased, is indisputable. So is the fact that the legislative history shows that there was concern over the confusion caused by the language used prior to 1910. But it is not at all clear that Congress' remedy was to make the powers of a corporation the governing criterion. As we have seen, a number of courts believe that Congress' answer was to make state classification controlling. The legislative history reveals that the author's remedy for the confusion was not to make powers the test—nothing was said about corporate powers—but to abandon the enumeration of corporations subject to bankruptcy and adopt "the scientific way" of declaring that all corporations are subject to bankruptcy, with certain specified exceptions.111

The court's first point is hardly persuasive when we remember that ultra vires action by a corporation often has legal consequences. The question to be answered in Gamble v. Daniel was whether ultra vires activity should be sufficient to bring a corporation within one

110. Id. at 450.
111. This explanation was given on the floor of the House: "My next amendment undertakes to make a scientific classification of those who may be put into involuntary bankruptcy. As the bill was originally drawn, an effort was made to name in detail those individuals who were amenable to the law. Instead of stating the rule and then naming the exception, they simply reversed it, so that I provide that any 'moneyed, business, or commercial corporations, excepting municipal, railroad, insurance, or banking corporations, may be put into involuntary bankruptcy.' "The old law provided that 'a corporation engaged principally in manufacturing, trading, printing, publishing, mining, or mercantile pursuits' could be put in bankruptcy, and the question then came up in the court as to what was meant by the word 'principally,' and you have some very strange decisions. . . . So, instead of having them enumerated, I have adopted the scientific way of declaring a class and then stating the exceptions to the class." 45 Cong. Rec. 2275 (1910) ; see H.R. Rep. No. 511, Ser. No. 5591, 61st Cong., 2d Sess. 4 (1910), fully quoted in Sen. Rep. No. 691, Ser. No. 5584, 61st Cong., 2d Sess. 4 (1910).
of the section 4 exclusions, and the court's first point merely assumes the answer. We submit that it assumes the wrong answer. Whatever reasons Congress may have had for deeming bankruptcy inappropriate for the corporations excluded by section 4, surely Congress' primary concern was not for the excluded corporations themselves, but for those dealing with them, those who buy insurance and those who deposit funds with banks and building and loan associations. And whether or not there are such people who will be adversely affected by bankruptcy administration depends not on what the corporation is empowered to do, but on what it is actually doing. Consequently, a bankruptcy court should not refuse to hold a corporation a bank merely because its banking activity is ultra vires.

No case has presented the converse of the problem presented by Gamble v. Daniel; that is, what result when a debtor is empowered to engage in, say, banking, but instead of exercising that power is engaged in ultra vires activity which would make it subject to bankruptcy? While this question was not posed by Gamble v. Daniel, some of the court's language would resolve this question too by reference to the debtor's powers rather than activities. In addition to the discussion already quoted, the court says, "The most natural meaning of the words is: A corporation empowered to do a banking business." Our criticism of the reference to powers in the Gamble v. Daniel situation is also applicable here. That is to say, if a corporation empowered to do a banking business is not engaged in banking, the interests Congress sought to protect by excluding banks from bankruptcy need no protection, and the debtor should be held subject to the Bankruptcy Act.

The need to choose between powers and activities is not confined to cases in which a corporation exercises less than all of its charter powers. The Eighth Circuit noted half the problem in Gamble v. Daniel: "Whether a corporation empowered to do a banking business and also other character of business, but actually doing no banking business is included, we need not determine, as that situation is not present here." The court didn't bother to raise the question of the corporation empowered to do banking and other business, but which does only banking. While there are no holdings on the latter question, such a corporation would probably be exempt from bankruptcy. Nor is there much authority on the question

112. 39 F.2d at 450.
113. Ibid.
raised and left unanswered in *Gamble v. Daniel. In re Supreme Lodge of the Masons Annuity* seems to support an activities test:

[A] corporation often has power to do many things. . . . So many corporations are chartered both as banks and trust companies. Surely whether such a one was actually doing a banking business could be inquired into, if it was sought to be put in bankruptcy. . . . The true rule is that the charter is first to be looked to in classifying the corporation, but that the business really done . . . may also be looked to either to explain or rebut the inferences from the charter powers.\(^{114}\)

A number of cases, without attempting to discriminate among the various ways in which the powers-activities choice may be presented, state that powers control.\(^{115}\) Whether these statements were intended to apply to anything more than the ultra vires situation is not clear. In any event, there is no more reason to pass over activities in favor of powers in a multiple powers case than there is in an ultra vires case.

In sum, regardless of whether a bankruptcy court must choose between powers and activities because a debtor is engaged in ultra vires activity or because a debtor has more powers than it uses, if the corporation is to be characterized independently of state classification, that characterization should refer to the debtor's activities rather than its powers.\(^{116}\)

\(^{114}\) 286 Fed. 180, 183 (N.D. Ga. 1923). The district court which decided *In re Fidelity Assur. Ass'n*, 42 F.Supp. 973 (S.D. W.Va. 1941), thought the debtor was empowered to engage in insurance and other business but was carrying on only the other business. It disposed of the question this way: "In deciding whether a corporation is to be classified as an insurance or banking corporation or a building and loan association within the meaning of the Bankruptcy Act, the court must first examine the provisions of its corporate charter. If the charter authorizes the company to engage in business in any of the excepted fields, and if the company in fact engages principally in a business which lies within that field, such a corporation must be treated as one excluded from the benefits of Chapter X. However, if its charter authorizes the corporation to engage in activities outside the excepted fields, and if all the business actually done by the corporation is outside those fields, then it must be treated as not being within any of the excluded classes. By this test debtor must be classified as a corporation which is not an insurance corporation within the meaning of . . . the Bankruptcy Act." *Id* at 982. The Court of Appeals disagreed with the district court's view of the facts and the law and reversed. 129 F.2d 442 (4th Cir. 1942), *aff'd*, 318 U.S. 608 (1943).

\(^{115}\) E.g., *In re Union Guarantee & Mortgage Co.*, 75 F.2d 984, 985 (2d Cir.), *cert. denied*, 296 U.S. 594 (1935); *Clemens v. Liberty Savings & Real Estate Corp.*, 61 F.2d 448, 450 (5th Cir. 1932).

\(^{116}\) When an involuntary petition is filed against a corporation that has been dissolved, the debtor's activities at the time the petition is filed obviously should not control. Since a dissolved corporation will normally be engaged solely in winding up its affairs, permitting its activities at the time the petition is filed to control would mean that all of the excepted corporations would become eligible for bankruptcy as soon as they ceased doing business. While this might produce desirable results, it hardly accords with Congress' purpose. See note 36 *supra*. The solution would seem to be a reference to
C. Is State Classification Preferable to Independent Characterization by Bankruptcy Courts?

A court often decides difficult questions of statutory interpretation in the light of the policy underlying the statute, but the policy underlying the exclusion from bankruptcy of a few types of corporation is not clear. If we accept the common judicial rationale that Congress' purpose was to leave the insolvency administration of strictly regulated enterprises to the state which regulates them, the sound approach would be to resolve all close cases in favor of exclusion from bankruptcy if the corporation is strictly regulated, and against exclusion in the absence of strict regulation. Probably most close cases would then be resolved in favor of exclusion. On the other hand, since the exclusions were originally adopted, Congress has expanded the Bankruptcy Act to provide for rehabilitation of stricken corporations. If this machinery would be helpful to a particular debtor, perhaps the approach should be to narrow the definition of the exclusion at issue and thus make the beneficence of reorganization available to as many debtors as possible.

The absence of a clear policy to be effectuated by the exclusions means that the choice between state classification and independent characterization must be made on some other basis. We have seen that the state classification test offers predictability and that predictability is important in this area. Arguing against state classification is the minor disadvantage that it fails to yield uniform treatment of corporations that are essentially the same if their home states classify them differently. This would not, however, be the only instance in which the Bankruptcy Act permits similarly situated debtors to be treated differently because of applicable state law, and, of course, such corporations are treated differently all through their lives because of differences in the laws of the states which govern them. This additional difference in treatment hardly rises to the level of injustice. More serious is the possibility, especially likely with respect to insurance corporations, that the state of incorporation is not the state with the greatest interest in deciding how an enterprise should be liquidated or rehabilitated. If a company does most of its business outside of its state of incorporation, the arbitrary nature of a reference to that state's classification becomes most patent and abdication by a bankruptcy court to that the debtor's activities immediately before dissolution or at the time the act of bankruptcy was committed. Cf. Bankruptcy Act § 4b: "The status of an alleged bankrupt as a wage earner or farmer shall be determined as of the time of the commission of the act of bankruptcy."

117. See text following note 63 supra.
state's decision most questionable. Even in such a case, though, the state of incorporation is not entirely without interest in what becomes of the beleaguered corporation. Furthermore, a court accepting the state classification test still retains the residual power to ignore a state classification which it regards as unreasonable.\footnote{119}

The disadvantages of the state classification test do not attend independent characterization by bankruptcy courts, but neither does the advantage — predictability — for the attempts at independent characterization have not been very enlightening. We know little more about banks than that there can be no banking corporation in the absence of power to receive deposits.\footnote{120} Fraternal benefit societies are generally not treated as insurance corporations, but beyond that the meaning of insurance corporation for bankruptcy purposes remains unclear. We can only guess about how building and loan association will be defined. And, finally, the powers-activities problem has not been satisfactorily resolved.

Given the unsatisfactory results of independent characterization, the attraction of the state classification test is readily understandable. Nor should it surprise that the attraction appears to be strongest in the insurance cases, where the courts have had most difficulty with an independent definition, and weakest in the banking cases, where independent characterization has been least troublesome.\footnote{121}

\begin{footnotes}
118. See, e.g., Bankruptcy Act § 6, 30 Stat. 548 (1898), as amended, 11 U.S.C. § 24 (1952) ("This title shall not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States or by the State laws in force at the time of the filing of the petition in the State wherein they have had their domicile for the six months immediately preceding the filing of the petition. . . .") ; Bankruptcy Act § 70(e), 30 Stat. 565 (1898), as amended, 11 U.S.C. § 110(e) (1952) ("(1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this title which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this title, shall be null and void as against the trustee of such debtor.").

119. See Sims v. Fidelity Assur. Ass’n, 129 F.2d 442, 451 (4th Cir. 1942), aff’d, 318 U.S. 608 (1943): “These authorities establish the rule that in determining whether a corporate debtor is a member of the excepted classes, the provisions of the state law must be given predominating influence. This is not to say that the classification of a state statute must be followed literally in every instance without any regard whatsoever to the real activity of the corporate body.”

120. The emphasis on deposits cannot be justified in terms of any policy objective of the Bankruptcy Act, but may be explicable, like the attraction of the state classification test, in terms of predictability and judicial appreciation of a standard that is easy to apply.

\end{footnotes}
In fact, whatever the powers or activities of a debtor, it is hard to conceive of a bankruptcy court departing from state classification when the issue is insurance corporation or not,\(^{122}\) whereas, whatever the classification of the state of incorporation, it seems unlikely that a corporation will be held a bank if it lacks the power to receive deposits.\(^{123}\) However, a caveat on the banking cases is in order: while they all reflect great reliance on the deposit criterion, they all contain, too, at least a token reference to state classification, and the tendency of the courts to cite banking, building and loan association\(^{124}\) and insurance decisions indiscriminately when support for

\(^{122}\) A review of the current state of the authorities in the circuits reveals the following: The Second Circuit unequivocally espoused state classification in *In re* Union Guarantee & Mortgage Co., supra note 121, and while it retreated somewhat from that strong commitment in *In re* Prudence Co., 79 F.2d 77 (2d Cir.), cert. denied, 296 U.S. 646 (1935), it did so primarily with respect to banks and not insurance corporations. An early Third Circuit decision, *In re* Order of Sparta, 242 Fed. 235 (3d Cir. 1917), relied principally on independent characterization, but the court may not have needed to decide whether the debtor was an insurance corporation in order to decide the case before it. In any event, a later decision by one of the district courts in that circuit relied entirely on state classification without even citing the Sparta case. *In re* Nat'l Mortgage Corp., 17 F. Supp. 54 (D. N.J. 1935). The Fourth Circuit relied primarily on state classification in Sims v. Fidelity Assur. Ass'n, supra note 121, and reaffirmed that view in *Holle v. Unity Life Ins. Co.*, 136 F.2d 133 (4th Cir. 1943). The Fifth Circuit relied almost entirely on state classification in Grand Lodge, Knights of Pythias v. McKee, supra note 121, and reaffirmed that view in *Republic Underwriters v. Ford*, 100 F.2d 51 (5th Cir. 1938). Giving the problem very brief treatment, the Sixth Circuit seems to have relied on both state classification and independent characterization in *Capital Endowment Co. v. Kroeger*, 86 F.2d 976 (6th Cir. 1936). There are no decisions dealing with the definition of the total exclusions of section 4 in the First, Seventh and District of Columbia Circuits, and the Eighth and Tenth Circuits have only faced the problem in the banking context, where independent characterization is more significant. The Ninth Circuit has not had to define an insurance corporation, but it relied almost entirely on state classification in a building and loan association case, *Security Bldg. & Loan Ass'n v. Spurlock*, 65 F.2d 768 (9th Cir.), cert. denied, 290 U.S. 678 (1933). A later decision of one of the district courts in that circuit, however, relies on both state classification and independent characterization to define a building and loan association. *In re* Pacific States Sav. & Loan Co., 27 F. Supp. 1009 (S.D. Cal. 1939).

\(^{123}\) Since no banking decision has considered its independent characterization to be at variance with a state classification, the statement in the text obviously cannot be supported by any holdings. Nevertheless, each of the cases which refused to hold the corporation before it a bank stated without qualification or clearly implied that the power to receive deposits is a sine qua non of banking. *In re* Prudence Co., supra note 122; *Clemons v. Liberty Savings & Real Estate Corp.*, 61 F.2d 448, 450 (5th Cir. 1932); *Gamble v. Daniel*, 39 F.2d 447, 450 (6th Cir.), appeal dismissed, 281 U.S. 705, cert. denied, 282 U.S. 848 (1930); *In re* Bay Cities Guaranty Bldg.-Loan Ass'n, 49 F.2d 623, 624 (S.D. Cal. 1931).

\(^{124}\) The state classification test seems to be favored in building and loan association cases, but the authorities are too sparse to permit a definitive judgment. *Security Bldg. & Loan Ass'n v. Spurlock*, 65 F.2d 768 (9th Cir.), cert. denied, 290 U.S. 678 (1933), clearly favors state classification. *Clemons v. Liberty Savings & Real Estate Corp.*, supra note 123, favors independent characterization, but has been cited by a later decision in the Fifth Circuit in
the state classification test is desired may eventually cause state classification to become the controlling principle for banking cases.\textsuperscript{125}

In sum, the state classification test attains a desirable objective—predictability\textsuperscript{126}—and while it defines by essentially arbitrary means, it sacrifices relatively little of other attainable goals, for if bankruptcy courts reach unsound or confusing results when they characterize independently of state classification, arbitrary treatment is as likely to result from this method as from state classification. Nevertheless, that the section 4 exclusions must be defined by essentially arbitrary means raises the question of the wisdom of those exclusions. To that question we now turn.

III. Should Banking and Insurance Corporations and Building and Loan Associations Be Excluded From Bankruptcy?

The case for abandoning an exclusion from bankruptcy ultimately must rest on a showing that insolvency of the excluded corporation can be better dealt with under the Bankruptcy Act than under existing arrangements. In considering the bankruptcy alternative to the existing arrangements for insolvent banks, insurance corporations and building and loan associations, we need not, of course, regard bankruptcy as did the members of Congress in 1910, support of state classification. See Grand Lodge, Knights of Pythias v. McKee, 95 F.2d 474, 476 (5th Cir. 1938). Capital Endowment v. Kroeger, 86 F.2d 976 (6th Cir. 1936), and In re Pacific States Sav. & Loan Co., 27 F. Supp. 1009 (S.D. Cal. 1939), seem to rely on both state classification and independent characterization.

\textsuperscript{125} This caveat would appear to be especially appropriate with respect to the Fourth Circuit which has strongly committed itself to state classification in insurance cases and has not yet been called upon to define a banking corporation. However, the Second Circuit, after taking the strongest possible position in favor of state classification in In re Union Guarantee & Mortgage Co., 75 F.2d 984 (2d Cir.), cert. denied, 296 U.S. 594 (1935), rested its holding that the Prudence Co. was not a bank in part on the fact that, "[T]he debtor does not possess the power to receive deposits, which is generally recognized as the essential characteristic of a banking business." In re Prudence Co., 79 F.2d 77, 79 (2d Cir.), cert. denied, 296 U.S. 646 (1935). Compare Republic Underwriters v. Ford, 100 F.2d 511 (5th Cir 1938), and Grand Lodge, Knights of Pythias v. McKee, supra note 124, with Woolsey v. Security Trust Co., 74 F.2d 334 (5th Cir. 1934), and Clemons v. Liberty Savings & Real Estate Corp., 61 F.2d 448 (5th Cir. 1932).

\textsuperscript{126} The state classification test also avoids the theoretical danger of a corporation being left without any statutory way to liquidate or rehabilitate. If the federal courts are characterizing independently of state classification, it is conceivable that a debtor will be classified by a bankruptcy court as, for example, an insurance corporation, but be regarded by its state of incorporation as something other than an insurance corporation. The debtor will then be foreclosed both from bankruptcy and from the state of incorporation's procedures for insolvent insurance corporations. However, this will probably never happen, and even if it does, devices such as the assignment for the benefit of creditors and the equity receivership are still available.
as primarily a liquidation device. Not only does the Bankruptcy Act now contain two different procedures for rehabilitating corporations in general, but it also contains chapters setting up special procedures for particular corporations which cannot soundly be treated under the more general chapters. Nor is sole control over the outcome of the proceeding always in the hands of the bankruptcy court; in some situations the advice or consent of federal or state administrative officials may play a crucial part. Today, then, the alternatives to state control over the liquidation or rehabilitation of the excluded corporations are numerous. These corporations could be made eligible for both liquidation and rehabilitation under the general provisions of the Bankruptcy Act; their eligibility could be limited to the general reorganization provisions; or separate chapters could be enacted to deal specifically with the special problems of each of them. Any of these courses could be coupled with a requirement that the advice or consent of the administrators charged with the supervision of these corporations during their lives be obtained before final disposition. In short, anything that can be done outside of the Bankruptcy Act to deal with insolvency of the excluded corporations can probably now be done under the Bankruptcy Act.

Is there anything that can be done under the Bankruptcy Act that cannot be done outside of it? Since the Bankruptcy Act has grown from a statute dealing with liquidation into what is really and agglomeration of statutes dealing with insolvency in many ways, this question really asks whether anything can be achieved by federal legislation that the states cannot achieve themselves. It does not require a comprehensive review of the provisions and adminis-

128. See note 2 supra.
§ 577. Approval of plan for public utility.
In case a debtor is a public-utility corporation, subject to the jurisdiction of a commission having regulatory jurisdiction over the debtor, a plan shall not be approved,... until—
(1) it shall have been submitted to each such commission;
(2) an opportunity shall have been afforded each such commission to suggest amendments or offer objections to the plan; and
(3) the judge shall have considered such amendments or objections at a hearing at which such commission may be heard.
§ 578. Same; intrastate public utility.
In case a debtor is a public-utility corporation, wholly intrastate, subject to the jurisdiction of a State commission having regulatory jurisdiction over such debtor, a plan shall not be approved ... unless such State commission shall have first certified its approval of such plan as to the public interest therein and the fairness thereof. . . .
tration of state legislation dealing with the liquidation and rehabilitation of banks, insurance companies and building and loan associations to see that the limitations of our federal system do make it extremely difficult for individual states to solve all of the problems posed by the financial failure of the excluded corporations.

A. Insurance Corporations.

The difficulties with respect to insurance corporations are sufficiently well catalogued in the Commissioners' Prefatory Note to the Uniform Insurers Liquidation Act to justify quotation at length.

[Insurance company assets take the form, for the most part, of special deposits required by state law, balances in the hands of insurance agents, policy premiums due but unpaid, and investments of reserve funds. The greater number of these assets naturally have their situs in the state of domicile of the company, but a substantial portion is normally scattered over the entire territory within which the company carries on its business. This is necessarily true of the special deposits required by the laws of non-domiciliary states and the balances in the hands of nonresident agents. On the other side of the balance sheet the liabilities of insurance companies, consisting primarily of policy obligations, are also distributed over the several states in which the companies do business. This wide distribution of assets and liabilities creates a formidable array of problems when liquidation, rehabilitation or reorganization proceedings becomes necessary for an insurer which has drifted into financial difficulties. The equitable and expeditious solution of these problems is rendered the more difficult by wide differences in the provisions of the statutes of the several states regarding such matters as special deposits, preferred claims, securities, set-off, and the administrative and judicial procedures to be followed. . . .]

Specific features of insurer delinquency proceedings causing the greatest embarrassment are the following:

1. In some states the statutes provide that the Insurance Commissioner shall serve as receiver; in others, the courts appoint receivers as their discretion dictates. In the latter states experience has shown that efficient administration is less likely to ensue.

2. Very frequently the domiciliary receivers, whether or not deemed statutory successors to the defunct companies, have but little authority in nondomiciliary states, and in some states they receive no recognition whatsoever. As a consequence, company assets located outside the home states are likely to be dissipated, and, unless ancillary proceedings are started, debtors living in such states are all too frequently able to avoid meeting their just obligations.

3. There is much confusion in the law concerning the title and right to possession of the property of a defunct nonresident insurance company. In some states the title and the right to pos-
session are recognized as reposing in the domiciliary receiver; in others, they are in the ancillary receiver. The absence of clear definition of the law as to these matters hampers effective administration.

4. Serious inconvenience in making proof of claims is experienced by creditors who are so unfortunate as to live outside the state of the defunct insurer’s domicile. It frequently happens that ancillary receivership proceedings are not commenced, or, if commenced, the property in the hands of the ancillary receiver is insufficient to meet the obligations of local creditors. As a consequence, such creditors are forced to bear the expense, annoyance, and hardship of proceeding in the courts of the domicile of the insurance company to prove their claims. Statutory provisions which would make possible the proof of claims in the states of creditors’ residence would be a great boon.

5. Another difficulty arises from the diversity of state laws concerning preferences, such as wage claims, compensation claims, tax claims and the like. Administration would be simplified and greater equity would be obtained if the laws of a single state, preferably the state of domicile of the insurance company, were made to govern all such preferences.

6. Finally, inequity often results from the fact that creditors in nondomiciliary states may, if they are sufficiently well informed and diligent, obtain preferences for themselves by commencing attachment or similar proceedings against such property as may be found in their respective states. Such proceedings can easily be commenced by properly informed creditors before ancillary proceedings are started, and as a result other less well-informed creditors suffer accordingly. There is no just reason for permitting such preferences to prevail.\textsuperscript{130}

While somewhat overstated,\textsuperscript{131} the Commissioners’ summary of

\textsuperscript{130} 9A Uniform Laws Ann. 148. The difficulties of liquidating and rehabilitating interstate insurance companies are also ably discussed in two addresses. See Vance, Interstate Aspects of the Liquidation of Insolvent Insurance Corporations, 6 Ass’n of Life Ins. Counsel 343 (1935); Van Schaick, Interstate Liquidations — A National Problem, Proceedings of the National Convention of Insurance Commissioners 99 (1933). Mr. Van Schaick’s remarks are reprinted in 77 Cong. Rec. 5222 (1933) and in The Eastern Underwriter, June 9, 1933, p. 23. For citation of authorities and further exposition of some of the problems discussed by the Uniform Commissioners, see, e.g., Notes, 37 Colum. L. Rev. 1031 (1937), The Uniform Insurers Liquidation Act, 89 U. Pa. L. Rev. 92 (1940), Some Problems in Liquidation and Rehabilitation of Insurance Companies, 31 Va. L. Rev. 190 (1944), Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act, 66 Yale L.J. 1072 (1957). For discussion going beyond the insurance context, see, e.g., Goodrich, Conflict of Laws 585-599 (3d ed. 1949); Cheatham, The Statutory Successor, the Receiver and the Executor in Conflict of Laws, 44 Colum. L. Rev. 549 (1944); Annot., 98 A.L.R. 351 (1935).

\textsuperscript{131} Many states are willing to accord extensive rights to a domiciliary receiver, at least if the state of his appointment characterizes him as a statutory successor, as is often the case with insurance company liquidators. See Goodrich, op. cit. supra note 130 at 587; Cheatham, supra note 130 at 552. Referring to statutory successors, section 161 of the Restatement, Conflict of
the problems involved is essentially accurate. Not surprisingly, the response of the National Conference of Commissioners on Uniform State Laws was a uniform statute, the Uniform Insurers Liquidation Act, which, if widely adopted, would undoubtedly go a long way towards eliminating many of the difficulties of administering multi-state insolvent insurance corporations.\textsuperscript{132} Unfortunately, in the eighteen years since the statute was promulgated, only sixteen states have adopted it.\textsuperscript{133} The nature of the uniform act and the problems with which it was designed to deal make the failure of two-thirds of the states to accept it particularly debilitating. Because the statute is reciprocal, an adopting state will not apply it to assets belonging to an insurance company whose state of incorporation has not enacted it.\textsuperscript{134} Furthermore, even if the state of incorporation has adopted the uniform act, if any of the states in which the company owns assets has not, the statute is, of course, inapplicable to those assets, and all the problems of the right of the domiciliary liquidator to that property, preferences to attaching creditors from it and the law governing the order of its distribution may still be present.

The federal equity receivership may, on occasion, prove helpful, but it, too, fails to provide anything like a complete answer. When the managers of a corporation desire to have it reorganized, they may arrange to have a friendly creditor of the corporation whose claim exceeds $3,000 and whose citizenship differs from that of the corporation seek the appointment of a receiver by a federal district court. The creditor’s bill will be rapidly followed by the corpora-

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\textsuperscript{132} This, of course, is not to say that the statute could not be improved in several respects. For some constructive criticism, see Note, The Uniform Insurers Liquidation Act, 89 U. Pa. L. Rev. 92 (1940).


\textsuperscript{134} Martin v. General American Casualty Co., 226 La. 481, 76 So. 2d 537, 46 A.L.R.2d 1178 (1954).
tion’s answer admitting the allegations of the complaint and joining in the prayer for relief.\textsuperscript{135} However, where the creditor’s suit is brought at the instigation of an unfriendly group, hoping perhaps for liquidation of the corporation, the corporation is likely to contest the suit, and when a corporation fights the appointment of a receiver, the creditor’s bill will probably be dismissed if the creditor is an unsecured simple contract creditor,\textsuperscript{136} and it may be dismissed

\textsuperscript{135} The adaptation of the federal equity receivership to corporate reorganization and the shortcomings of this makeshift are fully discussed in, e.g., 6 Collier, Bankruptcy § 0.04 (14th ed. 1943); Finletter, Principles of Corporate Reorganization in Bankruptcy 1-18 (1937); Gerdes, Corporate Reorganizations 22-63 (1936); Report of the Counsel to the Special Committee to the Chairman of the Special Committee to Investigate Receivership and Bankruptcy Proceedings and Administration of Justice in United States Courts, S. Doc. No. 268, 74th Cong., 2d Sess. 19-28 (1936). The shortcomings led to the enactment of the Bankruptcy Act’s corporate reorganization provisions. It is conceivable that the federal equity receivership could be adapted to meet the needs of insolvent insurance corporations, but, as the text and notes following indicate, this is not likely to occur.

\textsuperscript{136} In order to determine whether the action will be dismissed we must discover first whether state or federal law controls. Pusey & Jones Co. v. Hanssen, 261 U.S. 491 (1923), held that a statute in the forum state permitting an unsecured simple contract creditor to obtain a receiver of an insolvent corporation over the corporation’s objection did not affect the contrary federal equity rule, because the state statute conferred “merely a remedy,” and not “a substantive right.” Professor Moore argues persuasively that a repudiation of this aspect of Pusey & Jones is demanded by the theory of Erie R.R. v. Tompkins, 304 U.S. 64 (1938), and the logic of the Supreme Court’s decisions following it: hence where state law permits the appointment of a receiver, a federal court sitting in a diversity case should do the same. See 2 Moore, Federal Practice § 2.09 (2d ed. 1948). He concedes, however, that language in the Court’s opinion in Guaranty Trust Co. v. York, 326 U.S. 99 (1945), “is susceptible of being interpreted as an endorsement of” this aspect of Pusey & Jones, and a recent court of appeals decision has so interpreted it. Inland Empire Ins. Co. v. Freed, 239 F.2d 289, 292 (10th Cir. 1956) (dictum). Consequently, until the Supreme Court gives us a definitive statement on the subject, whether state law determines whether a receiver of a corporation should be appointed in a diversity action brought by an unsecured simple contract creditor.

What, then, is the federal law on the subject? The leading statement appears at p. 497 of Pusey & Jones Co. v. Hanssen, \textit{supra}: “A receiver is often appointed upon application of a secured creditor who fears that his security will be wasted. . . . A receiver is often appointed upon application of a judgment creditor who has exhausted his legal remedy. . . . But an unsecured simple contract creditor has, in the absence of statute, no substantive right, legal or equitable, in or to the property of his debtor. . . . He has no right whatsoever in equity until he has exhausted his legal remedy. . . . The objection that the bill does not make a case properly cognizable in a court of equity does not go to its jurisdiction as a federal court. . . .” However, in Inland Empire Ins. Co. v. Freed, \textit{supra}, a divided court permitted the appointment of a receiver on application of an unsecured contract creditor over the objection of the corporation under these circumstances: “It is clear from the record that the Company is hopelessly insolvent and must be liquidated. When disaster came, it was doing business in twenty-one states, where its assets and liabilities are to be found. The record shows that more than one and a half million dollars is due the company from its agents in all of the states . . . .
even if he holds security for or has recovered judgment on his claim.\textsuperscript{137} Even if the corporation consents to the appointment of a receiver or the situation is one in which a receiver would be ap-

The states of its domicile and principal place of business have freely conceded their inability to rehabilitate or to liquidate for the best interest of the Company, its creditors, policyholders and stockholders. The trial court observed that only six states in which the Company has been authorized to transact business had adopted the uniform liquidation act for insurance companies, and that the only alternative is independent receivership proceedings in each state for the liquidation of the Company and the distribution of the assets. The court said, and we agree, that it would be wholly impractical under existing state laws to liquidate the Company by local receiverships in the various states in which the defendant Company is doing business.\textsuperscript{239} F.2d at 293. If Inland Empire is followed, the federal equity rule will now be that a receiver of an insolvent corporation may be appointed on petition of an unsecured simple contract creditor over the objection of the corporation when unusual circumstances are present; and perhaps such circumstances will be found whenever an insurance corporation cannot soundly be liquidated by the various state officials.

Since there is an excellent chance that the surge of Erie will displace the federal equity rule and make state law govern, an inquiry into state law is in order. Many states have enacted statutes permitting receiverships of insolvent corporations on petition of an unsecured simple contract creditor. See Moore, Cases and Materials on Debtors' and Creditors' Rights 147 (1955). However, statutes of this character, applicable to corporations in general, must yield to more specific enactments dealing with receiverships of insurance corporations, and another common statutory development has been the adoption of statutes which have the effect of prohibiting the appointment of a receiver of an insurance corporation on petition of an unsecured simple contract creditor. E.g., Ill. Stat. Ann. c. 73, § 813 (Smith-Hurd 1940); Mich. Stat. Ann., Ins. Code § 24.17808 (1956); Minn. Stat. Ann. § 60.875 (47) (1946). The Minnesota statute provides: "No order, judgment, or decree providing . . . for the appointment of a temporary or permanent receiver [of an insurer], shall be made or granted otherwise than upon the petition of the commissioner . . . except in an action by a judgment creditor in proceedings supplementary to execution after notice has been served upon the commissioner of such judgment at least 30 days prior to the filing of a petition for that purpose." It is thus apparent that if the Inland Empire gloss on Pusey & Jones Co. v. Hanssen is followed, the law of many states on the availability of a receiver is less liberal than the federal equity rule. If Inland Empire is not followed, both the federal rule and the rule in many states will be that a receiver cannot be appointed on petition of a simple contract creditor over the objection of the corporation.

\textsuperscript{137} See, e.g., the Michigan statute cited supra note 136: "No application for injunction against or proceedings for the dissolution of or the appointment of a receiver for any such insurance corporation included within the provisions of this chapter, shall be entertained by any court in this state, unless the same is made by the attorney general upon relation or application of the commissioner of insurance of this state." If this statute is applicable in a diversity action, not only are suits for receiverships by all creditors barred, but even if a receivership on petition of a stockholder or policyholder might otherwise be appropriate, see Glenn, Liquidation 254, 261 (1935), the statute precludes the granting of such relief. Several decisions have held statutes of this character applicable to federal court proceedings brought by policyholders. Cook v. Illinois Bankers' Life Ass'n, 46 F.2d 782 (7th Cir.), \textit{cert. denied}, 284 U.S. 627 (1931); McGarry v. Lentz, 13 F.2d 51 (6th Cir.), \textit{cert. denied}, 273 U.S. 716 (1926); Wright v. The Praetorians, 63 F. Supp. 839 (N.D. Tex. 1943), \textit{aff'd}, 152 F.2d 856 (5th Cir. 1945). Presumably, even the consent of the corporation to the receivership would be unavailing in the face of such a statute.
pointed over the corporation's objection, the attempt may still founder if the official in the state of incorporation charged with dealing with the insolvency of this debtor insists upon handling the liquidation or rehabilitation himself.\textsuperscript{138}

\textsuperscript{138} If that official commences state court proceedings for the liquidation or rehabilitation of the debtor before the federal receivership proceeding is begun, the federal court will be obliged to yield unless the state court is willing to do so because, "[T]he first court whose jurisdiction and processes is invoked by the filing of a suit [for receivership], is treated as in constructive possession of the res and authorized to proceed in the cause. Having thus acquired jurisdiction and possession, the property is thereby withdrawn from the jurisdiction of all other courts, except to the extent to which that court may determine." Continental Bank and Trust Co. v. Apodaca, 239 F.2d 295, 297 (10th Cir. 1956), collects the leading authorities; additional authorities are collected in Annot., 11 A.L.R.2d 460 (1950).

Even if the state official takes no action before federal jurisdiction attaches, the continuation of the federal proceeding may depend upon his consent. See Pennsylvania v. Williams, 294 U.S. 176 (1935), and Gordon v. Ominsky, 294 U.S. 186 (1935), in which the Supreme Court reversed lower court decisions for failure to order federal equity receivers to turn over the assets of Pennsylvania building and loan associations to the Pennsylvania Secretary of Banking. Accord, Gordon v. Washington, 295 U.S. 30 (1935); Penn General Casualty Co. v. Pennsylvania ex rel. Schnader, 294 U.S. 189 (1935). In the Williams case, after pointing out that federal jurisdiction was present, the Court said: "The question remains whether, in the special circumstances of the case, the district court rightly retained its jurisdiction. The relief prayed in the bill of complaint is equitable in its nature, and the prayer was addressed to the sound discretion which is the controlling guide of judicial action in every phase of a suit in equity. The relief sought, an injunction and the appointment of receivers, was aimed at the prevention of irreparable injury, from the waste of the assets of the insolvent corporation which would ensue from a race of creditors . . . . By local statutes elaborate provision is made for accomplishing the same end, through the action of a state officer, in substantially the same manner and without substantially different results from those to be attained in receivership proceedings in the federal courts. There is no allegation or contention that the procedure thus provided is inadequate, or that it will not be diligently and honestly followed. In such circumstances the discretion of the district court . . . should have been exercised to relinquish the jurisdiction in favor of the statutory administration of the corporate assets by the state officer." 294 U.S. at 182. It can be inferred from the latter part of this passage that a federal court should exercise its jurisdiction where a federal receivership will attain substantially better results than state administration either because the state procedure is inadequate in some respect or because the state procedure will not be diligently and honestly followed. While the Supreme Court has not had occasion to elaborate this facet of its opinion, the Court of Appeals for the Ninth Circuit has made the inference, holding in Intermountain Building & Loan Ass'n v. Gallegos, 78 F.2d 972 (9th Cir.), cert. denied, 296 U.S. 639 (1935), that the federal district court for Arizona did not abuse its discretion by appointing a receiver of the Arizona assets of a Utah building and loan association over the objection of the Utah official charged with the supervision of such corporations when it appeared that the association had been insolvent for several years and the Utah official had failed to take action. The court observed that the district court could properly have found that the Utah official "had shown himself not to be a proper person to husband the dwindling assets of the failing Association." Id. at 983. Cf. Gallegos v. Smith, 111 F.2d 805 (9th Cir.), cert. denied, 311 U.S. 668 (1940); Brashear v. Intermountain Bldg. & Loan Ass'n, 109 F.2d 857 (9th Cir.), cert. denied, 311 U.S. 655 (1940), in which the same court affirmed refusals to appoint receivers for the Oregon and California assets of the same association because the statutory procedures of Oregon
If a federal receivership can be obtained, section 754 of title 28 does seem to promise that at least the collection of assets of an insolvent insurance corporation will proceed more efficiently than it would under numerous state administrations. That statute provides:

A receiver appointed in any civil action or proceeding involving property, real, personal or mixed, situated in different districts shall, upon giving bond as required by the court, be vested with complete jurisdiction and control of all such property with the right to take possession thereof.

He shall have capacity to sue in any district without ancillary appointment, and may be sued with respect thereto. . . .

However, recent litigation involving the Inland Empire Insurance Company illustrates that the gain in efficiency may not be very great. Inland Empire is an Idaho corporation with assets and liabilities in twenty-one states and its principal place of business in Utah. A two-judge majority of the Court of Appeals for the Tenth Circuit believed that a receiver for Inland Empire should be appointed because, "[I]t would be wholly impractical under existing state laws to liquidate the Company by local receiverships in the various states in which the defendant Company is doing business," and "[F]ederal law has made adequate provision for the acquisition and complete jurisdiction and control over the property of the Company wherever and in whatever district it may be located. . . ."

Notwithstanding the federal law's provision for complete control over the company's property, the court's concluding paragraph intimates that perhaps the receiver ought not to exercise this control in all cases:

It may well be that a number of the state insurance commissioners having authority and duty to act will assert the right to exclusively control the liquidation of the assets (sic) of the Company in their respective states. In these circumstances, it will of course be in the wise discretion of the trial court to avoid undue conflict with the state court processes.

and California were adequate and it was not shown that those procedures would not be diligently and honestly followed.

Inland Empire Insurance Co. v. Freed, supra note 140, at 293. See Intermountain Bldg. & Loan Ass'n v. Gallegos, supra, would further limit the holding of the Supreme Court in Pennsylvania by Williams, supra, by permitting a receiver to be appointed where the state in which the federal receiver is sought has a public policy favoring local creditors over an out-of-state liquidator of a foreign corporation and the official contesting the federal receivership is from another state.

140. See Inland Empire Insurance Co. v. Freed, 239 F.2d 289 (10th Cir. 1956); Continental Bank and Trust Co. v. Apodaca, 239 F.2d 295 (10th Cir. 1956); Continental Bank & Trust Co. v. Gold, 140 F. Supp. 252 (E.D. N.C. 1956).
141. Inland Empire Insurance Co. v. Freed, supra note 140, at 293.
142. Ibid.
If this means that the trial court should not insist that the federal receiver prevail over the claims of local administrators to liquidate property and satisfy claims within their states, then, of course, unified administration of the corporation is possible only if all of the state administrators consent to the receivership. The improbability of all twenty-one state officials being so agreeable is adequately demonstrated by the fact that one took the trouble to intervene and oppose the appointment of the receiver in the first instance.

The Court of Appeals for the Tenth Circuit had a chance to delineate more clearly the extent of its concern for avoidance of "undue conflict with state court processes" in Continental Bank and Trust Co. v. Apodaca. After the commencement of the Inland Empire suit, but before the receiver was appointed, a New Mexico state court appointed the superintendent of insurance of that state conservator of $40,000 deposited by Inland Empire with the New Mexico state treasurer for the protection of New Mexico creditors and policy holders. After the federal receiver was appointed, he brought suit in the federal district court for New Mexico to require the New Mexico superintendent to turn over the $40,000. On appeal from the dismissal of the receiver's suit, the court indicated first that since the suit for a receiver was instituted in the Utah federal court before the New Mexico state court proceeding was begun, the Utah federal court had exclusive jurisdiction over the $40,000. However, the court reasoned, because a federal court of equity may adopt any means it deems appropriate to liquidate a debtor's estate, the Utah federal court may, if it wishes, relinquish jurisdiction to the New Mexico state court. Since New Mexico claimants have substantive rights in the deposit made for their benefit, it may be that the best means of proceeding would be to permit the New Mexico courts to deal with that deposit. But this is a question for the Utah, not the New Mexico, federal court: the dismissal must be reversed and the lower court instructed to abide the decision of the Utah federal court. While refusing to exercise the Utah court's discretion for it, the Court of Appeals did say:

It seems not inappropriate ... to observe that each of the states involved has provided procedural details for the rehabilitation, conservation and liquidation of domestic insurance companies or insurance companies licensed to do business in the state. And, as we indicated in Inland Empire Insurance Co. v. Freed, ... it may be in the public interest to leave the procedural details to the conservators of the respective states, subject always of course to the paramount jurisdiction of the domiciliary federal

143. 239 F.2d 295 (10th Cir. 1956).
court... [I]t will be within the province of the Utah court to use its wise discretion to avoid unseemly conflicts within the framework of the federal court receivership.\textsuperscript{1144}

Thus, it appears that while the Tenth Circuit is willing to appoint a receiver for the affairs of an insolvent insurance corporation, it is not sure of the extent to which that receiver ought to displace individual state administrations. The Utah district court is left to fashion, as best it can, a truncated system of bankruptcy administration for insurance corporations.

That serious difficulties await the receiver of Inland Empire is illustrated by \textit{Continental Bank & Trust Co. v. Gold},\textsuperscript{1145} in which Inland Empire's receiver sought to compel the Commissioner of Insurance and the Treasurer of North Carolina to turn over a statutory deposit made by the predecessor of Inland Empire. The court held that the receiver was not entitled to possession of the deposit under 28 U.S.C. § 754 because the deposit was not the property of the insurance company:

\begin{quote}
It is the manifest intention of the North Carolina Legislature that the title and rights to securities deposited in accord with the above statutes are vested in the Commissioner, the Treasurer, and the State. These securities cannot be said to be the "property" of the company which maintains them... the only property right of the company or its receiver is in the securities or funds remaining after the trust is administered in accord with the statutes that create it.\textsuperscript{1146}
\end{quote}

In this case the federal receiver was no better off than a receiver from another state would have been.\textsuperscript{1147}

In sum, neither uniform legislation nor the federal equity receivership has been able to resolve the difficulties inherent in the insolvency administration of multi-state corporations. The failure of a large majority of states to accept uniform legislation on this subject seems to have vindicated the early prediction that such legislation "is no more than a Utopian dream."\textsuperscript{1148} The receivership suffers from several ills: its limited availability is an obvious drawback; it requires case by case development of a body of principles for unravel-

\textsuperscript{1144} Id. at 300.
\textsuperscript{1145} 140 F. Supp. 252 (E.D. N.C. 1956).
\textsuperscript{1146} Id. at 257.
\textsuperscript{1147} Cf. Note, \textit{Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act}, 66 Yale L.J. 1072, 1074 n. 11 (1957), citing Brief for Receiver, p. 7, Inland Empire Ins. Co. v. Freed, 239 F.2d 289 (10th Cir. 1956) : "In the recent insolvency of the Inland Empire Insurance Co., the federal receiver has been able to marshal assets in sixteen of the twenty-one states in which Inland did business. In the other states, where jurisdiction over the insolvent's property was first assumed by the state courts, distribution will be made through independent receiverships."
\textsuperscript{1148} Van Schaick, \textit{supra} note 130, at 103.
ling the complexities of administering insolvent insurance companies, a task that is surely more susceptible of accomplishment by legislation; and respect for the tender sensibilities of state courts and administrators is, to some undefined extent, likely to impede its use. That leaves the Bankruptcy Act.\textsuperscript{149}

In view of the complexities of insurance company liquidation and rehabilitation, it would be presumptuous for us to propose specific legislation. When the peculiarities of the insurance business are considered, the most fruitful avenue for further study appears to be a special bankruptcy chapter, rather than simple admittance to straight bankruptcy and reorganization.\textsuperscript{150} To be dealt with are such problems as how to treat the security deposits that insurance companies are often required to make in the states in which they do business. To what extent should state laws which prefer local creditors and policyholders out of such deposits be respected? Should creditors and policyholders who receive part payment from such deposits be permitted to prove the remainder of their claims on a par with creditors who have not been so preferred? Should such preferred creditors and policyholders be postponed in distribution until other creditors and policyholders have received as great

\textsuperscript{149} As the title of Note, \textit{Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act} 66 Yale L.J. 1072 (1957), indicates, this piece recommends that the problems of liquidating interstate insurance companies be dealt with under the commerce power via an amendment to the McCarran-Ferguson Act, rather than by bankruptcy legislation. While the legislation needed could be sustained under either the commerce or bankruptcy power, use of the commerce power seems tactically inadvisable. The opposition of the insurance industry to federal legislation dealing with the problems of insolvent insurance companies is probably based in part on the fear that such legislation would be the opening wedge in the replacement of state regulation by federal regulation. This fear, and hence the industry's opposition, is apt to become even more pronounced if such legislation takes the form of an exercise of the federal government's virtually limitless commerce power than if it appears as an exercise of the more confined bankruptcy power.

\textsuperscript{150} See 1 Corp. Reorg. 134 (1934), \textit{But see} Report of the Counsel to the Special Committee to the Chairman of the Special Committee to Investigate Receivership and Bankruptcy Proceedings and Administration of Justice in United States Courts, S. Doc. No. 268, 74th Cong., 2d Sess. 46 (1936), which advocated that Section 77B be amended to permit the excluded corporations to reorganize under that statute, subject to this qualification: "In order, however, that benefit may be taken of beneficent State statutes, the Federal court should be authorized to yield jurisdiction to the State courts, where the following factors are all present: (1) all the assets and the places of business of a corporation are located within the State of its organization; (2) an adequate State statute for reorganization exists; (3) the corporation is one which is subject to the jurisdiction of a regulatory commission or commissions or other regulatory authority or authorities created by the law of the State of its organization and (4) the court finds the interests of the debtor and its creditors will be best subserved by such relinquishment of jurisdiction."
a proportion of their claims as the preferred group?\textsuperscript{151} Or should preferences from these special deposits be interdicted entirely and the deposits devoted to the payment of all creditors and policyholders regardless of where located? Another problem is the role to be accorded state administrators. A possible model is provided by sections 177 and 178 of the Bankruptcy Act, which require the appropriate regulatory commission's approval of a reorganization plan for an intrastate public utility and an opportunity for such commissions to suggest amendments or offer objections to a plan for a public utility which is not confined to one state.\textsuperscript{152} Perhaps state insurance commissioners should have an even greater role; it has been suggested that if insurance corporations are brought under the Bankruptcy Act, the right to invoke the statute should be confined to state officials and they should be appointed bankruptcy trustees.\textsuperscript{153} Some thought would also have to be given to priorities. For example, should a policyholder's claim for unearned premiums, a widow's claim for benefits on her husband's life insurance policy and a claim of a commercial creditor of the company all receive the same treatment?\textsuperscript{154} Many other questions could be added to this list,\textsuperscript{155} but enough have been set forth to warrant the conclusion that a special bankruptcy chapter is probably the most appropriate vehicle for solving the problems involved in administering an insolvent insurance corporation.

\textbf{B. Banking Corporations.}

The need for bankruptcy legislation for banks is not nearly so compelling as the need for insurance corporations. For one thing, an insolvent bank is not likely to have its assets and liabilities quite so widely scattered as an insolvent insurance company.\textsuperscript{156} More


\textsuperscript{152} See note 129 supra.

\textsuperscript{153} See Van Schaick, supra note 130, at 104; 1 Corp. Reorg. 134 (1934).

\textsuperscript{154} See Note, Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act, 66 Yale L.J. 1072, 1083 (1957), for a suggested solution to this problem which the authors hope may help overcome "the traditional reluctance of Congress to dictate to the states in the field of insurance."

\textsuperscript{155} For some further problems to be considered, see authorities cited in note 130 supra.

\textsuperscript{156} The prevalence of statutes forbidding out-of-state banks to accept deposits generally limits, but does not prevent wholesale scattering, for this still leaves qualified out-of-state banks free to do such things as lend money, buy and sell bills of exchange, issue letters of credit, and receive money for transmission. See, e.g., Cal. Fin. Code Ann. § 1756 (West 1955). Out-of-state banks are more severely limited in Minnesota. See Minn. Stat. Ann. § 303.04 (1947).
important, insolvent banks are not all left to the same devices as insolvent insurance companies.

Unified and probably efficient insolvency administration is available for national banks by virtue of the fact that Congress has vested primary responsibility for their liquidation and rehabilitation in the Comptroller of the Currency and the Federal Deposit Insurance Corporation.157 Because federal law governs, the barriers to successful administration that face a state liquidator are avoided,158 and so there would seem to be no pressing reason to replace the present system for national banks with bankruptcy legislation.

Federal legislation has affected the insolvency administration of state banks too. Returning to the Uniform Commissioners’ list of problems,159 we find, first, that expertise in the handling of an insolvent bank’s affairs is made possible by the statutory authorization of the Federal Deposit Insurance Corporation to accept appointment as receiver of any closed insured bank if the appointment is offered “by the authority having supervision of such bank and is authorized or permitted by State law.”160 A majority of states, responding to this invitation, have authorized tender of receivership appointments to the FDIC.161

Neither the statute governing the FDIC, the regulations promulgated under it, nor the cases construing it deal specifically with the problems of collecting assets outside of the state of incorporation. It will be recalled that there are three major problems here: (1) limitations on the right of a receiver to sue outside of the state


158. See Glenn, Liquidation 855 (1935): "Although [a national] bank while in operation is treated for some jurisdictional purposes as a citizen of the state where it is located, that is because the federal statutes make the concession. But there is no such concession when it comes to the winding up of the institution. As the liquidation is wholly a matter of federal law which operates uniformly in all the States, the receiver whom the Comptroller puts in charge of a national bank is an officer of the United States, and his powers are just as effective in one State as in another."

159. See text at note 130 supra.


of his appointment;\textsuperscript{162} (2) possible conflicts between the domiciliary receiver and ancillary receivers over the title to and right to possession of assets outside of the state of incorporation; and (3) the danger that creditors outside of the state of incorporation will obtain preferences by attaching property of the insolvent corporation in their states before ancillary proceedings are commenced.\textsuperscript{163} While appointment of the FDIC as receiver of a state bank may insure greater expertise in the handling of the bank’s affairs, it probably does not confer any greater rights upon the FDIC than an ordinary state receiver would have.\textsuperscript{164} Consequently, states which deny out-

\textsuperscript{162} One of the exceptions to the limitations on the power of a receiver to sue outside the state of his appointment is particularly relevant to bank receivers. Many states have had statutes imposing liability on bank stockholders in addition to their ordinary liability for stock subscriptions. This added liability is for corporate debts and is imposed for the benefit of a bank’s creditors. When the statute creating this added liability empowers a receiver to collect on it, the receiver is treated as a “quasi-assignee” of the corporation’s creditors and may sue stockholders of the corporation in any state. If a state denies him the right to sue, it denies full faith and credit to the statutes of the state of incorporation. \textit{E.g.}, Broderick v. Rosner, 294 U.S. 629 (1935); Converse v. Hamilton, 224 U.S. 243 (1912); see Goodrich, Conflict of Laws 588 (3d ed. 1949). This exception has become less important as a number of states have elected to rely on the Federal Deposit Insurance Corporation for the payment of an insolvent bank’s debts and have largely eliminated “superadded” bank stockholder liability. See, \textit{e.g.}, Cal. Fin. Code Ann. §§ 3135, 3138 (West 1955); Minn. Stat. Ann. § 48.03, as amended, 1957 Minn. Laws c. 601. For further consideration of the problems of collecting on stockholders’ liability outside the state of incorporation, see Note, Foreign Enforcement of Stockholder Liability, 36 Colum. L. Rev. 1108 (1936) and authorities there cited; \textit{cf.} Pink v. A.A.A. Highway Express, Inc., 314 U.S. 201 (1941); Christopher v. Brusselback, 302 U.S. 500 (1938).

\textsuperscript{163} See text at note 130 \textit{supra} and authorities there cited. The problem of preference by attachment is obviated for banks in a number of states by statutes which deny attachment to creditors of a bank. See, \textit{e.g.}, Cal. Fin. Code Ann. § 3105 (West 1955). The 1957 session of the Minnesota Legislature amended § 571.43 of the garnishment statute to provide: “No person or corporation shall be adjudged a garnishee by reason of: . . . Any money or other thing due to the defendant where the defendant is a bank, savings bank, trust company or a savings and loan association.” Minn. Laws 1957, c. 184. However, no comparable limitation was imposed on attachment, and while the remedy of attachment is rather narrowly limited in Minnesota, it is available against a foreign corporation. Minn. Stat. Ann. § 570.02 (1947).

The problem of preferences to creditors outside of the state of incorporation was presented in a different fashion by Hornick, More & Porterfield v. Farmers’ & Merchants’ Bank, 56 S.D. 18, 227 N.W. 375 (1929), which held that reduction of a bank’s liabilities pursuant to a plan of reorganization does not bind a non-resident creditor who did not participate in the reorganization proceeding; such a creditor may, therefore, recover the full amount of his claim. See 43 Harv. L. Rev. 1154 (1930); Comment, 32 Mich. L. Rev. 221 (1933).

\textsuperscript{164} 48 Stat. 174, as amended, 12 U.S.C. § 1821(e) (1952) assures the FDIC “all the rights, powers and privileges granted by State law to a receiver of a State bank,” but goes no further. The fourth paragraph of § 1819 tends to support the conclusion that the FDIC acquires only the rights which any state receiver would have. That paragraph excepts from the provision that suits to which the FDIC is a party “shall not be deemed to arise under the laws of the United States” suits “to which the Corporation is a party in its
of-state chancery receivers\textsuperscript{165} the power to sue probably can deny that power to the FDIC in its capacity as receiver if bank receivers are merely chancery receivers under the law of the state in which the FDIC was appointed. Similarly, if a state in which an insolvent bank has assets wishes to confer the title to and right to possession of those assets on an ancillary receiver other than the FDIC, the FDIC’s rights to those assets as domiciliary receiver would be inferior to the rights of the ancillary receiver. Finally, it would seem that a state’s power to permit an attaching creditor to prevail over an out-of-state receiver previously appointed is not diminished by the fact that the out-of-state receiver happens to be the FDIC.\textsuperscript{166} The FDIC could, of course, seek appointment as ancillary receiver in each of the states in which the bank had assets, but this can be cumbersome and expensive and, furthermore, not every state has authorized appointment of the FDIC as receiver.

Despite the failure of the authorities to deal specifically with the problems of collecting assets outside of the state of incorporation, the FDIC does have powers which may help it achieve the benefits of unified insolvency administration. When an insured bank becomes insolvent and is unable to pay its depositors in full, the FDIC can fulfill its insurance obligation by having another insured bank assume the deposit liabilities of the insolvent bank. Obviously, no bank will agree to assume those liabilities unless it receives a commensurate transfer of assets, and since the insolvent bank presumably lacks the requisite assets, the FDIC must agree to supply the deficiency. It may do this by lending to the insolvent bank enough funds to make up the deficit, with the insolvent bank’s more dubious assets as collateral for the loan. The insolvent bank then transfers its acceptable assets, including the proceeds of the FDIC loan, to capacity as receiver of a State bank and which involves only the rights or obligations of depositors, creditors, stockholders, and such State bank under State law . . . .”

\textsuperscript{165} A chancery receiver is a receiver whose powers derive primarily from court appointment rather than from a statute in the state of incorporation designating him as the official to whom title to the assets of a bank in liquidation shall pass. Authorities on the nature of bank receiverships in various states are collected in Legis. Note, Legal Devices for the Rehabilitation of Banks, 32 Colum. L. Rev. 1395 nn. 3 & 4 (1932; see 3 Michie, Banks and Banking 34-37 (1931).

\textsuperscript{166} That states may, and often do, permit an attaching creditor to prevail over an out-of-state chancery receiver previously appointed is clear. See Goodrich, op. cit. supra note 162, at 590. A state’s power to treat an out-of-state statutory successor this way is somewhat limited by the Clark v. Williard litigation, 292 U.S. 112 (1934), 294 U.S. 211 (1935), but some states continue to permit a levying creditor to prevail over an out-of-state statutory successor previously appointed. See Note, Insurance Liquidations: A Proposed Amendment to the McCarran-Ferguson Act, 66 Yale L.J. 1072, 1073 (1957), and authorities there cited.
the assuming bank. The transaction leaves the insolvent bank with only its equity of redemption in the doubtful assets transferred to the FDIC, which is worthless, of course, because the loan extended by the FDIC will have far exceeded the value of the doubtful assets transferred to it. Use of this arrangement could avoid to a considerable extent the problems of collecting the bank's assets outside of the state of incorporation. As transferee of those assets, the assuming bank or the FDIC, as the case may be, obviously has the right to sue anywhere to protect the rights acquired by the transfer. No ancillary receivership is worth the trouble because the insolvent bank's only remaining asset is presumably worthless. Similarly, nothing remains for any creditor of the bank to attach.

If the procedure outlined above is successfully employed, another problem on the Uniform Commissioners' list ceases to be bothersome. If there are not ancillary administrations, there will be no need to determine whether the law of the corporation's domicile or the law of the place of ancillary administration governs priorities in the distribution of an insolvent bank's assets.

Unfortunately, the assumption of deposit liabilities arrangement has some rather serious drawbacks when viewed as a device for avoiding the problems of collecting out-of-state assets. If creditors who are unprotected by deposit insurance learn of the bank's pre-

167. A full description of this sort of arrangement can be found in Thomas P. Nichols & Son Co. v. National City Bank of Lynn, 313 Mass. 421, 48 N.E.2d 49, cert. denied, 320 U.S. 742 (1943). Authorization for this practice is contained in § 1823(e) of Title 12: "Whenever in the judgment of the Board of Directors such action will reduce the risk or avert a threatened loss to the Corporation and will facilitate a merger or consolidation of an insured bank with another insured bank, or will facilitate the sale of the assets of an open or closed insured bank to and assumption of its liabilities by another insured bank, the Corporation may, upon such terms and conditions as it may determine, make loans secured in whole or in part by assets of an open or closed insured bank, which loans may be in subordination to the rights of depositors and other creditors, or the Corporation may purchase any such assets or may guarantee any other insured bank against loss by reason of its assuming the liabilities and purchasing the assets of an open or closed insured bank." As this section indicates, variations on the arrangement described in the text are possible. The FDIC, instead of lending money on the security of the dubious assets, may purchase them outright. See Brown v. New York Life Ins. Co., 152 F.2d 246 (9th Cir. 1945); Lamberton v. FDIC, 141 F.2d 95 (3d Cir. 1944); FDIC v. Rectenwall, 97 F. Supp. 273 (N.D. Ind. 1951); FDIC v. Cloonan, 165 Kan. 68, 193 P.2d 656 (1948). Or, instead of dealing with an existing insured bank, the FDIC may organize a new bank to take over the deposit liabilities of the insolvent corporation. 48 Stat. 175 (1933), as amended, 12 U.S.C. § 1821(h)-(l) (1952); see FDIC v. Wainer, 4 Ill. App.2d 233, 124 N.E.2d 29 (1955). Section 1823(c) even authorizes the FDIC to keep the insolvent bank in operation by loans or purchase of its assets "when in the opinion of the Board of Directors [of the FDIC] the continued operation of such bank is essential to provide adequate banking service in the community."
carious condition before the transfer is completed, they can attempt a levy on the bank's assets or take steps to obtain a receivership of the bank's assets in their state. If either event occurs before the transfer is completed, the interest of the levying creditor or receiver in those assets will be superior to that of the insolvent bank's transferee, whether that is the assuming bank or the FDIC. In addition, the rights of creditors other than depositors are uncertain when the assumption arrangement is employed. The assumption agreements reported in the cases characteristically make no provision for creditors other than depositors. The indications are that non-deposit claims are settled either by the insolvent bank with the approval of the FDIC before the transfer to the assuming bank is concluded, or by the FDIC after the transfer. However, if the claim of a creditor other than a depositor is not settled, while he may have a remedy against the assuming bank, he has no practical remedy against the judgment-proof defunct bank and no rights at all against the FDIC. There is some danger, then, of oppression of creditors.

168. In many states receivership proceedings can only be instituted by the state official in charge of banking: See 9 Zollman, Banks and Banking § 6204 (1936) and authorities there cited.

169. See cases cited note 167 supra.


If the bank offers partial payment to creditors before the deal is concluded, there is the obvious danger that those creditors will attempt to gain a greater share of their claims by levying on the assets of the bank. Consequently, to the extent that this means of settling with creditors other than depositors is used, one purpose of the assumption arrangement may be defeated.

171. In Lamberton v. FDIC, supra note 170, the bank's board of directors, over the objection of the FDIC's representative, voted to pay the bank's employees their full month's wages even though the bank was to close on the twentieth of the month. After the payment was made, the FDIC's representative caused the amount of the excess payment to be charged against the deposit account of plaintiff, the bank's president. Since the assuming bank was only to be responsible for the closed bank's deposit liabilities, plaintiff was credited by the assuming bank with only the amount of his reduced account. Holding that the FDIC was not liable to the plaintiff for the amount by which his deposit was diminished, the court stated that, "The fact that a particular claim against a bank was not taken into consideration in fixing the terms upon which the F.D.I.C. made a loan to a bank, gives the creditor of the bank no claim against the F.D.I.C." Id. at 97. The court declined to pass on the question whether the payment to the bank's employees was illegal and properly chargeable to the plaintiff. For the purposes of the decision, then, it must be assumed that the plaintiff had a valid claim against the closed bank which was unprovided for by the assumption agreement, and the court's language indicates that it would apply the same rule to any non-deposit creditor whose claim was not included in the assumption agreement, regardless of how the claim arose. See Thomas P. Nichols & Son Co. v. National City Bank of Lynn, 313 Mass. 421, 48 N.E.2d 49, 53, cert. denied, 320 U.S. 742 (1943).

The assumption agreement was not, of course, invented by the draftsmen of the FDIC legislation: before that legislation was enacted, such agreements
other than depositors when the assumption agreement is employed. Finally, if the insolvent bank has deposited securities in another state pursuant to a statute which makes a security deposit for the benefit of local creditors a condition to doing business in that state, the bank's lack of power to transfer those securities without the consent of their official custodian would prevent title from passing to either the FDIC or the assuming bank, and the securities would be applied to the claims of creditors in the depository state.

Whatever the potential utility of the assumption of liabilities arrangement, it cannot be much help unless the FDIC is willing to use it. The regulations provide that, "The Corporation's practice has been to make such payment[s] [of insured deposits] by issuing its check for the amount of the insured deposit." In fact, however, the Corporation has utilized the assumption arrangement in a substantial proportion of the cases in which insured banks have failed: "During the 23 years of Federal deposit insurance ending December 31, 1956, the Corporation made disbursements to protect depositors of 431 banks. . . . Deposits were paid up to the insurance maximum in 250 cases; deposit assumptions were arranged in the remaining 181 cases." Whether the FDIC will arrange a deposit assumption depends largely on how serious the difficulties of the distressed bank are: the greater the deterioration of the distressed bank's position the greater the likelihood that the FDIC will elect to pay depositors off directly and let the bank go into receivership. The FDIC's practice in this respect is attributable to the fact that when an assumption arrangement is employed, the $10,000 per

were occasionally worked out by banks without any governmental assistance. See Annot., 84 A.L.R. 1425 (1933) for a collection of some instances. If such an agreement failed to provide for creditors other than depositors, it might be held a fraudulent transfer assailable by a general creditor's bill demanding ratable distribution to all creditors of the assets transferred. See 1 Glenn, Fraudulent Conveyances and Preferences 481-483 (1940). There would seem to be no harm in applying this principle to assumption agreements arranged by the FDIC as long as the funds provided by the FDIC are not considered a part of the assets to be shared by all creditors. Non-deposit creditors would then be assured of their fair share of the distressed bank's assets. New York has adopted a statute which specifically protects the rights of all creditors to pro rata payment even though the FDIC arranges a deposit assumption. N.Y. Banking Law § 605-a.

174. FDIC Ann. Rep. 9 (1955). With the exception of 1955, the practice in recent years actually seems to have favored the assumption arrangement. A deposit assumption was arranged for one of the two insured banks which failed in 1956 and for one of the five insured banks which failed in 1955. Deposit assumptions were arranged for every one of the twenty-seven insured banks which failed during the decade 1945-1954. See ibid.; FDIC Ann. Rep. 162 (1955).
account insurance limit is not applied, every deposit being assumed in full regardless of size. Since the assumption arrangement thus subjects the FDIC to much greater potential loss than would direct payment of depositors within the insurance limits, its reluctance to employ this procedure for a really woebegone bank is readily understandable.

In sum, the FDIC has at its disposal a procedure that can help achieve efficient and fair insolvency administration of state banks, but this procedure does have serious drawbacks and the FDIC is not likely to use it if doing so will substantially increase its own losses.

The principal impact of the FDIC on the problems of state bank insolvency has nothing to do with the machinery for liquidation at its disposal. The FDIC's impact derives, rather, from its power to help prevent insolvency and from the fact that it assures the overwhelming majority of a bank's creditors, depositors of less than $10,000, of full payment. Insured banks must submit to considerable supervision by the FDIC in order to acquire and retain

177. While, at the end of 1956, approximately 98 per cent of all accounts in insured banks had balances of less than $10,000 and hence were fully insured, the balances in the remaining 2 per cent of accounts were sufficiently large to bring the estimated percentage of insured funds down to 55 per cent of the funds on deposit with insured banks. Thus, of $218 billion on deposit in insured banks, only about $120 billion were insured. See FDIC Ann. Rep. 3 (1956). Because the largest banks contain the largest deposits and so have the largest amount of uninsured deposit liability, see FDIC Ann. Rep. 49 (1955), the larger the bank the greater the apparent cost to the FDIC in excess of its insurance obligation when a deposit assumption is arranged. We might expect, then, that the larger the bank the less attractive an assumption arrangement would be to the FDIC. In fact, the FDIC's statistics reveal that the larger the bank the greater the likelihood that an assumption of deposits will be arranged. Thus, deposit assumptions were arranged for forty-seven of the 216 insured banks which failed with deposits of less than $250,000, for fifty-nine of the 122 insured banks which failed with deposits between $250,000 and $1 million, for fifty-seven of the seventy-two insured banks which failed with deposits between $1 million and $5 million, and for seventeen of the nineteen insured banks which failed with deposits in excess of $5 million. See FDIC Ann. Rep. 162 (1955). This apparent contradiction is accounted for in part by the fact that larger banks generally hold substantial interbank deposits which are normally well over $10,000. Id. at 53. If the FDIC refuses to arrange a deposit assumption and all but $10,000 of each interbank deposit is lost to the depositing banks, the depositing banks may well find themselves in difficulties which cause additional failures. Thus, even though arranging a deposit assumption may cause the FDIC a greater immediate loss with respect to the failed bank, the arrangement may actually save the FDIC from considerable losses over the long run.
178. "Losses to depositors of insured banks since establishment of the Corporation have amounted to .5 per cent of their deposits; and only .3 per cent of the depositors have experienced any loss. All depositors of the 181 banks whose deposits were assumed by another insured bank were fully protected. In the 250 banks where payoffs occurred, 97.4 per cent of deposits have been paid or made available; and full recovery has been received or made available to 99.1 per cent of the depositors." FDIC Ann. Rep. 12 (1956); see
their insured status.\textsuperscript{170} The FDIC's supervision, in conjunction with that of other government agencies,\textsuperscript{180} diminishes the likelihood that an insured bank will engage in unsound banking practices leading to insolvency or continue in such practices for very long.\textsuperscript{181} If insolvency does occur, the FDIC's assurance of payment to depositors means that there will be few creditors interested in seeking preferences by levy on the bank's out-of-state assets. Similarly, since a domiciliary liquidator is resisted by other states largely because of fear that local creditors would be prejudiced by according him full rights,\textsuperscript{182} the FDIC's assurance of payment to depositors may result in the FDIC's supervision, in conjunction with that of other government agencies,\textsuperscript{180} diminishes the likelihood that an insured bank will engage in unsound banking practices leading to insolvency or continue in such practices for very long.\textsuperscript{181} If insolvency does occur, the FDIC's assurance of payment to depositors means that there will be few creditors interested in seeking preferences by levy on the bank's out-of-state assets. Similarly, since a domiciliary liquidator is resisted by other states largely because of fear that local creditors would be prejudiced by according him full rights,\textsuperscript{182} the FDIC's assurance of payment to depositors may result in


\textsuperscript{180} The FDIC's supervision supplements that exercised by the Comptroller General and Federal Reserve System over national banks, that exercised by state authorities and the Federal Reserve System over members of the Federal Reserve System and that exercised by state authorities over state banks not members of the Federal Reserve System.

\textsuperscript{181} See, e.g., FDIC Ann. Rep. 4 (1955): "When examination of a bank reveals unsafe or unsound banking practices or a violation of law or regulations, the examiner confers with the officials of the bank and its board of directors. The necessary corrections are usually forthcoming. However, where such practices or violations persist, the Corporation has a legal duty imposed upon it by Section 8(a) of the Federal Deposit Insurance Act to institute proceedings for the involuntary termination of the insured status of such bank. Proceedings are initiated only after every effort has been made through cooperation with the bank to obtain the observance of sound and lawful procedures; for the primary purpose of such proceedings is to secure discontinuance of the unsound and unlawful practices."

\textsuperscript{182} If a domiciliary liquidator is permitted to prevail over local levying creditors, they may receive a smaller share of the distribution than their levies would net them; if he is permitted complete freedom to sue and collect assets, there may be insufficient assets left in the state to satisfy local creditors, and they may then be forced to the inconvenience and expense of presenting their claims in the proceedings at the corporation's domicile, where the rules
duce hostility to the domiciliary liquidator of a bank. Again, since contests over what state's law ought to govern the priority of claims usually arise only when creditors fear that nobody but priority claimants will be fully satisfied, the FDIC's assurance of payment to depositors should render such contests uncommon.

Therefore, if we were to decide that no bankruptcy chapter is needed for state banks, it would be largely because we believe, not that existing insolvency machinery is adequate, but that the problems which are likely to cause this machinery to break down will be prevented from arising by the operations of the FDIC, coupled with the activities of other supervisory authorities. In assessing the extent to which we ought to repose confidence in this belief, we should consider several gaps in the protection afforded by the FDIC.

First, almost five per cent of the nation's total banking assets and liabilities are still carried by uninsured banks over which the FDIC has no control and to whose depositors it owes no obligation. Second, a small percentage of every bank's liabilities is made up of non-deposit claims which do not fall within the FDIC insurance coverage. Finally, notwithstanding the high percentage of accounts which are fully protected by insurance, approximately forty-five per cent of the funds on deposit with insured banks are uninsured because carried in accounts which exceed the $10,000 insurance maximum. The FDIC does, of course, have some effect on these gaps: its existence promotes greater confidence in banks and thereby reduces the likelihood and severity of failure-causing runs; its payment of insured claims may prevent a worsening of the over-all governing provability and priority of claims may be less favorable to them. For a less earthy explanation of the inhospitable treatment accorded out-of-state receivers, see Goodrich, Conflict of Laws 585-586 (3d ed. 1949) and authorities there cited.

183. See 43 Fed. Res. Bull. 47 (1957). These assets and liabilities are carried by over 5 per cent of the nation's banks. See FDIC Ann. Rep. 3 (1955). The absence of FDIC supervision and coverage does not, of course, mean that these banks are moving inexorably to their doom. In fact, the record of failures among uninsured banks in recent years is quite favorable: from the beginning of 1951 to the end of 1955 only seven uninsured banks failed. See FDIC Ann. Rep. 161 (1955); id. at 165 (1954); id. at 131 (1953); id. at 139 (1952); id. at 187 (1951).

184. The total non-deposit liabilities of all insured commercial banks in the United States constituted 1.49 per cent of these banks' total liabilities (including capital accounts) at the end of 1955. See FDIC Ann. Rep. 145 (1955). The percentage increases with the size of the bank, ranging from 0.25 per cent for banks with deposits of less than $1 million to 2.46 per cent for banks with deposits of $500 million or more. Ibid. The percentages for insured mutual savings banks are somewhat lower. Id. at 159. While the percentages are small, the actual sums involved are rather substantial. Thus, at the end of 1955, non-deposit liabilities for all banks in the United States totalled $3,503,162,000; $3,562,435,000 of this was owed by insured banks. Id. at 124.

185. See note 177 supra.
economy and thereby reduce the likelihood that additional banks owing uninsured debts will fail; and when an assumption of deposits is arranged for a failing insured bank, claims will probably be paid in full even though not insured in full. Nevertheless, the gaps are not wholly closed, and since we can only guess about whether the operations of the FDIC and other governmental agencies will prevent widespread failures in an economic crisis or avoid the evils of fragmented insolvency administration if such failures do occur, it seems the better part of valor to take further precautions and provide more adequate insolvency machinery for state banks.

As with insurance corporations, a special bankruptcy chapter adapted to the special problems of insolvent banks seems the wisest course. Again, as with insurance corporations, among the important problems to be resolved will be the role to be assigned to existing administrative agencies and the extent to which state law dealing with such matters as priorities and special deposits should be respected. In order to preserve the best of existing procedures, it probably would be wise to provide that only the FDIC could invoke the Bankruptcy Act for insured banks, and that if the statute were invoked the FDIC would be appointed trustee. For uninsured banks, the possibility of permitting the statute to be invoked only by the state official charged with supervision of the bank involved should be seriously considered.

C. Building and Loan Associations.

Our discussion respecting banks is also largely applicable to building and loan associations. The insolvency administration of federal savings and loan associations, like that of national banks, is controlled by federal officials acting under federal law. As with national banks, then, the barriers to successful administration that face a state liquidator are avoided, and so there would seem to be no compelling reason to replace the present system with bankruptcy legislation. Similarly, the Federal Savings and Loan Insurance Cor-

186. See text at note 176 supra.
187. See text at notes 150-155 supra.
188. See 48 Stat. 133 (1933), as amended, 12 U.S.C.A. § 1464(d) (1957), vesting exclusive jurisdiction in the Federal Home Loan Bank Board to appoint "a Supervisory Representative in Charge, a conservator, or a receiver" of a federal association, requiring that the Federal Savings and Loan Insurance Corporation be appointed receiver when a receivership is deemed necessary, and empowering the Federal Home Loan Bank Board "to make rules and regulations for the reorganization, merger, and liquidation of Federal associations and for such associations in conservatorship and receivership and for the conduct of conservatorships and receiverships"; 48 Stat. 1260 (1934), as amended, 12 U.S.C. § 1729(b) (1952), dealing with the powers of the Federal Savings and Loan Insurance Corporation as receiver.
poration is a close analog of the FDIC, performing for building and loan associations approximately the same functions which the FDIC performs for banks.\footnote{8} The only important question remaining is whether state building and loan associations should be left outside the scope of bankruptcy because they typically operate within a narrow geographical area,\footnote{9} reducing the probability that problems of fragmented insolvency administration will arise. While diffusion of assets and liabilities is apt to be a minor problem for the liquidator...
of an insolvent building and loan association, it can occasionally be troublesome. Consequently, since we incur no disadvantage by bringing state building and loan associations under the Bankruptcy Act and some advantage will occasionally result, this exclusion too should be ended.

IV. CORPORATIONS THAT ARE NOT MONEYED, BUSINESS OR COMMERCIAL

The state classification test is little used in applying the exclusion from involuntary bankruptcy of corporations that are not moneyed, business or commercial. This is undoubtedly due in part to the fact that states do not usually have such a classification, but even when help can be found in state law, independent characterization is preferred. Perhaps the state classification test is eschewed in this area because the premise used to justify it for banks, insurance companies and building and loan associations—

191. See, e.g., Brashear v. Intermountain Building & Loan Ass'n, 109 F.2d 857 (9th Cir.), cert. denied, 311 U.S. 655 (1940). Insofar as the restrictive state legislation set forth in note 190 supra, falls short of the total bar imposed by New York, interstate activity by a building and loan association is still possible. Nor is the fifty-mile limit imposed by the Federal Savings and Loan Insurance statute a complete bar to interstate activity. Fifty miles can, of course, include part of a state other than that in which the association's principal office is located; dispensations from the fifty-mile limit can be obtained under the statute and regulations; and the restriction obviously is inapplicable to uninsured associations, which hold about ten per cent of the savings and mortgages of all operating associations in the country. See Federal Home Loan Bank Board Ann. Rep. 34 (1955).

192. No case on this subject relies solely on state classification and few rely at all. In the latter group fall Hoile v. Unity Life Ins. Co., 136 F.2d 133 (4th Cir. 1943); In re Michigan Sanitarium & Benevolent Ass'n, 20 F. Supp. 979 (E.D. Mich. 1937), appeal dismissed, 96 F.2d 1019 (6th Cir. 1938); In re Dairy Marketing Ass'n, 8 F.2d 626 (D. Ind. 1925). The test is expressly rejected in In re Wisconsin Co-op Milk Pool, 119 F.2d 999, 1002 (7th Cir.), cert. denied, 314 U.S. 655 (1941): "The state can not determine who shall be admitted to bankruptcy; that is the function of Congress. We can only inquire whether a corporation, whose powers are defined by the state statute, comes within the Congressional definition of those who may be declared bankrupts. Thus far and thus far only may we have reference to the Wisconsin statutes. . . . Federal legislation, in pursuance of the Constitution, determines whether an interest or right created by local law is within the federal law. The latter must prevail no matter what name is given the interest or right by the local law." Even one of the leading cases for the state classification test in the insurance context concedes that it would define "moneyed, business or commercial" by referring to the principal business conducted by the debtor. See Sims v. Fidelity Assur. Ass'n, 129 F.2d 442, 448 (4th Cir. 1942), aff'd, 318 U.S. 608 (1943) (dictum). 193. To the extent that bankruptcy courts have assumed that a corporation is not moneyed, business or commercial if it is a nonprofit enterprise, see text infra at note 210 and authorities there cited, a state classification may be found, since several kinds of corporations are typically styled nonprofit by state statute. See, e.g., the state statutes discussed in Hoile v. Unity Life Ins. Co., 136 F.2d 133 (4th Cir. 1943); Schuster v. Ohio Farmers' Co-op Milk Ass'n, 61 F.2d 337 (6th Cir. 1932).
Congress desired to leave the liquidation of these corporations to the states—is clearly inapplicable. If Congress had wished to leave the liquidation of corporations that are not moneyed, business or commercial to their home states, certainly the exclusion would have been extended to voluntary as well as involuntary bankruptcy. It seems likely that when Congress adopted this involuntary bankruptcy exclusion in 1910, it did so because it thought that corporations which were unconcerned with money, business or commerce should not have their laudable activities disrupted by liquidation at the instance of pestiferous creditors. Perhaps, too, the members of Congress felt that a remedy once thought of as the special province of blackguards, and occasionally still so regarded, ought not to be inflicted on such highminded enterprises. In short, Congress' purpose was not to leave the liquidation of corporations that are not moneyed, business or commercial to the states, but to give those corporations a dispensation from an unpleasant law designed for the self-seeking world of commerce and business.  

In view of the primacy of independent characterization in this area, we might expect to find some serious grappling with the problem of whether the powers or activities of a corporation should determine its characterization. In fact, this problem has received very little consideration. Almost all of the cases have involved corporations which did approximately what they were empowered to do;\(^{195}\) in the one case in which a corporation apparently did exceed its powers, the court, without explanation, relied on activities, to find that the debtor was moneyed, business or commercial.\(^{196}\) While no attempt was made to justify this conclusion, we submit that the case was correctly decided. If there is something especially meritorious about corporations that are not moneyed, business or commercial which justifies sparing them from involuntary bankruptcy, it must stem from their activities, for unused powers set forth in a corporate charter have no effect, beneficial or otherwise, on anybody.\(^{197}\)  

The basic problem remains: how have the courts defined "moneyed, business or commercial"? It will be recalled that the phrase first appears in the Act of 1867 in response to the fear that

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194. See text at notes 39-41 supra.  
195. See, e.g., Misso Homestead Ass'n, Inc. v. United States, 185 F.2d 280 (8th Cir. 1950); In re Michigan Sanitarium & Benevolent Ass'n, 20 F. Supp. 979 (E.D. Mich. 1937), appeal dismissed, 96 F.2d 1019 (6th Cir. 1938); In re Deauville, Inc., 52 F.2d 963 (D. Nev. 1931).  
196. In re Roumanian Workers Educational Ass'n, 108 F.2d 782 (6th Cir. 1940).  
religious, educational and eleemosynary corporations might be involuntarily adjudicated bankrupt if all corporations were made subject to bankruptcy.\textsuperscript{198} This bit of legislative history found favor with the courts, the following passage being rather typical of the language used in cases decided under the Act of 1867:

[S]uch private corporations as are ecclesiastical, or eleemosynary, or established for the advancement of learning, are clearly not made subject to the provisions of the act. . . . The words . . . "moneyed, business or commercial corporations," would seem to have been intended to embrace all those classes of corporations that deal in or with money or property in the transactions of money, business or commerce for pecuniary gain, and not for religious, charitable or educational purposes.\textsuperscript{199}

The cases decided since the 1910 resurrection of the "moneyed, business or commercial" clause have generally been faithful to Congress' indication that it was enacting that language as judicially construed under the Act of 1867.\textsuperscript{200} Thus, there is no doubt that any corporation which seeks to earn profits to be distributed to its stockholders is amenable to involuntary bankruptcy.\textsuperscript{201} The prevailing view treats agricultural marketing cooperatives the same way; that profits are distributed to producers, not on the basis of shares owned, but on the basis of the amount of business transacted with the organization does not negate the fact that the corporation is seeking financial gain for its members.\textsuperscript{202} It is equally clear that religious, charitable and educational corporations which do not engage in profit-making activity are not moneyed, business or commercial.\textsuperscript{203}

The law is not so clear when a religious, charitable or educational corporation carries on profit-making activity, even though it

\textsuperscript{198} See text at notes 5-8 supra.


\textsuperscript{200} See text at note 27 supra.

\textsuperscript{201} E.g., In re Deauville, Inc., 52 F.2d 963 (D. Nev. 1931); In re R. L. Radke Co., 193 Fed. 735 (N.D. Cal. 1911); Hoile v. Unity Life Ins. Co., 136 F.2d 133, 135 (4th Cir. 1943) (dictum); In re Wisconsin Co-op. Milk Pool, 119 F.2d 999, 1001 (7th Cir.), cert. denied, 314 U.S. 655 (1941) (dictum).

\textsuperscript{202} Missco Homestead Ass'n, Inc. v. United States, 185 F.2d 280 (8th Cir. 1950); In re Wisconsin Co-op. Milk Pool, supra note 201; Schuster v. Ohio Farmers' Co-op. Milk Ass'n, 61 F.2d 337 (6th Cir. 1932); In re South Shore Co-op. Ass'n, 4 F. Supp. 772 (W.D. N.Y. 1933); see Hanna, The Law of Cooperative Marketing Associations 339 (1931). Two earlier district court decisions are contra: In re Weeks Poultry Community, Inc., 51 F.2d 122 (S.D. Cal. 1931); In re Dairy Marketing Ass'n, 8 F.2d 626 (D. Ind. 1925).

\textsuperscript{203} E.g., In re Michigan Sanitarium & Benevolent Ass'n, 20 F. Supp. 979 (E.D. Mich. 1937), appeal dismissed, 96 F.2d 1019 (6th Cir. 1938); Missco Homestead Ass'n v. United States, supra note 202, at 282 (dictum); Schuster v. Ohio Farmers' Co-op. Milk Ass'n, supra note 202 at 338 (dictum).
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does so, not for the purpose of distributing gains to members, but for the purpose of supporting its non-profit activity. In re Michigan Sanitarium & Benevolent Association\(^{204}\) held ineligible for involuntary bankruptcy a hospital founded to care for indigents and for people who could afford to pay for treatment, the payments of the latter group to be used, together with gifts, solely to maintain and improve the institution. The court stated that, "There is no reason why a corporation, such as the respondent association here, should be held to be a business corporation merely because in the carrying out of its objects and purposes it performs business transactions, which are, however, not for any one's benefit or pecuniary gain."\(^{205}\)

On the other hand, a masonic lodge was held subject to involuntary bankruptcy because it derived substantial income from renting its lodge rooms to groups other than Masons.\(^{206}\) The court's approach is contrary to that employed in the Michigan Sanitarium case:

I am convinced that [the lodge] conducted a regular course of transactions for the purpose of making a profit out of them and that these transactions were on a sufficiently large scale and sufficiently numerous to make the bankrupt a business company. These transactions were of far more economic importance to the

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\(^{204}\) 20 F. Supp. 979 (E.D. Mich. 1937), appeal dismissed, 96 F.2d 1019 (6th Cir. 1939).

\(^{205}\) Id. at 982.

\(^{206}\) In re William McKinley Lodge, 4 F. Supp. 280 (S.D. N.Y. 1933).

The case is distinguished in In re Michigan Sanitarium & Benevolent Ass'n, supra note 204, on the ground that the William McKinley Lodge was "an unincorporated company." At the time In re William McKinley Lodge was decided, section 4(b) of the Bankruptcy Act provided that, "[A]ny unincorporated company, and any moneyed, business, or commercial corporation (except a municipal, railroad, insurance, or banking corporation, or a building and loan association) owing debts to the amount of one thousand dollars or over, may be adjudged an involuntary bankrupt. . . ." Since "moneyed, business, or commercial" modified only "corporation," and not "any unincorporated company," it can be argued that in order to adjudicate the William McKinley Lodge an involuntary bankrupt, the court did not have to decide whether or not it was moneyed, business or commercial. However, that the court did not regard its holding as so restricted is evidenced by its statement of the problem before it: "The only question argued was whether the bankrupt, an unincorporated company, was in business, so as to be included among the possible involuntary bankrupts." 4 F. Supp. at 283. There is ample precedent for this method of handling the definition of unincorporated company. See, e.g., In re Tidewater Coal Exchange, 280 Fed. 638, 643 (2d Cir.), cert. denied, 259 U.S. 584 (1922), in which the court held an unincorporated company subject to involuntary bankruptcy on the ground that it was a business or commercial enterprise, and stated that, "Whether an unincorporated company not organized for a business purpose can be adjudicated a bankrupt under the act is not before us and is not decided." The Chandler Act eliminated the phrase, "any unincorporated company," from section 4 of the Bankruptcy Act. 58 Stat. 845 (1938), 11 U.S.C. § 22 (1952). Since unincorporated companies were already included in the Act's definition of corporations, 44 Stat. 662 (1926), as amended, 11 U.S.C. § 1 (1952), there is no longer any doubt that an unincorporated company cannot be involuntary adjudicated bankrupt unless it is moneyed, business or commercial.
alleged bankrupt than the purely fraternal transactions which were more closely connected with the primary object of the association. The fact that such profit as the lodge might make from the business transactions was not intended to be divided among the members did not prevent the lodge from being a business association.207

The court did not say that the lodge's profit-making transactions were more important to it than its fraternal activities, but only that the profit-making transactions were of more economic importance, an observation that is likely to be true of most corporations which support their non-profit activities in part by a profit-making enterprise. Since, as we shall attempt to demonstrate, the exemption from involuntary bankruptcy of corporations that are not moneyed, business or commercial is unsound, the more restrictive interpretation of that exemption employed in the Masons case has a certain attraction. Nevertheless, because many corporations which Congress obviously intended to exclude from involuntary bankruptcy carry on incidental activity which results in profit (e.g., the church bazaar, the university bookstore), the approach of the Masons case probably has to be rejected as doing too much violence to Congress' purpose. Under the present law, profit-making activity probably should not subject a religious, charitable or educational corporation to involuntary bankruptcy unless the profit-making activity becomes the corporation's predominant pursuit.208

Different from the debtor which carries on both profit-making and religious, charitable or educational activity, but equally troublesome for the courts, is the debtor which does not seek financial gain for distribution to its members, but which cannot be regarded as primarily religious, charitable or educational either. The position that a debtor is not moneyed, business or commercial if it does not seek profits was taken in Hoile v. Unity Life Insurance Company,209 where the court said:

It is contended that Unity Life Insurance Company is a "moneyed, business or commercial corporation" because of the money and property which it owns and the moneys which it collects and pays out in benefits. But this contention is untenable because the phrase by judicial interpretation and reenactment has acquired a meaning which limits it to corporations organized for profit, and the facts in the pending case show that the debtor corporation was organized under the South Carolina statute "for

207. In re William McKinley Lodge, supra note 206 at 283.
208. See In re Roumanian Workers Educational Ass'n, 108 F.2d 782 (6th Cir. 1940).
209. 136 F.2d 133 (4th Cir. 1943).
the mutual benefit of its members and their beneficiaries and not for profit.\textsuperscript{210}

Other cases refuse to rely entirely on the profits vel non test, but do little to define "moneyed, business or commercial," except to indicate that it does not include religious, charitable and educational corporations. These decisions seem to assume that there are just some things that are unquestionably moneyed, business or commercial, and no articulation of what lies behind those words is necessary or, perhaps, even possible. Thus, an association organized at the instance of the federal government to expedite wartime coal shipments was held subject to involuntary bankruptcy notwithstanding the absence of any possibility of pecuniary profit to the association because, the court explained, the debtor was "engaged in the prosecution of a business enterprise, as distinguished from one which is charitable, or religious, or educational, or social."\textsuperscript{211} Similarly, a corporation formed for the sole purpose of liquidating the assets of an insolvent partnership was held to be moneyed, business or commercial, the court stating only that, "[T]here would

\textsuperscript{210.} \textit{In re} Elmsford Country Club, 50 F.2d 238 (S.D. N.Y. 1931). Since both \textit{In re} Weeks Poultry Community, Inc., 51 F.2d 122 (S.D. Cal. 1931), and \textit{In re} Dairy Marketing Ass'n, 8 F.2d 626 (D. Ind. 1925), proceeded on the assumption that agricultural cooperatives were non-profit enterprises and hence not subject to involuntary bankruptcy, they support the proposition set forth in the text. However subsequent decisions dealing with cooperatives have refused to follow these two cases. See note 202 supra.

\textsuperscript{211.} \textit{In re} Tidewater Coal Exchange, 280 Fed. 638, 643 (2d Cir.), \textit{cert. denied}, 259 U.S. 584 (1922). On the significance of the fact that the debtor was unincorporated, see note 206 supra. \textit{In re} Supreme Lodge of the Masons Annuity, 286 Fed. 180 (N.D. Ga. 1923), is more articulate than the other cases which attempt to define "moneyed, business or commercial," without reference to the profits test, but still does not take us very far towards a definition of general applicability. Regarding a nonprofit fraternal benefit society as moneyed, business or commercial because its activities partook too much of the nature of insurance, the court said, "It is a fair statement of the Georgia law that the conception of a fraternal and beneficial society has changed from that of benevolence to one of business; the business being insurance of a definite sort and separately regulated, but still insurance. When this company departed from the plan of raising a fund to be distributed to the aged and needy at the discretion of its governing body—this was Masonic benevolence—to a direct obligation to pay to persons chosen, not because of their need, but because of the relative unlikelihood of having to pay them at all, which is business, the realm of the social and charitable was left and that of selfishness entered; mutual insurance pure and simple was undertaken. Calling premiums dues and policies certificates does not alter the essence of the matter." \textit{Id.} at 187. Of course, the debtor was still not subject to bankruptcy because it was an insurance corporation. \textit{In re} Order of Sparta, 242 Fed. 235 (3d Cir. 1917), is in accord with \textit{In re} Supreme Lodge of the Masons Annuity in regarding a fraternal benefit society as a business enterprise when insurance is its predominant activity. The Order of Sparta was an unincorporated company, but in concluding that it ought to be adjudicated, the court proceeded on the same theory employed by the cases discussed in note 206 supra.
have to be business operations of some amount in order to liquidate the assets. ..."212

Because the cases to which Congress referred in 1910 typically spoke of profit-seeking corporations on the one hand and religious, charitable and educational corporations on the other,213 the legislative history does not resolve the problem of the corporation which is neither the one nor the other. Since our own view is that the exclusion of corporations that are not moneyed, business or commercial should be construed as narrowly as the legislative history permits, and since that history does not compel the conclusion that only profit-seeking enterprises are subject to involuntary bankruptcy, we prefer the cases which admit non-profit corporations to involuntary bankruptcy. This raises the question whether all corporations which are not religious, charitable or educational should be treated as moneyed, business or commercial. Occasional brief dicta under both the Act of 1867 and the amendment of 1910 support the view that social214 and literary215 associations are not moneyed,

212. In re Cochrane & Harper Securities Co., 27 F.2d 917, 919 (D. Mass. 1928). The notion that "moneyed, business or commercial" has content independent of the profit vel non standard is not confined to cases involving corporations that do not seek financial gain. It has been used, along with the argument that a debtor is moneyed, business or commercial if it seeks to earn profits, to buttress holdings that agricultural marketing cooperatives are subject to involuntary bankruptcy. Thus, in In re South Shore Co-op. Ass'n, 4 F. Supp. 772, 773 (W.D. N.Y. 1933), after listing the debtor's extensive powers, the court said: "If a 'business' corporation ... means a corporation organized for profit, the alleged bankrupt is not subject to the bankruptcy law. But the Bankruptcy Act says nothing about 'profits' in this connection. It is quite patent from the authority conferred by the statute that the alleged bankrupt is authorized to do 'business.' Clearly it is a business corporation in the sense that the word 'business' is ordinarily construed. ..." The court went on to point out and rely on the fact that the debtor was seeking financial benefit for its members. Accord, In re Wisconsin Co-op. Milk Pool, 119 F.2d 299 (7th Cir.), cert. denied, 314 U.S. 655 (1941); Schuster v. Ohio Farmers' Co-op. Milk Ass'n, 61 F.2d 337 (6th Cir. 1932); cf. In re Roumanian Workers Educational Ass'n, 108 F.2d 782 (6th Cir. 1940).

213. See text at notes 199-200 supra.

214. In re Tidewater Coal Exchange, 280 Fed. 638, 643 (2d Cir.), cert. denied, 259 U.S. 584 (1922) (dictum); In re Order of Sparta, 242 Fed. 235, 238 (3d Cir. 1917) (dictum); Alabama & C. R. Co. v. Jones, 1 Fed. Cas. No. 126, at 278 (S.D. Ala. 1871) (dictum). It can be argued that In re Elmsford Country Club, 50 F.2d 238 (S.D. N.Y. 1931), in which a corporation formed to operate a golf course for the pleasure of its members was held not to be moneyed, business or commercial, supports the proposition that social corporations are exempt from involuntary bankruptcy. However, the court rested its decision entirely on the premise that a corporation is not moneyed, business or commercial if it is not organized for financial gain. Since the court did not recognize the possibility that a nonprofit corporation might be moneyed, business or commercial, it did not have before it the question we are presently concerned with, viz., if some nonprofit corporations are subject to involuntary bankruptcy, which ought not to be?

215. Missco Homestead Ass'n, Inc. v. United States, 185 F.2d 280, 282 (8th Cir. 1950) (dictum); In re Deauville, Inc., 52 F.2d 963, 966 (D. Nev.
business or commercial. However, exclusion of these two types of corporation has never received the same extensive judicial approval that has been accorded the exemption of religious, charitable and educational corporations, and so the conclusion that they ought to be subject to involuntary bankruptcy would require no serious break with existing authority. In line, then, with our desire to limit the exclusion of corporations that are not moneyed, business or commercial, we would admit social and literary corporations to involuntary bankruptcy and exempt only those corporations which are religious, charitable or educational.

The ideal way to limit that exclusion would, of course, be to abolish it entirely. Congress never attempted to explain why religious, charitable and educational corporations should be exempt from involuntary bankruptcy and the only serious judicial attempt to do so comes off rather lamely:

The rule that an eleemosynary corporation, charitable and benevolent in character, not operated for pecuniary gain, is not a "business corporation" so as to be amendable to the provisions of the Bankruptcy Act on involuntary petition, is in accordance with good, sound, common sense. Congress saw fit to specifically except farmers and laborers from involuntary bankruptcy, and there is far less reason for its excepting laborers and farmers than for excepting an eleemosynary association . . . which, generally speaking, operates for the good of humanity without hope of private gain or reward to any individuals. All of the common-law remedies for the collection of debts are available to those who deal with farmers, laborers, and this kind of corporations. Congress desired to encourage persons philanthropically inclined to give their money and their time and services through an eleemosynary corporation in promulgating charitable and benevolent, philanthropic, and humanitarian doctrines . . .

Such a corporation fundamentally is entirely different from a business or commercial corporation. In one, a man invests his money and efforts so that he may share in its profits; in the other, he gives his money so that the objects and purposes of the corporation may be furthered. He receives in return no monetary interest in the corporation. In the first, the primary purpose is to conduct a business for the purpose of making money. In the second, the primary purposes are philanthropic, humanitarian, charitable, and benevolent in character. Not only are the purposes different, but the emphasis is likewise different. It is not easy to define this difference in words, but it stands out readily in one's mind, as it undoubtedly did in the minds of the courts in the cases cited above.

of the lawmakers... There are a variety of reasons, most of them apparent, why such a corporation should be specially dealt with.\footnote{216}

While the preceding passage is commendably pregnant with good will towards man, it offers little by way of solid argument in support of the exemption of religious, charitable and educational corporations from involuntary bankruptcy. That the court sees no good reason for excepting farmers and laborers from involuntary bankruptcy does not, of course, justify the existence of other exceptions. The notion that the ineligibility of eleemosynary corporations for involuntary bankruptcy influences in any way potential donors of time and money seems incredible to us.

The court's only other point is that creditors of the excluded corporations still have their common-law remedies for debt collection. Analysis of this argument, we think, reveals that it provides as much support for abolishing the exclusions as it does for continuing them. If Congress had succeeded in liberating religious, charitable and educational corporations from involuntary liquidation, the absence of a means to compel ratable distribution of an insolvent debtor's assets coupled with the power of individual creditors to reach those assets would encourage creditors to seek preferences, either by persuasion or by legal action, and the scramble could be stopped only by the debtor's invocation of the Bankruptcy Act. While reposing sole power in the debtor to call a halt would permit it to struggle on a bit longer than it otherwise might, this added life would probably be purchased at the cost of equal treatment of creditors. Consequently, those creditors who were slow to press hard for collection would wind up subsidizing the debtor's last days, a result at variance with the policy which underlies holding religious, charitable and educational corporations liable for their debts. It seems to us that once a debtor has become insolvent the only interests to be protected are those of creditors, unless there is a reasonable chance of revival. Surely, then, creditors should have the right to insist that the assets of the debtor be distributed equably. If there is a chance for revival, the arrangement and corporate reorganization provisions of the Bankruptcy Act can be used to continue the enterprise without sacrificing the interest of creditors in pro rata payment.

The foregoing argument is premised on the assumption that Congress achieved its apparent purpose to liberate religious, educa-

tional and charitable corporations from involuntary liquidation. To a considerable extent this assumption is unfounded. During the periods in which our country had no national bankruptcy law, a number of states enacted their own bankruptcy statutes, and while these statutes are universally regarded as suspended by the Bankruptcy Act for most purposes, some courts have held that the involuntary provisions of their local statutes are still applicable to debtors excluded from involuntary bankruptcy. Ironically enough, among the reasons commonly offered in support of this view is the argument that Congress could not conceivably have intended to leave creditors without the right to compel equal distribution of an insolvent debtor's assets. Other courts, probably more accurate in divining Congress' purpose in excluding certain debtors from involuntary bankruptcy only, have held their state bankruptcy statutes as inapplicable to these debtors as to those which are subject to both voluntary and involuntary bankruptcy. However, that credi-

217. For a list of states having insolvency laws which embody many of the features of the Bankruptcy Act, see 5 Remington, Bankruptcy § 2108 (5th ed. 1953).


219. E.g., Pitcher v. Standish, 90 Conn. 601, 98 Atl. 93 (1916); Old Town Bank v. McCormick, 96 Md. 341, 53 Atl. 934 (1903); Lace v. Smith, 34 R.I. 1, 82 Atl. 268 (1912). Additional authorities are collected in Annot., 1917 A.L.R. 109. The cases on this subject typically involve involuntary proceedings against a farmer, and, in fact, we have been able to find no post-1910 cases which decide whether the involuntary provisions of a state insolvency law otherwise suspended by the Bankruptcy Act remain operative as to a charitable, religious or educational corporation. Nevertheless, the rationales of the cases permitting farmers to be involuntarily adjudicated under state law are equally applicable to all of the debtors excluded solely from involuntary bankruptcy. Cf., State Nat. Bank v. Syndicate Co., 178 Fed. 359 (W.D. Ark. 1910); R. H. Herron Co. v. Superior Court of City and County of San Francisco, 136 Cal. 279, 68 Pac. 814 (1902); Rogers v. Boston Club, 205 Mass. 261, 91 N.E. 321 (1910).

220. See, e.g., Pitcher v. Standish, supra note 219, at 609, 98 Atl. at 96: "[In the absence of involuntary proceedings, creditors] are left to the ordinary, and frequently inadequate, machinery of the law or the debtor's volition for their protection. They are powerless to compel an equal distribution of his assets among them. . . . They cannot secure it against his will. We can hardly assume that Congress intended to deprive creditors of that right, generally if not universally accorded to them by the states. . . . We can more readily believe that Congress deemed it wiser that Federal jurisdiction be not assumed in the matter of proceedings in invitum, and that such action be left for State regulation. . . ."

221. Closser v. Strawn, 227 Fed. 139 (D.C. Pa. 1915); Littlefield v. Gay, 96 Me. 422, 52 Atl. 925 (1902); Adrian State Bank v. Klinkhammer, 182 Minn. 57, 233 N.W. 588 (1930), 15 Minn. L. Rev. 582 (1931); see Williston, The Effect of a National Bankruptcy Law Upon State Laws, 22 Harv. L. Rev. 547, 549-555 (1909); Comment, (1938) Wis. L. Rev. 302. The Supreme Court of the United States has never passed on whether a state may enact bankruptcy statute for debtors eligible for voluntary, but ineligible for involuntary bankruptcy. The statement in International Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929), that, "States may not pass or enforce laws to inter-
tors of the excluded corporations have no local bankruptcy act to which they can resort in the latter group of states and in states which have no bankruptcy statute does not necessarily mean that they are impotent to compel liquidation or rehabilitation of a religious, charitable or educational corporation. The existence of the Bankruptcy Act does not prevent liquidation or rehabilitation of a troubled corporation via an equity receivership, nor does it suspend a statute which can be construed as being merely in aid of the equitable remedy. In addition, statutes in some states confer on creditors the right to sue for the dissolution of an insolvent corporation, and, as an incident to the termination of the corporation's existence, its assets will be liquidated and the proceeds distributed to

fere with or complement the Bankruptcy Act or to provide additional or auxiliary regulations," supports the position taken by the authorities cited in this note, but nothing in the opinion indicates whether the Court had in mind the problem under consideration here when it uttered that statement. Furthermore, the Court's later decisions in Pobreslo v. Joseph M. Boyd Co., 287 U.S. 518 (1933), and Johnson v. Star, 287 U.S. 527 (1933), demonstrate quite clearly that the dictum in Pinkus overstates the limitations on state action in the bankruptcy field. For discussion of the general problem of what provisions in a state statute will or should result in suspension by the Bankruptcy Act, see, e.g., Glenn, Liquidation 208-213, 304-308 (1935); Miller, The Illinois Business Corporation Act and Bankruptcy Legislation, 29 Ill. L. Rev. 695 (1935); Radin, The Nature of Bankruptcy, 89 U. Pa. L. Rev. 1 (1940).

222. E.g., Stevens v. Carolina Scenic Stages, 208 F.2d 332 (4th Cir. 1953), cert. denied, 347 U.S. 917 (1954); In re Schwartz Bros., Inc. 58 F. Supp. 761 (D. Minn. 1945), 30 Minn. L. Rev. 638 (1946); Hazelwood v. Olinger Bldg. Department Stores, Inc., 205 Wis. 85, 236 N.W. 591 (1931). See note 136 supra for discussion of the authorities on whether a receiver will be appointed over a debtor's objection if the petitioning creditor is unsecured and has not recovered judgment and had execution returned unsatisfied.

223. A Minnesota statute which only slightly embroidered the equity receivership was sustained in In re Schwartz Bros., Inc., 58 F. Supp. 761 (D. Minn. 1945), 30 Minn. L. Rev. 638 (1946), the court concluding, at 766, that, "[W]here the state law has no other bankruptcy attributes but a distribution of the assets in sequestration proceedings, where a solvent as well as an insolvent corporation may be proceeded against by a creditor, and where it fairly appears that the statute was merely enacted for the purpose of aiding a court of equity in carrying out its inherent equitable powers, the absence of a discharge provision in the statute under such circumstances is highly significant." A similar approach was employed to sustain a more elaborate Wisconsin statute in Hazelwood v. Olinger Bldg. Department Stores, Inc., 205 Wis. 85, 236 N.W. 591 (1931), but the Court of Appeals for the Tenth Circuit refused to accept a similar argument in striking down a rather mild New Mexico statute in First Nat. Bank in Albuquerque v. Robinson, 107 F.2d 50 (10th Cir. 1939). The more elaborate the statutory scheme, the greater the likelihood that a court will refuse to view the statute as merely in aid of the equitable remedy and will hold the statute suspended by the Bankruptcy Act. See, for example, the involuntary provisions of the Wisconsin statute which were recently treated as suspended in In re Wisconsin Builders Supply Co., 239 F.2d 649 (7th Cir. 1955). And, of course, an express provision for discharge of the debtor is certain to result in either suspension of that provision or of the whole statute. E.g., Pobreslo v. Joseph M. Boyd Co., 287 U.S. 518 (1933) (dictum).
creditors. The authorities are divided on whether such statutes are suspended by the Bankruptcy Act.

Since state law will often give creditors some sort of remedy to compel liquidation or rehabilitation of a religious, charitable or educational corporation, the picture we painted earlier of creditors powerless to compel a fair distribution of their insolvent debtor's assets is obviously overdrawn. Nevertheless, it is substantially more difficult to force a religious, charitable or educational corporation into insolvency proceedings than would be the case if these associations were subject to bankruptcy: many states do not have insolvency laws; others have such laws but hold them suspended even as to debtors exempt from involuntary bankruptcy; many states will not grant an equity receivership on petition of a creditor who has not yet recovered judgment; some states do not permit dissolution of a religious, charitable or educational corporation on petition of a creditor, and some others require the petitioning creditor to recover judgment first. Furthermore, the remedies offered by the states as a substitute for involuntary bankruptcy are not nearly so effective as the Bankruptcy Act in insuring equal treatment of creditors. For example, a state remedy may provide no way to set aside preferences made shortly before the commencement of the proceeding. In addition, if an excluded corporation operates across state lines, the problems of interstate insolvency administration discussed earlier are likely to be present. There is no reason to put up with these disadvantages. While it can at least be argued, though unpersuasively we think, that insolvency administration of banks, insurance corporations and building and loan associations can be handled best by the state authorities which supervise those organizations during their business lives, the absence of comparable state supervision of religious, charitable and educational corporations


226. See text at notes 130, 162-163 supra.

227. See text at note 55 supra.
renders even this argument unavailable on behalf of their exemption. 

In sum, the exclusion from involuntary bankruptcy of corporations that are not moneyed, business or commercial makes unfair treatment of creditors possible, and neither facilitates the operation of such enterprises during their lives nor achieves the soundest administration of them when they become insolvent. This exclusion should be abolished.

V. Conclusion

Insolvency can afflict any sort of enterprise that incurs debts, and when it does, the stricken corporation and its creditors obviously should have available the most helpful remedy our legal system presently offers. We have attempted to demonstrate that this principle is violated by the exclusion from involuntary bankruptcy of corporations that are not moneyed, business or commercial, and by the complete exclusion from bankruptcy of insurance corporations, state banks and state building and loan associations. The situation with respect to corporations that are not moneyed, business or commercial can most easily be corrected. Since there is no reason why such corporations should not be subject to involuntary bankruptcy like any other corporation, all that is needed is an amendment to section 4b of the Bankruptcy Act, striking the words, "moneyed, business or commercial." The solution for insurance companies and state banks and state building and loan associations is more complicated. The operations of these debtors are sufficiently different from those of most other corporations, and from those of each other, to make it inadvisable to simply bring them under the straight bankruptcy and corporate reorganization provisions. We suggest, therefore, that special bankruptcy chapters, dealing with the special problems of these corporations, be adopted.