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EQUITY'S JURISDICTION OF CHATTEL MORTGAGES

Chattel mortgages are an ancient field of equity jurisdiction. Statutes have regulated priority; they have created rules regarding recording and renewal. But the relation between the chattel mortgagor and mortgagee has long been and continues a province of equity jurisdiction. The growth of the jurisdiction is best indicated by an analysis of the legal basis of chattel mortgages. At law the mortgagor conveys a legal title in the property to the mortgagee which is absolute but this title returns to the mortgagor on the condition of payment by him of an indebtedness at an agreed time. In *Hughes v. Harlam*¹ the Court of Appeals of New York stated the legal rule in these words:

“When the security consists of personal property the instrument pledging it as security for a loan operates to transfer the legal title to the mortgagee, to be defeated only by the full performance of the condition; or as it is expressed by Beardsley, J., in the old case of *Charter v. Stevens*, 3 Denio 33, the mortgage transfers ‘a defeasible title to the property mortgaged.’ The mortgagor can revest himself by complying with the conditions of the defeasance, but, if he fails to do it, he has no remedy at law.”

At law, failure to comply with the conditions results in forfeiture. Equity, as a general rule, relieves from forfeitures, under certain conditions, and this power gave equity courts a basis of jurisdiction over chattel mortgages, which was stated and applied by the New York Court of Appeals in *Hughes v. Harlam*. In a court of law the mortgagor's rights are ended on the failure to pay at the time agreed. The mortgagee's estate was absolute at the making of the mortgage, and on default the reversion lapses. But equity says that upon certain conditions the mortgagor may still avoid the forfeiture and redeem. In *Hughes v. Harlam* the New York Court of Appeals said:

¹ 166 N. Y. 427, 432, 60 N. E. 22, 24 (1901). See, also, *Darrow v. Wendelstadt*, 60 N. Y. S. 174, 43 Am. Dec. 426 (1899).

"Courts of equity, however, long ago decided that a mortgagor so situated might be permitted to redeem."

The conditions that govern this right to redeem are several. They do not require tender of the sum due.² As one case says, the tender only bears upon the plaintiff's (mortgagor's) willingness to do equity. The suit in equity for redemption permits a computation of the amount due with interest and the decree directs payment as a condition of redemption and failure to make the payment results in a decree of foreclosure. The suit in equity must be brought promptly. It must be free from laches. It must be brought before the right of redemption is cut off by a valid sale by the mortgagee. The mortgagee upon default may cut off the equitable right of redemption by one of two possible proceedings, that is, by a sale conducted in good faith or by a foreclosure suit in equity brought by the mortgagee.³ If the mortgagee elects to proceed by sale to cut off the equity of redemption, he does not, by the process of conducting a sale, put himself or the mortgage beyond the range of an equity court. Equity still retains the right to examine the nature of the sale and its good faith. In *Freeman v. Freeman*⁴ the New Jersey Court of Chancery has stated this power in these words:

"A sale of the chattels by a mortgagee or pledgee, in the absence of statutory regulations, is attended with some difficulty and embarrassment. The conduct and fairness of the sale, and the rights acquired under it, are always open to investigation at the instance of the mortgagor or pledgor. *Morris Canal and Banking Co. v. Fisher*, 1 Stockt. 667, 687-9; *Same v. Lewis*, 1 Beas. 323."

With respect to the sale, equity requires the exercise of good faith. It has no set regulations and the cases are the only guide as to what equity deems good faith. There is no rule as to advertising or notice but if the seller undertakes

² *Bernheimer & Schwartz Pilsner Co. v. H. Koehler Co.*, 42 Misc. Rep. 377, 86 N. Y. S. 716 (1904).

³ *Freeman v. Freeman*, 17 N. J. Eq. 44 (1864).

⁴ *Op. cit. supra* note 3, at 47.

to give such notice it must be reasonable.⁵ The property must be in the view of the bidders at the time of sale and must be sold in such lots as will bring the best price.⁶ The mortgagee may become the purchaser but the price must be fair.⁷ The purpose of the sale is to ascertain and estimate value, and courts of equity insist upon sales of such a character as to fulfill that function; and equity finds its guide as to reasonableness in a rule of the common law with respect to judicial sales. Such was the rule adopted and applied in *Sherman v. Slayback*.⁸ Sales conducted by mortgagees against mortgagors in distress and which are part of a scheme to deprive the mortgagor of a part of the property to the mortgagee's benefit are within the equity jurisdiction and voidable under the rules laid down in the cases cited. If the mortgagee relies upon an agreement with the mortgagor under which and in execution of which such sales are held, the agreement may be examined by equity and voided along with the sale under the equitable rules covering the preservation of the equity of redemption.

Before discussing the nature of the equity of redemption, the rule of waiver⁹ may be noted with respect to both forfeiture and sales. Waiver is a rule of equitable nature, but with respect to chattel mortgages it is applied by courts of law as well as those of equity. There are some old cases decided as law actions which state the rule with the sharpness and clarity of lightning. In *Charter v. Stevens*¹⁰ Beardsley, J., wrote:

"It has been adjudged that a tender of the mortgage money, after default in payment, would not, at law, re-invest the mortgagor with

⁵ *Morrisania Laundry Service v. Strauss*, 137 Misc. Rep. 48, 242 N. Y. S. 579 (1930); *Fleischmann v. Clausen*, 225 N. Y. S. 288, 222 App. Div. 7 (1927).

⁶ *Sherman v. Slayback*, 58 Hun. 255, 12 N. Y. S. 291 (1890).

⁷ *Casserly v. Witherbee*, 119 N. Y. 522, 23 N. E. 1000 (1890).

⁸ *Op. cit. supra* note 6.

⁹ As stated in *Taylor v. Goelet*, 208 N. Y. 253, 101 N. E. 867, Ann. Cas. 1914D, 284 (1913).

For an application of the rule to chattel mortgages, see *Hutchings v. Munger*, 41 N. Y. 155 (1869).

¹⁰ 3 Den. 33, 35 (1846). This case is quoted as an authority in *Hughes v. Harlam*, 166 N. Y. 427, 432, 60 N. E. 22, 24 (1901).

his former title to the property; *Patchin v. Pierce* [12 Wend. 61 (1834)] . . . and [*Brown v. Bement and Strong*] 8 John. 96 [1811]; but an acceptance of the amount tendered, that is, full payment being made, at any time, would, as between mortgagor and mortgagee, extinguish all right and interest of the latter in the property mortgaged. If made before the pay day had passed, it would satisfy the conditions on which the property had been transferred, and thus defeat it altogether; and, if made after forfeiture, it would be conclusive evidence the forfeiture had been waived, and that all right under the mortgage was extinguished." *Patchin v. Pierce, supra*; *Parks v. Hall*, 2 Pick. 206, 210, 211 [1824]; *Barry v. Bennett*, 7 Metc. 354, 360, 361 [1844]; *Hatch v. White*, 2 Gall. 152 [1814]."

There are several similar decisions at law with respect to waiver.¹¹ In equity upon payment the mortgagee becomes a trustee and is bound to account to the mortgagor¹² and the result of waiver operating by payment arises in a different way and as if in different dress. In *Earle v. Gorham Manufacturing Co.*¹³ equity applied the usual rule of waiver with respect to installment payments under a chattel mortgage holding that when the mortgagee accepts an overdue installment he obliterates the forfeiture and restores the previous status.

Equity has another field of jurisdiction with regard to chattel mortgages. This might be described as an inherent jurisdiction. It is founded in the very nature of the transaction. Like a red twine it runs through the entire cord. It is so mixed with the substance it may not be refined from it. Lord Eldon said: "You shall not by special terms, alter what this court says are the special terms of that contract."¹⁴ It is expressed in the aphorism: Once a mortgage always a mortgage. If the conveyance or assignment was a mortgage in the beginning the right of redemption is an inseparable incident and cannot be restrained or clogged by agreement.

¹¹ *Barry v. Bennett*, 7 Metc. 354 (1844); *Hutchings v. Munger, op. cit. supra* note 9; *Patchin v. Pierce*, 12 Wend. 61 (1834); *West v. Crary*, 47 N. Y. 423 (1872).

¹² *Charter v. Stevens, op. cit. supra* note 10.

¹³ 2 App. Div. 460, 37 N. Y. S. 1037 (1896).

¹⁴ *Seton v. Slade*, 7 Ves. Jun. 265, 273, 32 Eng. Rep. 108, 111 (1802).

The rule may be made clear by an analysis of one of the old cases which sustain it. In *Clark v. Henry*,¹⁵ an equity action, we find this statement of facts and finding: Henry purchased of Clark a span of horses and a wagon for \$285 which was to be paid on January 1, 1820. It was not paid, and on February 16, 1820, Clark asked for security and took an assignment of a bond and mortgage upon real property as security. Henry filed a bill in equity to redeem. The answer set up the assignment of the mortgage was absolute, that Henry not having funds to pay had *executed an agreement that the assignment would become absolute if the money was not paid by October 1, 1820*. The chancellor held the bond and mortgage were assigned by way of mortgage and any agreement that the assignment was to be an absolute sale, without redemption upon default of payment, was oppressive, illegal and void, and that the equity of redemption still existed in the plaintiff notwithstanding such agreement. Upon appeal the judgment was affirmed, Woodworth, J., saying:

"The right to redeem is carefully protected by courts of equity. They will not suffer an agreement to prevail, that the estate shall become an absolute purchase in the mortgagee, upon any event whatever. The reason of the rule is, because it puts the borrower too much in the power of the lender, who, being distressed at the time, is generally too much inclined to submit to any terms. There is no exception to the rule 'once a mortgage, always a mortgage.' (1 Madd. 413). No agreement of the parties can affect the doctrine as to redemption in a court of equity."

This rule precludes all covenants in the chattel mortgage whereby the mortgagor surrenders the right to redeem. In *Mooney v. Byrne*¹⁶ the Court of Appeals of New York says:

"The right to redeem is an essential part of a mortgage, read in by the law, if not inserted by the parties. Although many attempts have been made, no form of covenant has yet been devised that will cut off the right of a mortgagor to redeem, even after the law day has long passed by. (*Clark v. Henry*, 2 Cow. 324, 331; *Jones, Mortg.* § 1039.)"

¹⁵ 2 Cow. 324 (1823).

¹⁶ 163 N. Y. 86, 92, 57 N. E. 163, 165 (1900).

The extent of this jurisdiction of equity is further shown by its approval by the Supreme Court of the United States in *Peugh v. Davis*.¹⁷

While the inception of this jurisdiction rests in the idea that what is given by way of security may not be treated by the taker as absolute nevertheless it rests also in the more persistent right of redemption which is branded into the transaction by equity so that it becomes, in the words of Lord Eldon, "the special terms of the contract." Agreements between the mortgagor and mortgagee, made after the contract of chattel mortgage, are, also, within its orbit. *Clark v. Henry* is an example. At no place in the course of the relationship may the mortgagee, by contract, and by "friendly" sale, escape beyond the jurisdiction. In *Peugh v. Davis* the Supreme Court of the United States wrote with respect to releases subsequent to the mortgage:

"A subsequent release of the equity of redemption may, undoubtedly, be made to the mortgagee. There is nothing in the policy of the law which forbids the transfer to him of the debtor's interest. The transaction will, however, be closely scrutinized, so as to prevent any oppression of the debtor. Especially is this necessary, as was said on one occasion by this Court, when the creditor has shown himself ready and skilful to take advantage of the necessities of the borrower. *Russell v. Southard* [12 How. 139 (1851)]. Without citing the authorities, it may be stated, as conclusions from them, that a release to the mortgagee will not be inferred from equivocal circumstances and loose expressions. It must appear by a writing importing in terms a transfer of the mortgagor's interest, or such facts must be shown as will operate to estop him from asserting any interest in the premises. The release must also be for an adequate consideration; that is to say, it must be for a consideration which could be deemed reasonable if the transaction were between other parties dealing in similar property in its vicinity. Any marked undervaluation of the property in the price paid will vitiate the proceeding."

The jurisdiction of equity, when once established, is equal to the purpose of affording full relief. If the mortgagor establishes his right to an accounting and the mort-

¹⁷ 96 U. S. 332, 337 (1877). See, also: *Conover v. Palmer*, 123 App. Div. 817, 108 N. Y. S. 480 (1908); *Hughes v. Harlam*, *op. cit. supra* note 10; *Casserly v. Witherbee*, *op. cit. supra* note 7.

gagee has sold, lost or otherwise converted the chattels, the court may make reparation in damages.¹⁸ The theory of accounting on the basis of value is followed. The mortgagor may not compel the mortgagee to purchase at a price. The same theory of value applies if the mortgagee after an alleged seizure retains the chattels for his own use. If after proper seizure he seeks to collect the indebtedness he must credit the mortgagor with the value at the time of seizure and the indebtedness is reduced by that value.¹⁹ If the value is less than the indebtedness, the balance may be recovered; if it is greater, the surplus must be accounted for to the mortgagor. The mere seizure does not in itself discharge the indebtedness; this is controlled by the rule of value.

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¹⁸ *Stoddard v. Denison*, 38 How. Prac. 296, 307 (1872); *Flanders v. Chamberlain*, 24 Mich. 305, 321 (1872); *Blodgett v. Blodgett*, 48 Vt. 32, 34 (1875).

Equity practice also differs from legal practice in that equity looks to conditions at the close of the trial rather than beginning of the action, *Haffey v. Lynch*, 143 N. Y. 241, 248, 38 N. E. 298, 299 (1894).

¹⁹ *Harrison v. Hall*, 239 N. Y. 51, 145 N. E. 737 (1924).