New Jersey Court of Errors and Appeals

Heard Below before CHURCH, *V. C.*

PAUL MULLER, Receiver in Bankruptcy of the Hamilton Warping and Winding Co., Inc., a corporation, Complainant-Appellee, vs. BERNARD SCHRAM and ANNA SCHRAM, his wife, IRVING SIROTA and LOTTIE SIROTA, his wife, Defendants-Appellants.	On Appeal from the Court of Chancery.

BRIEF OF APPELLANTS.

This is a bill brought by the Receiver of a Bankrupt Corporation against its former officers, Bernard Schram and Irving Sirota, and Anna Schram and Lottie Sirota, their wives, to have impressed a trust on certain lands situated in the City of Paterson, N. J., which now appears to have title in the aforementioned wives.

It is alleged that the officers, in the months of October and November of the year 1922 took funds and moneys of the said corporation aggregating $2500.00 and for it purchased certain premises, known as #161 Godwin Street, Paterson, N. J., taking title thereto in the names of their wives. The property was purchase on November 27th, 1922, and the corporation filed

a petition in bankruptcy on May 22, 1924, approximately two years later.

There is no allegation in the complaint setting up fraud on the part of the defendants nor is there any allegation to the effect that the corporation was insolvent at the time the funds were withdrawn. The bill prays for a decree.

> "* * * adjudging and determining that said defendants hold said real estate in trust for said Bankrupt (Corporation) and that the said Bankrupt is the beneficial owner of said lands and premises, and that said defendants may be decreed to hold the title to said lands and premises in trust for complainant, said bankrupt and said creditors * * *"

In other words, complainant is seeking to impose a ~~constructive~~ RESULTING trust upon these premises, to the extent, at least, of the moneys of the corporation therein represented.

Defendants oppose such a decree because there is no basis for declaring a ~~constructive~~ RESULTING trust to exist either as a matter of fact or as a matter of law.

POINT I.

The Court erred in decreeing that the defendants hold the land in trust for the complainant because the facts do not support such a decision.

There is no dispute as to the sum of $250 being withdrawn on October 21st, 1922, by the officers in question nor is the withdrawal of $2250 of November, 1922, contradicted. It is the reason for these withdrawals as explained by the accountant, Nathan Magill, that conflicts

with the contention of the complainant. Complainant relies on the fact that the withdrawals were loans made by the officers to themselves without any authorization and that that being illegal, a trust of necessity must follow assuming that they can be traced.

In attempting to show that these withdrawals were loans, complainant called on a witness, Nathan Magill, who at one time was the accountant for the defunct corporation. His testimony, as that of an expert and as one who is familiar with the transactions in question shows that the terminology in the books of account were not actually the circumstances as they existed but that withdrawals which were in effect, salaries to the officers were accounted for as loans to members simply for the purposes of increasing the assets in the balance sheet.

At this point it might be noted that the complainants are not proceeding on the theory of fraud but rely solely on the implication that the law draws from the transaction. There is nothing that prevents one from carrying on his books in his own particular fashion, and whether or not one calls sheep, sheep, or sheep, goats it is the actual facts that will govern and not the mere misnomer.

The situation was amply and fully explained by the complainant's own witness whose testimony appears more fully on page 30 of the state of the case.

On direct examination by Mr. Bilder:

> "Q. What is the meaning of the words 'Loans to members receivable', which is embodied in the entry of October 21st, which you have read on Page 103, of Ex. C-5. A. Well, that would be a rather

lengthy explanation, it seems to me; if you want me to go through it I could explain it.

Q. As an accountant, what is the expert meaning of that?

Mr. Weinberg: I object to the version as an accountant.

The Court: Well, let us see what he says.

A. You see, there are times when these members took loans, took money from the corporation, which should have been salaries, and charged it as a loan, the simple reason being,—I don't know, I never questioned them, I suppose is to show by withdrawing money from the corporation which they were entitled to as salaries, it might reduce the assets of the corporation to some extent, and they felt that they wanted to show everything on the books."

And at page 69, defendant, Schram, also called as a witness by complainant, was asked on cross-examination by his counsel:

"Q. At the time this property was bought by your wives, was your company in solvent condition? A. Yes, sir."

"Q. And is it a fact that when you withdrew moneys from the company speaking now with regard to the item of two hundred and fifty dollars and the item of $2,250, that you withdrew that money as part of the salary and wages then due and part that might become due to you for salary and wages? A. Yes, sir."

The answers given by these two witnesses called by the complainant to prove his case was the only evidence offered on his behalf.

And at page 59, Vera F. Hirsch, Cross. Mrs. Hirsch was the stenographer who took the depositions before the Referee in Bankruptcy.

Through her some of the depositions were offered in evidence.

> "Q. Page 39: 'With the money you took out of the corporation and gave them? A. We didn't take out any money from the corporation'. A. Yes, sir.
>
> Q. At page 19, the following question and answer appeared, did they not: 'Q. Who went and paid the last interest? A. My wife and his wife.' Is that correct? A. Yes, sir.
>
> Q. At page 36, the following question is asked of Irving Sirota and the answer appearing thereto: 'Cover what? A. Our wages'? A. That is right.
>
> Q. Page 37: 'It was put in the books as money borrowed from the corporation, wasn't it, you got the money and never paid it back? A. Yes, sir; the book shows we didn't pay it back, we were not supposed to pay it back.
>
> Q. Why were you not supposed to pay it back? A. It was coming to us. Q. For what? A. Wages'? A. That is right."

This was the testimony of Schram sworn before the Referee.

Thus the evidence elicited from three sources, tapped by complainant, shows that these withdrawals were proper. It will be answered that these replies came from hostile parties. That, we contend, makes no difference. Complainant brought the answers out and they must be given weight. If weight *is* given to them, it appears that these withdrawals were perfectly proper and no attack can successfully be made thereon. However, should the Court say they were not proper, what consequence can attach thereto? Surely not that attempted by complainant.

In considering the legal significance of the facts under consideration, it should be remembered throughout that each step presents a distinct and separate situation with certain equitable doctrines applicable to each. To analyze the situation, it seems appropriate at this time to consider the entire circumstances as divided into two fixed transactions. One concerns the withdrawal of the moneys from the corporation and whatever legal construction will be placed upon that, and the other, the passing of certain moneys from the husbands to the wives and then their respective purchase of the realty. So that, before we can actually consider that a resulting trust is established, it is essential that a presumed intent commencing with the corporation and running through the entire transaction be found to exist, that the moneys were in fact to belong to the corporation and not to the wives.

The doctrine of resulting trusts is based on the presumption that the one who parts with the property expects a return and it is this which the Court must find before it is able to create a trust.

Our contention, as illustrated by the testimony previously quoted at length, tends to show that the moneys withdrawn from the corporation were paid out by it to the individual members, Schram and Sirota with no expectation of ever receiving a return thereof for the reason that they were considered as salaries. In the lower court and in the opinion of the Vice Chancellor, from which we are taking an appeal, the contention is made that the complainant in the suit below, the trustee in bankruptcy, does

not represent the creditors, but is merely acting in the stead of the corporation.

If such are the facts, and it further appearing that this action is not brought on the theory of fraud or on the allegation that the moneys were withdrawn to the prejudice of creditors, then it follows that there can be no contradiction of the statements of the officers as to the reasons for these withdrawals and it cannot be contended that these withdrawals were not legal or were not deserving for all the rules and regulations of the corporation were complied with and there is no testimony to the effect that they were improper withdrawals or that the corporation was not financially able or was insolvent so that the action was illegal.

On page 68 of the state of the case, Schram, on cross-examination answered as follows:

> "Q. Who owns that property? A. Our wives, Mrs. Schram and Mrs. Sirota.
>
> Q. Did you ever have any interest in that property at all? A. Never.
>
> Q. Did you or the company ever have any title to that property? A. No.
>
> Q. Mr. Schram, who collected the rents, paid the bills for the carrying of that property, all along from the time it was bought down to date? A. Our wives.
>
> Q. Who paid the interest on the mortgage? A. Our wives. * * *
>
> Q. And who collected the rent from the tenants? A. Our wives. * * *
>
> Q. *At the time this property was bought by your wives, was your company in a solvent condition?* A. *Yes, sir.*
>
> Q. *Was every creditor, in fact, paid whom you had?* A. *Yes, sir.*"

This evidence that the corporation was solvent and that all creditors were paid at the time

that the money was withdrawn is absolutely uncontradicted at any point in the record. None of the creditors, who claim to be represented by the complainant in this litigation, therefore, were in existence at the time these withdrawals took place. The bankruptcy of the corporation occurred a year and one-half later. As to creditors who were in existence at the time of the withdrawals they cannot complain as they were all paid. Present creditors would have to show an actual fraudulent intent towards them if we assume for the moment that the officers acted contrary to law.

In the *Foss* case, reported in 147 Fed. 790, a bankrupt conveyed certain real estate to his wife but at the time was solvent and he soon thereafter began to keep a liquor saloon. It was there held that a trust could not be established without some affirmative testimony showing an attempt to commit fraud under the Bankruptcy Act, and the Court there held that it would not find that a resulting trust arose in favor of the creditors of the bankrupt even though the purchase money was paid by the husband. The Court held as follows:

> "I find that all the testimony in the record, taken together, proves that the real estate was the property of Mrs. Foss. Whatever consideration for the purchase price of the real estate proceeded from the husband was paid while he was free from debt; and the transactions between the husband and wife clearly import a promise by him to repay her any sums of money which she advanced in his behalf.
>
> "* * * I have examined the testimony with great care upon this point and must come to the conclusion that all the testi-

> mony taken together falls far short of proving such resulting trust to the husband. So far as we have to do with consideration which proceeded from the bankrupt when he was free from debt, I must find that the deed to his wife constituted a voluntary settlement upon her, which cannot now be disturbed in bankruptcy."

In the case at bar there appears no testimony to establish that these moneys were withdrawn for any other purpose than salaries. And we maintain as a matter of law that complainant is estopped to deny that fact insofar as he has not proceeded on the theory of fraud. A resulting trust arises by implication of law from the facts and circumstances as they appear. It is not based on mere guess work and speculation as to what the parties intended unless the intention of the person making the entries or withdrawals, as the case may be, is attacked on the ground of being illegal and fraudulent.

Even if we took the facts to exist in a light most favorable to the complainant's position, now that the withdrawal by the defendants of the sums alleged was a loan as the complainant contends and not an illegal abstraction in fraud of creditors, a resulting trust would fail.

We now assume that the complainant has finally decided on the position which he desires to take and is confining himself to the legal principle, which apply to a resulting trust, rather than to those of a constructive trust as would appear from the allegations of the original complaint. The complainant contends that the Trustee in Bankruptcy brought this action, not merely as a representative of the creditors, but as a representative of the corporation itself.

If that is the position taken by the complainant, his remedy lies rather on a suit against the directors based on the loan, or if it is the creditors who are bringing this action, then no resulting trust can arise in their favor for the reason that Section 48 of the Corporation Act supplies an adequate remedy against the individual officers or stockholders, who caused the loan to be made.

General Corporation Acts, Section 48, reads as follows:

> "Nothing but money shall be considered as payment of any part of the capital stock of any corporation organized under this act, except as hereinafter provided, in case of the purchase of property, and no loan of money shall be made to a stockholder or officer thereof; and if any such loan shall be made, the officers who make it or assent thereto shall be jointly and severally liable, to the extent of such loan and interest for all debts of the corporation until the repayment of the sum so loaned."

Thus a complete remedy is afforded creditors of a corporation where the officers unlawfully abstract funds therefrom.

It therefore follows that if the complainant is proceeding on the theory of the misconduct of the officers that that would defeat any implication of a resulting trust and is more aptly in the nature of a constructive trust, which the proofs in this case do not establish.

Whether the corporation under consideration is composed of Schram and Sirota only, or whether it includes third parties as stockholders would not alter the legal entity which arises from the act of incorporation.

The Court is undoubtedly familiar with the doctrine that a corporation is a fiction which will only be disregarded in the case of fraud.

Sanborn, *J.*, in the case of *United States* v. *Milwaukee Refrigerator Transit Company,* reported in 142 Fed. 247, reiterated the doctrine mentioned and said as follows, at page 255:

> "A corporation, from one point of view, may be considered an entity without regard to its shareholders, yet the fact remains self-evident that it is not in reality a person or thing distinct from its consistent parts. The word corporation is but a collective name for the members who compose the association. * * * If any general rule can be laid down, in the present state of authority, it is that a corporation will be looked upon as a legal entity as a general rule, and until sufficient reason to the contrary appears; but when the notion of legal entity is used to defeat business convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons; this much may be expressed without approving the theory that the legal entity is a fiction or mere mental creation; or that the idea of invisibility or intangibility is a sophism. A corporation, as expressive of legal rights and powers, is no more fictitious or intangible than a man's right to his own home or his own liberty."

We cite the above case to illustrate our previous contention so that assuming that there was a loan by the corporation to the individuals we cannot hurdle from that transaction to the payment of the purchase money to the wives for the realty, and declare the entire transactions as a resulting trust.

In Bogert on "Trusts", a leading authority in this field, on page 102, the author says, in discussing resulting trusts,

> "Hence, that A has lent money to B and that B has purchased property with such money and taken title in his own name is not ground for the declaration of a resulting trust in A's favor. The money furnished for the property had become B's by virtue of the loan and it cannot be considered that A furnished the consideration for the conveyance to B."

The above statement, supported by many citations, including the case of *Phillips* v. *Phillips* (81 N. J. E. 459), in which case Vice Chancellor Backes, speaking for the Court, said:

> "The burden of establishing a resulting trust is on the party asserting it. He must prove, not only that the consideration for the conveyance was paid by him out of his funds, but also that the money was paid as the purchase price and not as a loan. *When there is evidence from which it may be inferred that the money was advanced as a loan, the burden is on him to overcome this inference by clear and satisfactory proof.*" (Italics ours.)

This principle, so universally recognized as defeating resulting trusts, is applicable to the facts in this case. If, as the defendants contend the withdrawals were salaries, or, as the complainant contends, the withdrawals were loans, there can be no implication that the moneys passed for a conveyance for the benefit of the corporation. The situation is no different from that of a borrower from a bank buying a piece

of property in his wife's name and the bank trying to set up a resulting trust under such circumstances. The answer is in the negative, for the reason that the bank looked to the borrower for the return of the money and has its remedy against him in the law Court, but under such set of facts could the bank establish a resulting trust in the property of its borrowers?

In addition to the transaction between the corporation and the individuals, severing the resulting trust, the transactions between the husbands and their wives would also defeat any recovery under that theory. The adjudications in this State bearing out the principle that where a husband pays the consideration of the purchasing of lands, and has the conveyance made to his wife, the presumption is that a gift or settlement was intended and that a resulting trust will not arise in his favor from such payment.

Read v. *Huff* (40 Eq. 229);
Shotwell v. *Stickel* (83 Eq. 188).

In the latter case the Court held that the presumption was rebutted because there was testimony as to certain conversations that took place between the husband and the wife to the effect that the wife agreed to convey the property to her husband whenever it became convenient to have the proper conveyances prepared. In the case at bar the facts are different. The proof is that the wives collected the rent, paid the taxes, and managed the property in every detail, and it is quite clear that when this corporation was solvent and the directors were drawing fair salaries that they should

buy a home to live in and give it to their wives so as to keep the home conditions and living quarters as a separate and distinct affair from their everyday business transactions. There is nothing unusual about such an arrangement, nothing extraordinary to excite suspicions and if we take the straight view that the moneys were loaned from the corporation at a time when there was sufficient funds and that those funds were given to the wives as a gift to purchase a home, it can hardly be said that a resulting trust is properly established under those facts.

In the opinion of the Vice Chancellor below, his only finding of fact, insofar as our interpretation of his opinion is concerned, is as follows:

> "Speaking generally, this transaction creates a trust."

and he cites cases to support that proposition. They deal with withdrawals by persons in fiduciary capacities and the purchase by them of real estate or other property; but those cases have this limitation and that is that the fiduciary funds or assets must be used to purchase property in a third person's name; but where the facts are disclosed to the entire corporation and the concern has a surplus, it is quite proper for that concern to have loaned the surplus or to declare a dividend, whichever way they see fit and in this case such a withdrawal was proper. This was a closed corporation and it can hardly be said that where one takes from himself that he is violating a fiduciary relationship.

In 26 R. C. L. p. 1223, it is said:

> "Partners have an unquestionable right to deal with the funds of the firm as they please; and if, with their consent or knowledge or acquiescence, a portion of their funds is applied to the purchase of real estate in the name of an individual member, and as his private property, there is in such case no resulting trust. The partners may agree among themselves that any one member may withdraw any part of the common stock, and such part will then become his own; and it matters not how he invests it, even though it be in real estate to be used for the purposes of the firm. He is charged or chargeable with what is so withdrawn and appropriated in account."

Such is the situation in this case except that we are here concerned with a corporation which is practically in effect a partnership for the reason that it is privately owned.

If the Trustee in Bankruptcy, who is the complainant in this case, represents the corporation, then he represents Schram and Sirota and he is therefore in no position to deny that this was a loan and it would therefore follow that a resulting trust could not be established. His remedy, as pointed out previously, exists in the Courts of Law.

If, on the other hand, the trustee in this case appears to represent the creditors, they are not in the least entitled to establish a resulting trust, for it is not their moneys that were used to purchase this property, nor was it the moneys of the corporation. Among the assets of the corporation were listed the loans to the two owners.

In any event, the Court, without any evidence before it found a resulting trust in favor of the corporation in the property held by the wives, without considering the presumption that the law allows us that a gift, if anything, existed between the husbands and their wives.

At page 109, in Bogert on "Trusts", the author says:

> "If the payor of the consideration is related to the person to whom title is conveyed, and in such a way that there is a duty on the part of the payor to support the grantee, the presumption of a resulting trust does not prevail, but the presumption of advancement or gift is established. Thus, if A, the husband of B, paid the consideration for the conveyance of property to B, there is a presumption that A intended to give this property to B, because of the duty which A has to support B."

Numerous other cases support this contention, among which we find the case of *McGee* v. *McGee* (81 Eq. 190) the court said:

> "The result in this State is well settled that where a husband procures real estate to be conveyed to his wife, *he paying the consideration, a presumption arises that he intended to settle the property on her, and while such presumption may be rebutted, the proof offered to accomplish it must be certain, definite, reliable and convincing, leaving no reasonable doubt of the intention of the parties.*" (Italics ours.)

There is no question in the minds of the defendants that proof on this point to rebut that presumption was entirely lacking. There is not a scintilla of evidence to rebut the fact

that the husbands intended to make this a settlement on their wives and therefore, the Court's finding in that respect, was erroneous and without foundation.

Whether it is the corporation, the creditors of the corporation, the individuals, or the creditors of the individuals, the legal situation would remain exactly the same, inasmuch as the complainant does not proceed on the theory of fraud.

In the case of *McGee* v. *McGee, supra,* the husband filed a bill himself to create a resulting trust, which was rightfully refused by the Court for the reasons above stated.

It would, therefore, follow that the rights of the above mentioned parties would be no stronger than that of the individual himself in the absence of fraud, actual or constructive.

POINT II.

The application of the principles of law referred to in the opinion of the Vice-Chancellor, have no bearing on the facts at issue in this controversy.

At page 77 of the state of the case, lines 20-40 and page 78, lines 1-30, it will be observed that counsel for the complainant realized the dilemma in which he was placed, with regard to the proofs in the cause and accordingly requested the privilege of amending the bill of complaint so as to conform with the facts. This amendment was objected to unless it was reduced to writing, and it was further objected to if there was to be a radical departure from the bill filed in the cause. The further objec-

tion was made that the Receiver was not a proper party complainant. These objections, we insist, were properly taken. Counsel for the complainant has failed to make the amendments. The bill has not been re-drafted and it is obvious that the bill and amended bill filed, certainly cannot be regarded as proper causes of action which would justify the opinion rendered by the Court in this case.

We respectfully further contend that, as a matter of law, there could be no recovery in this case, because there was no proof which would justify a decree against the defendants on the evidence which was submitted. If this were an action instituted by the Trustee to recover moneys loaned to the defendants, Bernard Schram and Irving Sirota, there might be a recovery upon the theory of money due and owing by a stockholder or officer of the corporation to the corporation, but this is not the case. The Trustee is attempting here to charge real estate owned by Anna Schram and Lottie Sirota with a lien. They had received nothing from the corporation. They were not indebted to the corporation. There is no dispute about the fact that Schram and Sirota had a perfect legal right to borrow money from the corporation. Nothing in our law precludes or prevents a loan to an officer or a director of a corporation, so that in this case it was clearly legal for these men to have made the loan which they made. The loan having been legal, what they did with the money is immaterial and no one can deny them the right to give this money to their wives as a gift or do what they pleased with the money. This loan was actually made to these men one year and a half prior to the filing of

petition in bankruptcy. There is not a scintilla of evidence showing a fraudulent withdrawal or an intention to withdraw moneys from this corporation, with intent to deceive or defraud creditors. The bill is, of course, not predicated upon any such theory.

Even under the bankruptcy law moneys paid to creditors, outside of the four month period, would not be regarded as a preference, then how it is possible to charge those women with this indebtedness, as charged in the bill of complaint?

1. The bill does not charge a fraudulent withdrawal of money.

2. The bill does not charge a withdrawal of money to the prejudice of creditors.

3. The bill does not charge improper withdrawals.

4. The bill does not charge the corporation was not financially able or that the corporation was insolvent.

Then how can there be a recovery upon the principles of law referred to in the opinion of the learned Vice-Chancellor?

None of the present creditors who claim to be represented by the Receiver in this cause, existed at the time this money was loaned to these men. They certainly cannot complain. They were all paid. Present creditors must show some legal right to charge these women with the indebtedness, and where is there any proof which would justify the result reached by the Court.

There is no legal conceivable theory upon which the decision of the trial court can possibly be sustained.

A further obvious fatal defect is the fact that the Trustee should have been the complainant and should have been authorized to bring this action. This evidence was never supplied and we contend that the Receiver was not a proper party. This is not the proper subject matter of amendment.

The Vice-Chancellor seems to have laid considerable stress on the following cases:

Shaler v. *Trowbridge,* N. J. Eq. 595
(decision of this Court, and
Stratton v. *Dialogue,* 16 N. J. Eq. 70.

It will be noted, in these cases, that the great difference is in the fact that the moneys actually used were always the moneys of the corporation or the partnership and never lost the complexion of being assets of the corporation, and obviously therefore when title was taken in the name of the third party, with moneys belonging and still the property of the corporation, when the purchase was made such title would undoubtedly inure to the benefit of the company or the creditors and stockholders thereof, but in the case at bar, the undisputed facts are that a year and a half prior to the filing of the petition, loans were made by the corporation to two stockholders, the loans recorded and registered on the books of the company. These records were produced by the complainant and made part of the complainant's case. There is no dispute or denial of the fact that these were genuine loans and the bill does not charge

fraud. The fact is that these loans were made upon the theory of an advance payment of salary and that credits were thereafter made against the money so advanced on these loans or advances. That the husbands gave this money to their wives, as a gift so that the wives could be provided for with their homes. The money used by these wives was their money. There is no claim that there was any fiduciary relationship existing at the time. There is no proof in this case that there was, and therefore the cases cited by the Vice-Chancellor and by counsel in their brief, have no application to the facts at bar.

It will be observed that the wives had the absolute control and charge of the premises from the date of the purchase, paying the interest, taxes and collecting rents, and that the husbands had nothing to do with the same. There is no charge in this case that they did not exercise entire dominion and control over the premises.

There is no evidence upon which the decree might be justified which was made by the Honorable Vice-Chancellor in this case.

We respectfully submit, therefore, that the decree entered, decreeing a resulting trust, be reversed and the bill dismissed.

Very Respectfully Submitted,

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New Jersey Court of Errors and Appeals

PAUL MULLER, as receiver in bankruptcy of The Hamilton Warping & Winding Co., Inc., a corporation,
Complainant-Appellee,

vs.

BERNARD SCHRAM and ANNA SCHRAM, his wife; IRVING SIROTA and LOTTIE SIROTA, his wife,
Defendants-Appellants.

On Appeal from the Court of Chancery.

BRIEF OF RESPONDENTS.

This is a bill brought by the receiver of a bankrupt corporation against its officers and their wives to impress a resulting trust on certain lands in Paterson, New Jersey, the title to which stands in the names of the wives. It is admitted that $2,500 was withdrawn from the corporate funds for the purpose of making this purchase. The defendant, Schram, testified (see State of Case, p. 60, l. 29, to p. 62, l. 7) that on November 27, 1922, $2,250 was withdrawn from the funds of the corporation; that this sum was deposited in a bank account in the name of his wife and his "partner" Sirota's wife, and that the money paid for the house in question came out of the said bank account standing in the names of the wives. He testified that $250.00 was withdrawn from the corporation's bank account on October 21, 1922, and was paid as a deposit on the house to the vendor (see State of State, p. 68, ll. 5 to 15).

"There is no dispute as to the sum of $250 being withdrawn on October 21st, 1922,

> by the officers in question nor is the withdrawal of $2,250 of November, 1922, contradicted" (Brief of Appellants, p. 2).

The legal situation thus presented is one in which funds of a corporation are withdrawn by officers of the corporation and used for the purchase of property, title to which is taken in the names of the wives of the said officers. The defendants, Schram and Sirota, were respectively President and Treasurer of the corporation, as appears in the corporation's income tax report for 1922 marked in evidence, which was signed by said defendants as President and Treasurer respectively (see State of Case, p. 26, l. 17, to p. 27, l. 7).

Under the authorities in this State, the transaction was such as to create a resulting trust in favor of the corporation, so that the corporation was the equitable owner of the said property purchased in the names of the wives of said officers.

In the case of *Shaler* v. *Trobridge,* 28 N. J. Eq. 595 (Court of Errors and Appeals), the Court said:

> "The equitable doctrine applicable to the case is well settled. If a person having a fiduciary character purchase property with the fiduciary funds in his hands, and take the title in his own name, a trust in the property will result to the *cestui que* trust or other person entitled to the beneficial interest in the fund with which the property was paid for; or, if a partner purchase lands with partnership funds, and take the title to himself, a trust will result to the partnership. The rule embraces personal property as well as real estate, and if a man purchase a bond, annuity, stock, mortgage, or other personal interest, in the name of a third person, the equitable ownership results to

the person from whom the consideration moves. 1 Perry on Trusts, Sections 127, 130; Johnson *v.* Dougherty, 3 C. E. Gr. 406; Cutler *v.* Tuttle, 4 C. E. Gr. 558."

* * * * * * * * * * *

"If a person occupying a fiduciary capacity purchases property with fiduciary funds in his hands, and takes the title in his own name, he will, by construction, be charged as a trustee for the person entitled to the beneficial interest in the fund with which such purchase was made."

In the case of *Stratton* v. *Dialogue,* 16 N. J. Eq. 70, the Court said:

"1. Where real estate is in fact paid with the funds of a company, there is clearly a resulting trust in favor of the company, although the deed therefor is made absolute to a third party, and purports upon its face to be for his own use and benefit.

2. A party so taking the title, becomes a trustee for the creditors and stockholders, and the trust will be enforced for their benefit at the instance of the receiver."

In the case of *Durling* v. *Hammar,* 20 N. J. Eq. 226, the Court said:

"Any trustee who purchases property with trust funds in his hands will, at the option of the *cestuis que* trust, be declared to hold it in trust for them, although title was taken in his own name, and intended for his own benefit."

In 39 Cyc., page 149, the following note appears:

"Where the trustees of a religious corporation purchase land with the corporate funds, and take a deed in their individual names, they hold the land as trustees of the corporation, and if they subsequently sell the land, the proceeds received by them belong to the corporation and are held to its use. Cincinnati M. E. Church *v.* Wood, 5 Ohio 285."

In 39 Cyc., page 150, the following note appears:

> "Fithians' Estate, 15 N. Y. St. 734, 14 N. Y. Civ. Proc. 52, holding that where an executor receives money as such and invests the same for the benefit of his wife, the wife is a trustee, in favor of the original beneficiary."

Any question as to whether or not the corporation was insolvent when the corporation's funds in question were withdrawn by Schram and Sirota and used to buy the house, is absolutely irrelevant and immaterial. This is not a case where a transfer of corporate funds *to a creditor of the corporation* is attacked as preferential on the ground that the corporation was insolvent; nor is it the case of a transfer sought to be set aside as a fraudulent transfer. In those cases, of course, insolvency is a material consideration. But the point in this case is that the corporation's money was appropriated by the corporation's officers and used to pay for property purchased in their wives' names; and, therefore, the property in question was and is in equity the property of the corporation, regardless of whether or not the corporation was then insolvent.

For the same reason, it makes no difference whether or not any of the present creditors of the bankrupt corporation were creditors when the funds in question were withdrawn. Since as a matter of law the corporation was the equitable owner of the house immediately upon its purchase with the corporate funds in question, the corporation is still the equitable owner of the property, at least to the extent of the amount of corporate funds used, besides interest and *profits*. *Hence* the corporation's present

creditors can now claim said property *as corporate assets.*

Speaking of the two foregoing matters, the Vice-Chancellor in his opinion said:

> "Defendants finally contend that the corporation was not insolvent when its funds were used to buy the property and that no present creditor was then a creditor. Therefore, complainant should not succeed. This argument might be pertinent were this a suit to set aside a fraudulent conveyance, but such is not the case here. There is no attack made on the conveyance itself. The suit merely seeks in effect to have the equitable title to the property declared to be in the trustee in bankruptcy. The situation is the same as if the corporation were not the bankrupt and brought the suit itself. The trustee brings the action as the representative of the corporation as well as the representative of the creditors.
>
> See Remington on Bankruptcy, Vol. IV, p. 85, Section 1409:
>
> 'The trustee succeeds to the bankrupt's title and stands in his shoes and has the bankrupt's rights and remedies.'
>
> Page 190, Section 1479:
>
> 'The trustee is entitled to urge all rights and all the defenses the bankrupt might have urged had there been no bankruptcy.'
>
> I, therefore, think it immaterial whether the corporation was insolvent at the time the property was bought or whether present creditors were then creditors" (see State of Case, p. 87, l. 35, to p. 88, l. 31).

Defendants also contend that fraud actual or constructive must be shown before complainant can prevail. That is not so because the trust is a "resulting," not a "constructive trust." It arises from operation of law and fraud need not be shown.

See 39 Cyc., page 104:

"Resulting Trusts: 1. In General. a. Nature of Resulting Trust. A resulting trust never arises out of a contract or agreement between the parties, but arises by implication of law from their acts and conduct apart from a contract, the law implying a trust where the acts of the property to be charged as trustee have been such as are in honesty and fair dealing consistent only with a purpose to hold the property in trust, notwithstanding such party may have really intended to resist it. Such a trust cannot be subsequently changed by oral declarations. A resulting trust may arise: (1) Where an estate is purchased in the name of one person, but the money or consideration is paid by another; (2) where there is a disposition of property upon trusts which are not declared or are only partially declared, or are illegal; (3) where a conveyance is made without any consideration, and it appears from the circumstances that the grantee was not intended to take beneficially; (4) where a person standing in a fiduciary relation uses fiduciary funds or assets to purchase property in his own or a third person's name; and (5) it has been said that a resulting trust will arise in certain cases of fraud where transactions have been carried on *mala fide;* but the trust which arises in the case of fraudulent transactions is more properly classified as a constructive trust and not as a resulting trust."

* * * * * * * * * * *

Page 148:

"It is an established rule at equity that where trust and confidence are reposed by one party in another, and the latter accepts the confidence or trust, equity will convert him into a trustee, whenever it is necessary to protect the interest of the party so confiding and do justice between them. In accordance with this rule, if a receiver, executor, factor, or other fiduciary uses the

fiduciary funds or assets in the purchase of property and takes a conveyance in the name of himself or a third person, a resulting trust arises in such property in favor of the persons entitled to the funds or assets with which it is purchased, particularly where the purchase is made for the benefit of such persons. So where a guardian purchases property in his own name with funds of his ward, a trust results to the ward; and where an executor or administrator purchases property in his own or a third person's name with funds belonging to the estate, a resulting trust arises in favor of the heirs, legatees, or other persons entitled to the beneficial interest in the estate. If the fiduciary funds thus used constitute only a part of the consideration, a resulting trust *pro tanto* arises."

* * * * * * * * * * *

Page 150:

"Funds in Hands of Agent. Where an agent, having funds or assets of his principal in his possession, uses the same in the purchase of property, and the purchase is made or title taken in the name of himself or of a third person's, a resulting trust in the property so acquired arises in favor of the principal or his heirs, as against the agent or their heirs, or creditors, although the agent made no express promise to act as trustee, and although the principal is indebted to the agent in an amount equal to the value of the property purchased."

Defendants sought to avoid the foregoing legal effect of the appropriation and use of the corporation's funds by its officers Schram and Sirota by showing that Schram and Sirota *had a right to these funds.* This money could not lawfully be *borrowed* from the corporation by Schram and Sirota. Section 48 of the Corporation Law provides:

"Nothing but money shall be considered as payment of any part of the capital stock

> of any corporation organized under this act, except as hereinafter provided in case of the purchase of property, *and no loan of money shall be made to a stockholder or officer thereof;* and if any such loan be made the officers who make it, or assent thereto, shall be jointly and severally liable, to the extent of such loan and interest, for all the debts of the corporation until the repayment of the sum so loaned."

Consequently, the defendants had to resort to the pretense that this money was coming to the defendants, Schram and Sirota, as *unpaid* salary. Speaking of this, the Vice-Chancellor, in his opinion, says:

> "Defendants contend that the withdrawals were perfectly proper in that they were payments or advances for wages. I think the testimony is entirely too vague to establish such a proposition." (See State of Case, p. 85, ll. 15 to 19.)

In this connection, defendants' counsel, cross examining his own client, defendant, Schram, elicited from him over objection of complainant's counsel, the following testimony:

> "Q At the time that the property was bought by your wives, was there any wages due you from the company, you and your partner? A Yes.
>
> Q And is it a fact that when you withdrew moneys from the company, speaking now with regard to the item of two hundred and fifty dollars and the item of $2,250.00, that you withdrew that money as part of the salary and wages then due *and part that might become due to you* for salary and wages? A Yes, sir." (See State of Case, p. 69, ll. 30 to 40.)

Even if that testimony be considered as properly put in the case, it can have no claim to probative value or credibility. In the first place, the above testimony is to the effect that the with-

drawals in question were for "salary and wages then due *and that might become due.*" Insofar as the said sums withdrawn were for "salary and wages *that might become due,*" there was, of course, no justification for their withdrawal, and the sums as and when withdrawn were undeniably funds of the corporation. But since the defendant, Schram, did not testify as to how much of these sums were for wages and salary *that might become due,* and how much was for wages and salary *then due,* it is impossible to know how much of the said sums is to be regarded as moneys to which the defendants, Schram and Sirota claim they were *then* entitled. Consequently, the situation presented by this testimony, is one of utter failure on the defendants' part to prove what sum, if any, out of the said amounts withdrawn, can be regarded by this Court as moneys claimed to belong to them and not to the corporation.

But even the foregoing testimony of the defendant, Schram, that some of the said moneys withdrawn was for "wages and salary due *then,*" is utterly discredited and precluded by the overwhelming evidence to the contrary. To begin with, the entries of these withdrawals in the corporation's books, expressly designate them as *loans.* In the case of the withdrawal of $250.00 on October 21, 1922, the entry is as follows: "1239 10/21 A. Rosenthal. Loan (Receivable) to members, 13, Net Cash—$250.00." This is in the handwriting of the accountant, Magill, and was copied by him from the check book (see State of Case, p. 27, l. 28 to p. 28, l. 24). In the case of the $2,250.00, the withdrawal entry is as follows: "November 27, 1922—Cash for Loans Payable, 13, Net Cash—$2,250.00." This entry is in the handwriting of the defendant, Schram (see State of Case, p. 60, ll. 29 to 41).

The purport of these entries absolutely rules out any claim now made that any part of these sums was for salary due Schram and Sirota. It is impossible that the probative force and effect of these entries, one of which, viz, the $2,250.00, was made by defendant, Schram himself and the other by his accountant *contemporaneously with the withdrawals* could, in any degree, be impaired by the present *self-serving* testimony of Schram. Indeed, the defendants, Schram and Sirota, are legally bound by these entries. See 14A Corpus Juris, 100.

Moreover, the corporation's records show that both before and after these two withdrawals, Schram and Sirota were drawing a salary of $50.00 a week each, these withdrawals being designated as *salary.* During the month of November, 1922, there appear weekly entries of these salary withdrawals in Sirota's own handwriting (see State of Case, p. 60, ll. 29 to 34, and p. 101). This in itself completely refutes the present pretended claim.

Finally the income tax report for 1922 marked in evidence establishes the fact that Schram and Sirota were actually *indebted to the corporation* in the sum of $4,699.67 on December 31, 1922, which was *only one month* after the withdrawal by them of the $2,250.00. (See State of Case, p. 36.) Since the cash book marked in evidence as Exhibit C. 5 (see State of Case, p. 100), does not show any substantial withdrawals by Schram and Sirota after November 27, 1922, other than the weekly salary of $50.00 for each of them, it is conclusively shown that *defendants Bernard Schram and Irving Sirota must have been indebted to the corporation* in the sum of about $2,400 on November 27, 1922; so that the withdrawal by them on that date of $2,250.00 from

the corporation's funds could not have been a receipt by them of money *owing to them by the corporation.* Hence the attempt of the defendants to justify their appropriation of the corporation's funds in question as money owing to them by the corporation proves utterly false.

It may not be amiss to refer to the fact that the testimony of the defendant Schram is shown to be intrinsically unworthy of belief by the manner in which he sought to evade testifying as to the amount paid on account of the purchase price of the house and the amount of encumbrances thereon.

"Q And when you were testifying before Referee Van Cleve you remembered how much had been paid on the house, didn't you? A Yes, sir.

Q (By the Court.) Well, how much had been paid on the house? A I don't remember the exact amount. It is such a long time.

Q (By the Court.) Well, approximately? A It has been paid about three thousand—thirty-five hundred dollars.

Q Up to the present time? A Up to the present time.

Q And how much was paid right away, when you got the deed?

Mr. Weinberger: I object to that on the ground that he didn't say he got the deed.

The Court: No.

Q When the deed was given?

The Court: Yes, when the deed was given how much was paid?

Witness: Around two thousand dollars, something like that.

Q Wasn't it twenty-five hundred? A I don't remember.

Q (By the Court.) Did you testify to the amount before the Referee? A I don't remember.

The Court: Is there testimony before the Referee that this was the amount paid?

Mr. Bilder: Yes, sir.

The Court: Well, ask him if he didn't testify before the Referee so and so.

Q Didn't you testify before Referee Van Cleve that two hundred and fifty dollars was paid to Rosenthal as an account first, and then a balance of two thousand was paid afterwards?

Mr. Weinberger: I object to the question on the ground that it is not the function of the counsel who puts a witness on the stand to attempt to impeach the credibility of his own witness.

The Court: I will allow it.

Mr. Weinberger: I respectfully except.

Q (By the Court.) Did you so testify? A Yes.

Q That first two hundred and fifty dollars was paid directly to Rosenthal, was it not? A I don't remember.

Q (By the Court.) Did you testify that it was paid directly to Rosenthal, before the Referee?

Mr. Weinberger: Just a moment. May I have my objection?

The Court: Yes, you may have all your objections.

This man is trying to evade the clear statement here, plainly.

Mr. Weinberger: Your Honor please—

The Court: He knows perfectly well whether it was paid or not.

Mr. Weinberger: I don't know that and your Honor don't know that.

The Court: He knows.

Mr. Weinberger: The record is there to prove that if it is, in fact, in existence.

The Court: What I want him to answer is, did he tell this Referee that two hun-

dred and fifty was paid directly to Rosenthal.

Mr. Weinberger: May I have my objection to your Honor's question?

The Court: Yes, you can.

Mr. Weinberger: On the ground that if there is such a thing in the record, the witness is entitled to be confronted with it.

The Court: Very well, we will ask him if he so testified. If he did, that is the end of it.

(To witness): Did you so testify?

Witness: If I did testify, it was so.

The Court: Well, did you testify or didn't you?

Witness: I did testify.

The Court: Yes. All right, all you have to do is to answer the questions and tell the truth and you will get along better and more rapidly." (See State of Case, p. 65, l. 9 to p. 67, l. 41.)

Appellants, on page 4 of their brief, quote from the testimony of the witness Magill as follows:

"A You see, there are times when these members took loans, took money from the corporation, which should have been salaries, and charged it as a loan, the simple reason being—I *don't know,* I never questioned them, *I suppose* is to show by withdrawing money from the corporation which they were entitled to as salaries, it might reduce the assets of the corporation to some extent, and they felt that they wanted to show everything on the books."

The language of this quotation makes it manifest that the testimony therein contained is mere supposition and surmise on the part of the witness, and therefore, of course, such testimony is rendered worthless. This manifest character of

this testimony is confirmed by the subsequent testimony of the same witness.

> "Q Mr. Magill, have you now in your mind a distinct recollection of why you wrote the words 'Loans receivable to members' on October 21, 1922, on page 103 of this book? A You mean, do I know why I did it?
>
> The Court: Yes.
>
> The Witness: Well, I do not.
>
> The Court: All right." (See State of Case, p. 33, ll. 17 to 25.)

Appellants on page 8 of their brief refer to the "Foss" case, 147 Fed. 790, as a case in which they say the Court "held that a trust could not be established without some affirmative testimony showing an attempt to commit fraud under the Bankruptcy Act." It is sufficient to note that that was a case in which an *individual* conveyed *his own property* to his wife. The case at bar is one in which two *officers of a corporation* used money of the corporation to purchase property in their wives' names. In the cited case, the property in question belonged to the husband. In the case at bar, the property (originally money and subsequently property purchased therewith) did not belong to the husbands. In the case at bar the very use of the money by the husbands was itself a breach of trust, they being officers of the corporation to which the money belonged. The cited case, of course, involved no such breach of trust. Obviously, the cited case is inapplicable to the case at bar.

Appellants on page 12 of their brief quote from Bogert on "Trusts":

> "Hence, that A has *lent* money to B and that B has purchased property with such money and taken title in his own name is not ground for the declaration of a resulting trust in A's favor. The money furnished for the property had become B's by

> virtue of the loan and it cannot be considered that A furnished the consideration for the conveyance to B."

Of course, this quotation is not intended to refer to a case in which "A" is a corporation and the money in question is withdrawn from the corporation's funds by its officers who purchased property therewith. Likewise, the quotation from *Phillips* v. *Phillips,* 81 N. J. Eq. 459, set forth on the same page of appellant's brief, has no application to a case like the one at bar where the money in question belongs to a corporation, and the corporation's officers (in violation of law) borrow the money from the corporation. Also it has no application to a case where a fiduciary borrows or appropriates the trust funds.

A similar contention is made by appellants on page 13 of their brief:

> "The adjudications in this State bearing out the principle that where a husband pays the consideration of the purchasing of lands, and has the conveyance made to his wife, the presumption is that a gift or settlement was intended and that a resulting trust will not arise in his favor from such payment.
> *Read* v. *Huff* (40 Eq. 229);
> *Shotwell* v. *Stickel* (83 Eq. 188.")

The principle referred to by appellants evidently refers only to a case where a husband uses his own money, but not where he, as an officer of a corporation, or a fiduciary, uses money which does not belong to him. Appellants on page 14 of their brief argue to the effect that the withdrawal of the funds in question from the corporation by its officers was not improper. It is sufficient to say of this that Section 48 of the New Jersey Corporation Law makes it unlawful for officers of a corporation to borrow money from the corporation.

Appellants on page 15 of their brief quote from 26 R. C. L., page 1223, with reference to the rights of *partners* to use partnership funds. Of course, the principles therein referred to have no reference to corporations. Appellants on page 16 of their brief quote from Bogert on "Trusts." The quotation there set forth is obviously inapplicable to a case in which corporate funds are used by one of the corporation's officers to purchase property for his wife. The same comment applies to the quotation from the case of *McGee* v. *McGee,* 81 N. J. Eq. 190, set forth on the same page of appellant's brief.

It is respectfully submitted that the decree of the Court of Chancery should be affirmed.

Respectfully submitted,

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