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RECAPTURE REVIVED

THE recent action of the Interstate Commerce Commission, in response to the application of the railroads for a general increase in freight rates, struck a new and auspicious note in the development of the technique of rate regulation. While rejecting the application, the Commission made a counter proposal which would permit specific increases upon designated commodities, conditioned upon the effectuation of arrangements for pooling the revenue accruing from such increases so as primarily to enable the weaker carriers to meet their fixed interest charges.[1] "The . . . proposal . . . was a shrewd and adroit stroke of administrative diplomacy. It disarms at once those who cavil at the Commission for never doing anything constructive. It trumps the carrier's ace, their professed solicitude for railroad credit. It puts the burden on the rail executives of accepting or rejecting a plan which aims at a cooperative rescue of the most necessitous roads. And yet . . . there exists only the most tenuous warrant in law for any such overture. . . . In the field of diplomacy the

[1] Fifteen Per Cent Case, 1931, 178 I. C. C. 539 (Oct. 20, 1931).

proposed pool would be a master stroke; in the field of law, it is a bit of audacity." [2]

The contingency which evoked this proposal is not without precedent. Although in many respects the economic position of the railroads in 1920 differed materially from the existing situation, nevertheless then as now the curtailment of railroad credit was the most momentous consideration,[3] and precisely the same corrective, the creation of a fund available to weak carriers, was contemplated through the medium of the recapture provisions of the Transportation Act.[4] The experience of twelve years, however, has conclusively demonstrated the inability of the expedient to accomplish the desired result.

Prior to 1920, federal regulation of transportation had taken the form merely of specific restrictions upon the carriers in an attempt to eliminate certain flagrant abuses.[5] In that year it was proposed for the first time to look upon transportation as a subject of national concern,[6] and by the enactment of the Transportation Act it was sought affirmatively to build up a system of railways prepared to handle promptly all the interstate traffic of the country.[7] The major difficulty confronting the projected regulation was the necessity of maintaining uniform rates upon competitive traffic.[8] If rates were fixed with reference to the earning power of strong lines, the weak would be forced into bankruptcy, and thus a valuable unit of the national transportation system would be destroyed. On the other hand, rates fixed solely with a view to the needs of the weaker lines would impose an unreasonable tax on transportation, and seriously curtail the productivity of the country.[9] It has been strongly urged that the only ultimate solution of the problem lies in consolidation,[10] and in fact provision was made in the Act for the eventual

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[2] Editorial by Winthrop M. Daniels, former member of the Interstate Commerce Commission, in the New Haven Journal-Courier, Oct. 24, 1931, at 8.

[3] See Fifteen Per Cent Case, 1931, *supra* note 1, at 567.

[4] 41 STAT. 488, 489 (1920), 49 U. S. C. § 15a, par. 6 (1926).

[5] See The New England Divisions Case, 261 U. S. 184, 189, 43 Sup. Ct. 270, 273 (1923); BEARD, THE AMERICAN LEVIATHAN (2d ed. 1931) 399.

[6] SEN. REP. No. 304, 66th Cong. 1st Sess., Ser. No. 7590, at 18.

[7] See Dayton-Goose Creek Ry. v. United States, 263 U. S. 456, 478, 44 Sup. Ct. 169, 172 (1924).

[8] Speech of Representative Esch, (1920) 59 CONG. REC. 3912; Speech of Representatives Sanders, (1920) 59 CONG. REC. 3452.

[9] See Bunn, *The Recapture of Earnings Provisions of the Transportation Act* (1923) 32 YALE L. J. 213, 217.

[10] Speech of Representative Esch, *supra* note 8, at 3912; Address by Ezra Brainerd, Jr., chairman of the Interstate Commerce Commission, as reported in U. S. Daily, Oct. 21, 1931, at 1901. But *cf.* Doak, *Consolidation from the Railroad Employees' Viewpoint* (1929) 13 PROC. ACAD. POL. SCI. 406.

achievement of this end.[11] But it was realized that the accomplishment of such a project would necessarily require a considerable period of time,[12] and as an attempted substitute in the interim, the device of recapture was adopted.[13] By the recapture clauses, carriers receiving an annual income in excess of six *per cent* of the value of their railway property held for and used in the service of transportation were to pay one-half of such excess to the Commission, and the contingent fund so constituted was to be used by the Commission either by extending credit to carriers to meet capital account expenditures, or by purchasing equipment and leasing it to the carriers.[14]

Objections to the theory of this device ranged all the way from the fear that it would stifle incentive[15] to the conviction that it was a step leading inevitably to government ownership of railroads.[16] More significant opposition arose from the contention that it contravened the due-process clause of the Constitution.[17] Its constitutionality, however, was unanimously upheld by the Supreme Court in *Dayton-Goose Creek Ry v. United States*,[18] on the ground that the recapturable income was never the property of the carrier, since it held such excess only as trustee for the United States.

From the standpoint of practicability it was urged, on the basis of the prior experience of New Hampshire with recapture, that if necessary the carriers would insure the non-existence of excess income through extravagant expenditures.[19] Although the instant opinion of the Commission gives support to this conjecture,[20] it seems improbable that modern economic conditions would permit a carrier to assume the risk necessarily involved in such a course. Moreover, the assumption of such risk would

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[11] 41 STAT. 480 (1920), 49 U. S. C. § 5 (1926).

[12] Pursuant to the provisions of the Act, the Commission in 1921 promulgated a tentative plan for the consolidation of railroads. 63 I. C. C. 455. Its final plan was published in 1929, 159 I. C. C. 522, with minor modifications in 163 I. C. C. 188. At the request of Eastern railroads, portions of this plan will be reconsidered early in 1932. N. Y. Times, Nov. 10, 1931, at 5.

[13] See The New England Divisions Case, *supra* note 5, at 191, 43 Sup. Ct. at 273; SEN. REP. No. 304, 6th Cong. 1st Sess., Ser. No. 7590, at 15.

[14] 41 STAT. 489 (1920), 49 U. S. C. § 15a, par. 5 *et seq.* (1926).

[15] H. R. REP. No. 456, 66th Cong. 1st Sess., Ser. No. 7593, at 9. See Lovett, *Railroad Legislation* (1920) 90 CENT. L. J. 75, 81.

[16] Speech by Representative Sims, (1920) 59 CONG. REC. 3685.

[17] See opinion of Charles Evans Hughes (1920) 59 CONG. REC. 3456; Bunn, *op. cit. supra* note 9.

[18] *Supra* note 7.

[19] Speech by Representative Esch, (1919) 58 CONG. REC. 9347; REP. N. H. PUB. SERV. COMM., MACVEAGH, THE TRANSPORTATION ACT OF 1920 (1923) 850.

[20] Fifteen Per Cent Case, 1931, *supra* note 1, at 568.

be needless in view of the obvious vulnerability of the plan on the question of valuation, for the excess is to be computed on the basis of "fair value," determined with "due consideration to all the elements of value recognized by the law of the land for rate-making purposes." [21] The Commission was authorized to utilize the results of its investigations under the 1913 Valuation Act, and in pursuance of this authority it undertook to fix a single value for each property as of a given date,[22] and expected to maintain a practically continuous valuation as a matter of routine.[23] Following this formula, the Commission in 1927 made its first order to recover excess income from a carrier with less than nine miles of main line track.[24] The carrier's contention that the valuation was erroneous was upheld by the Supreme Court in *St. Louis & O'Fallon Ry. v. United States*.[25] In many respects the decision is inconclusive, for although it held that the cost of reproduction must be considered, it gave no indication of what would be sufficient consideration. Nevertheless, the implication of the decision is that the valuation plan of the Commission must be completely revised, and an almost endless amount of labor expended in the attempt constantly to revalue the property.[26] The *O'Fallon* decision looked upon the law of the land with respect to valuation as something distinct from underlying public policies and their dependence upon a practical standard of valuation for satisfactory administration.[27] A more satisfactory decision may follow upon the Commission's second final order, issued in 1931 against the Richmond, Fredericksburg & Potomac R. R.[28] The order will undoubtedly be contested on the valuation question, but the recent decline in the price level may well influence the carriers to withdraw their support from reproduction cost as the determinative factor in value. But whatever conclusions be reached on this point, until an explicit legislative definition of value for recapture purposes is provided, litigation over value will inevitably continue, with its consequent devitalization of the recapture provisions.

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[21] 41 STAT. 488 (1920), 49 U. S. C. § 15a par. 4 (1926).

[22] The method of valuation adopted by the Commission appears in 75 I. C. C. 1 (1918). See Note (1930) 8 TEX. L. REV. 566.

[23] See Bauer, *The O'Fallon Case* (1929) 18 NAT. MUN. REV. 458. The primary valuation reports have been substantially completed. REP. INTERSTATE COMMERCE COMM. (1931) 91.

[24] Excess Income of St. Louis & O'Fallon Ry., 124 I. C. C. 3 (1927).

[25] 279 U. S. 461, 49 Sup. Ct. 384 (1929).

[26] REP. INTERSTATE COMMERCE COMM. (1929) 87.

[27] See Bauer, *op. cit. supra* note 23, at 460.

[28] 170 I. C. C. 451 (1931). A tentative order has been issued against the Norfolk & Western R. R. A protest has been filed by the railroad, and a hearing thereon assigned for Jan. 6, 1932. Letter from the Interstate Commerce Commission, Bureau of Valuation, dated Dec. 7, 1931.

The concrete results of the operation of the recapture provisions justify the most pessimistic forecasts made for the project. The Commission has annually issued general orders to the carriers to report excess income,[29] on values computed upon such basis as the carriers may select. In response to such orders a negligible number of carriers have reported an excess of about $23,000,000.00,[30] whereas it has been estimated that the amount due from the carriers for the years 1920-1928 alone is in the neighborhood of $300,000,000.00.[31] The reported income assumes even less significance in view of the fact that the costly valuations now being produced by the Commission will in all probability differ considerably from those claimed in the carriers' reports.[32] The total of actual payments made to date is under $11,000,000.00 [33] but since practically all payments have been made with reservations and under formal protest, not even that fund has been available for the purposes contemplated by the Act.[34]

[29] 3 INTERSTATE COMMERCE ACTS ANN. (1930) 2114. The language of one of these orders is given in MACVEAGH, *op. cit. supra* note 19, at 909.

[30] REP. INTERSTATE COMMERCE COMM. (1931) 90. Reports have been made as follows:

Period	Number of Reports	Number of Reports in which excess income is reported	Total Amount of excess income reported
Applicable Period			
1920	993	34	2,505,006.03
Calendar year			
1921	975	27	458,535.72
1922	931	50	1,867,239.33
1923	903	53	6,909,296.66
1924	899	23	1,196,261.90
1925	894	32	2,402,198.71
1926	882	24	1,090,490.78
1927	873	10	177,566.32
1928	849	19	1,111,613.54
1929	822	27	5,378,101.20
1930	552	9	376,138.72
Total excess			23,472,448.91

[31] REP. INTERSTATE COMMERCE COMM. (1929) 87.

[32] *Ibid.* 84. *Cf.* Brooklyn East. Dist. Terminal v. United States, 28 F. (2d) 634 (S. D. N. Y. 1927).

[33] The total paid to date is $10,681,249.90. The present status of the fund, inclusive of payments made, interest on over-due payments, interest from investments and from bank balances is $13,207,762.78. REP. INTERSTATE COMMERCE COMM. (1931) 90.

[34] *Ibid.*

Even had recapture been so far successful as to set up a substantial and applicable fund, however, the conditions stipulated for its use would make it of doubtful utility under existing conditions. At the present time six *per cent* money is not particularly attractive, and any carrier which could qualify for the government loan by providing adequate security and offering reasonable assurance of repayment[35] could probably do better elsewhere. But assuming that such fund offered the only chance of borrowing, an increased debt at six *per cent* is not in the nature of direct financial relief to a needy line.[36]

Ironically enough, in view of the vicarious character of the recapture clause, its only positive achievement has been to prevent the consolidation of two railroads on the ground that the government would be deprived of otherwise recapturable income of the stronger road.[37] But in advocating the repeal of recapture, the Commission has presented more important considerations than its failure to accomplish its designated purposes.[38] Recapture invites, far more than does rate regulation, litigation on the part of the carriers, and recovery would often involve the earnings of several years. Since excess earnings do not exist in the form of cash, but are reinvested in the business, the carriers will resist to the utmost payment of amounts which might well prove disastrous. Litigation over questions of valuation arising under such circumstances would tend to evoke juristic formulae which might later be used with unfortunate effect on broader phases of regulation.[39]

With the recapture device thus the object of attack from all sides, the recent maneuver of the Commission appears all the more striking. In accordance with its proposal, the railroads submitted a plan for effectuating its terms, but with the significant variation, however, that the fund instead of constituting a community of property in all the carriers, would remain the property of the contributors and only become available for loans.[40] The ultimate effect of a credit extension must be to increase the burden on the weaker carriers, while the stronger roads will benefit indirectly from revenue denied to them as a direct increase. The exigencies of the situation, however, were undoubtedly felt by the Commission to outweigh these consider-

[35] 41 STAT. 490 (1920), 49 U. S. C. § 15a, par. 12 (1926).

[36] Speech by Representative Sims, *supra* note 16, at 3684.

[37] Lease of Tionesta Valley Ry., 94 I. C. C. 39 (1924), *aff'd* 105 I. C. C. 570 (1926). The only substantial activity of the carriers under the recapture clauses has been in attempts to qualify under the new line exception. 3 INTERSTATE COMMERCE ACTS ANN. (1930) 2124n.

[38] Special report to SEN. COMM. ON INTERSTATE COMMERCE, May 17, 1930.

[39] REP. INTERSTATE COMMERCE COMM. (1930) 90.

[40] U. S. Daily, Nov. 20, 1931, at 2139.

ations, and the plan was approved in order to avoid prolonged negotiations.[41] As a credit plan, it is not open to the interest rate and security objections to the supposititious recapture fund, for the qualifications are flexible and are based on contemporary conditions. Moreover, according to estimates, the function of the recapture clauses to provide capital will be fulfilled far beyond the expectations of the earlier provisions.[42] Since no question of valuation is involved, the administrative difficulties which beset the path of recapture are practically eliminated, and for the same reason the possibility of litigation is reduced to a minimum.

The plan is admittedly an emergency measure,[43] and does not purport to provide a panacea for the ills of transportation, but only a temporary expedient to meet the problem of the weak and strong railroads pending the advent of consolidation.[44] Like recapture, this *ad interim* proposal will undoubtedly be subjected to adverse criticism. Express authority for a conditional rate increase would be difficult to find, although the attitude of the Supreme Court in the *Dayton-Goose Creek* case might suggest that the spirit of the Transportation Act is sufficiently ample to embrace even this procedure. But the most significant aspect of the plan is the fact that it represents a constructive and ingenious move initiated by the Commission, at a time when ingenious moves are deemed peculiarly within the province of the railroads.

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[41] U. S. Daily, Dec. 8, 1931, at 2275.

Commissioners Eastman, McManamy, Mahaffie and Porter dissented. Excerpts from Commissioner Eastman's dissent appear in the U. S. Daily, Dec. 12, 1931, at 2314, Dec. 12, at 2322, Dec. 14, at 2332, and Dec. 15, at 2342. Commissioner Eastman regarded with "foreboding and apprehension" the introduction into the situation of the unregulated private Delaware Corporation which was suggested by the carriers as the medium for the loans.

[42] The Commission hoped to realize over $100,000,000 a year from the pool. A more recent study by Standard Statistics, Inc., places the annual increase at about $67,500,000, based on expected traffic. Both estimates must be revised somewhat in view of the change from car to tonnage basis. 18 STANDARD SERVICE ON RAILROADS (1931) 2418.

[43] It is expressly limited in duration to March 31, 1933. Fifteen Per Cent Case, 1931, *supra* note 1, at 578.

[44] Another illustration of the Commission's efforts to alleviate the difficulties of weak carriers by temporary expedients is its attempted revision of care-hire arrangements. 165 I. C. C. 495 (1930) (partial relief of short lines from daily rentals). The plan was frustrated by the Supreme Court. Chicago, Rock Island & Pacific Ry. v. United States, reported in U. S. Daily, Nov. 24, 1931, at 2170.

RIGHTS OF GENERAL DEPOSITORS IN ASSETS OF INSOLVENT BANKS

STATISTICS appearing in the annual reports of the Comptroller of the Currency indicate a material appreciation in recent years in the number and amount of preferred claims allowed against the assets of liquidating banks.[1] In part this development may be due to a tendency on the part of some courts to relax the particularity with which the funds on which the claim for preference is based must be traced and identified.[2] For example, in most jurisdictions, it is now held that the deposit of a check in the bank on which it is drawn constitutes an "augmentation of assets",[3] despite the obvious fact that it represents merely a diminution of the liabilities of the bank to the depositor. Again, it has been ruled that if the proceeds of a collection item have been traced into the cash assets of a bank, a priority may attach to the entire assets including credits with correspondents, checks, and overdrafts.[4] A few courts have entirely dispensed with the

[1] During the fiscal year ending Oct. 31, 1930, out of $28,224,066, general creditors with claims aggregating $19,993,710 received only $10,576,060, while secured and preferred creditors claiming $14,387,629 were paid $13,451,712. ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY (1930) 31. From the date of the first national bank failure in 1865 until Oct. 31, 1925, out of distributable assets totalling $314,407,614, $84,967,657 worth of preferred liabilities were paid, while general creditors received $188,697,889. ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY (1925) 6, 7.

[2] Ordinarily the claimant of a preference must show not only that his funds were held on a constructive trust but also that they augmented the commingled assets in the hands of the receiver. See Tinsley v. Amos, 135 So. 397, 399 (Fla. 1931); Townsend, *Constructive Trusts and Bank Collections* (1930) 39 YALE L. J. 980. *Cf.* Salem Elevator Works v. Commissioner of Banks, 252 Mass. 366, 148 N. E. 20 (1925) (requiring that the *res* be traced into a specific property as distinguished from augmented general assets). In proving augmentation, the claimant is aided by the presumption that withdrawals by the trustee from the commingled funds have left the trust property intact (Note (1931) 16 IOWA L. REV. 256, 259) to the extent that the cash assets of the bank were not exhausted or depleted below the value of the trust *res* subsequent to its deposit. Blumenfeld v. Union National Bank of Beloit, 38 F. (2d) 455 (C. C. A. 10th, 1930); 3 POMEROY, EQUITY JURISPRUDENCE (4th ed. 1918) § 1048 (e). But *cf.* Central National Bank of Lincoln v. First National Bank of Gering, 115 Neb. 472, 216 N. W. 302 (1927).

[3] United States National Bank of Omaha v. Glanton, 146 Ga. 786, 92 S. E. 625 (1917); Skinner v. Porter, 45 Idaho 530, 263 Pac. 993 (1928); Leach v. Farmers' Savings Bank of Hamburg, 204 Iowa 1083, 216 N. W. 748 (1927); State v. Excello Feed Milling Co., 131 Okla. 100, 267 Pac. 833 (1928). *Contra:* Rorebeck v. Benedict Flour & Feed Co., 26 F. (2d) 440 (C. C. A. 8th, 1928); Hecker-Jones-Jewell Milling Co. v. Cosmopolitan Trust Co., 242 Mass. 181, 136 N. E. 333 (1922).

[4] State v. Bank of Commerce of Grand Island, 61 Neb. 181, 85 N. W.

necessity for tracing the trust *res* into the hands of the receiver.[5]

However, in view of the fact that most of the traditional requirements of a preference are still observed in a majority of jurisdictions,[6] it seems probable that the augmentation of the class of preferred creditors is for the most part due rather to recent legislation than to tendencies of the courts. The past few years have witnessed the passage of many statutes looking to the protection of the owner or forwarder of collection items in the event of the failure of the drawee or collecting bank.[7] Prominent in this type of legislation is the Uniform Bank Collection Code drafted by the counsel for the American Bankers' Association and adopted in eighteen states.[8] Among other things, this code provides that, when a bank to which paper has been presented for collection, fails after having collected the items, but before having remitted for them in cash or given an unconditional credit therefore, the assets of such drawee or collecting bank shall be impressed with a trust to the amount of the items, and the owner of the paper "shall be entitled to a preferential claim . . . irrespective of whether the fund representing such item or items can be traced."[9] While at common law the collection of the paper was regarded as immediately transforming the col-

43 (1901); People v. Iuka State Bank of Iuka, 229 Ill. App. 4 (1923). The majority rule, however, is *contra*. Farmers Bank of White Plains v. Bailey, 221 Ky. 55, 297 S. W. 938 (1927). "Unless the facts warrant it, application of the presumption rule (augmentation) will not be made to property other than cash in the bank when its doors close. . . . It is not presumed the money was converted by the bank into bills receivable or into a deposit account with another bank or into any other form of property." Townsend v. Athelstan Bank, 237 N. W. 356, 360 (Iowa 1931).

[5] State v. Farmers' State Bank of Polk, 237 N. W. 857 (Neb. 1931); Eastman v. Farmers' State Bank of Olivia, 175 Minn. 336, 221 N. W. 236 (1928) (burden on receiver to show no augmentation).

[6] See Townsend, *op. cit. supra* note 2, at 993.

[7] See Bogert, *Failed Banks, Collection Items, and Trust Preferences* (1931) 29 MICH. L. REV. 545, 555. The North Carolina Statute provides that where an item was sent for collection and remittance, and collection was made, but there was no remittance, or the check sent in remittance was not paid, the item owner shall have a lien on the assets of the failed collecting bank. N. C. CODE ANN. (Michie, 1927) § 218 (c)-(14). Colorado provides that drafts given by a collecting bank in payment for items shall be entitled to a preference, and does not limit it to items sent for collection and remittance. COLO. ANN. STAT. (Mills, 1930) c. 13, § 381-h[1]. South Carolina declares all items sent for collection to be a trust fund, and a prior lien. S. C. ACTS (1927) No. 202, § 2.

[8] N. Y. CONS. LAWS (Cahill, 1930) c. 39, §§ 350–350 L. Other states which have adopted the code are: Idaho, Illinois, Indiana, Kentucky, Maryland, Michigan, Missouri, Nebraska, New Jersey, New Mexico, Oregon, Pennsylvania, South Carolina, Washington, West Virginia, Wisconsin, Wyoming.

[9] N. Y. CONS. LAWS (Cahill, 1930) c. 39, § 350–L.

lecting agent into a simple debtor,[10] under the code the agency relation is extended to cases in which insolvency occurred after collection. Thus the forwarder of an item would be granted a preference when collection had been effected and remittance made by a draft dishonored because of the subsequent failure of the drawee bank.[11] Perhaps an equally significant effect of this enactment is completely to eliminate, as a prerequisite to priority, the necessity for tracing the proceeds of the paper into cash on hand, credits with correspondents, or other funds and thus to permit the subjection of the entire assets of the bank to the item owner's claim.[12] In support of this provision it may be said that it increases the certainty of a section of the law which conflicting authority had rendered chaotic.[13] Theoretically it tends to facilitate the transferability of commercial paper. And it helps to recompense the item owner for the additional risk to which "direct routing" subjects him.[14]

On the other hand the tendency exemplified by such legislation, together with judicial expansion of the common law preferences, necessarily depreciates the security available to the general depositor in bank liquidations.[15] Statutory attempts to offset this tendency by machinery adapted to the protection of this import-

[10] See Citizens' Bank of Pinewood v. Bradley, 136 S. C. 511, 516, 134 S. E. 510, 511 (1926); Hecker-Jones-Jewell-Milling Co. v. Cosmopolitan Trust Co., *supra* note 3, at 186, 136 N. E. at 335. *Contra:* Monticello Hardware Co. v. Weston, 28 F. (2d) 672 (C. C. A. 5th, 1928); see also Lippitt v. Thames Loan & Trust Co., 88 Conn. 185, 202, 90 Atl. 369, 375 (1914) (extension of agency relation beyond collection depends on intent of parties).

[11] In re Jayne & Mason, 251 N. Y. Supp. 768, (Sup. Ct. 1931); see Bank of Republic v. Republic State Bank, 42 S. W. (2d) 27, 31 (Mo. 1931).

[12] Apparently this result is not assured unless the tracing requirement is specifically and expressly eliminated by the statute. Thus in Wachovia Bank & Trust Company v. People's Bank of Darlington, U. S. Daily, Sept. 13, 1930, at 2165, it was held that the South Carolina statute, creating a trust for the benefit of collection items but making no provision regarding identification (*supra* note 7), was not applicable when there had been no augmentation of assets.

[13] See Legis. (1929) 43 HARV. L. REV. 307, 311.

[14] See Turner, *Bank Collections—The Direct Routing Practice* (1930) 39 YALE L. J. 468, 485 *et seq.*

[15] In a letter opposing the passage of a bill providing that transferors for collection of negotiable instruments drawn against the delivery of an accompanying document of title, Secretary of the Treasury Mellon said, "Thus the passage of the bill would create a preference from the mere fact of collection of the proceeds regardless of whether or not such proceeds were afterwards traceable to the hands of the receiver. This is clearly unjust to the general creditors. The assets of the general creditors should not be taken for the purpose of preferring a creditor whose property is not included within said general assets." HEARINGS BEFORE THE COMMITTEE ON BANKING AND CURRENCY in H. R. 5634, pp. 71–72 (May 16, 1930); *cf.* Bogert, *op. cit. supra* note 7, at 563.

ant class of interests have, in general, met with small success. Thus the Depositor's Guaranty Funds proved inadequate to meet the very emergencies for which they were provided, and in all but one of the states which had installed them they have been repealed.[16] Likewise, any extensive attempts to protect depositors by requiring a bond to be given by banks for this purpose would probably be foredoomed to failure. Though it has been stated that, "The statistics of bank mortality are now ample for a computation of the risk assumed in such underwriting",[17] it would seem that the experience of the last few years might be regarded as complete refutation of this possibility. The collapse of the Guaranty Funds has left the interests of the general depositor unprotected in most jurisdictions except for the more general guards afforded by governmental examination of banks,[18] adequate reserve requirements,[19] and the preservation of a minimum ratio between capital and deposits.[20]

The typical bank liquidation statute, however, either makes no mention of the order in which the assets of defunct banks shall be disbursed,[21] or provides merely for *pro rata* distribution.[22] In either case priorities are generally meted out according to the established chancery rule.[23] A number of legislatures

[16] For an exhaustive analysis and history of the Guaranty Fund Laws see Butts, *Guaranty of Bank Deposits in Eight States* (1930) 3 MISS. L. J. 186.

[17] WHITE, MONEY AND BANKING (4th ed. 1911) 480.

[18] This is sometimes effected by requiring a certain number of verified reports from bank officials. 42 STAT. 1067 (1922), 12 U. S. C. § 161 (1926). Sometimes there is direct examination by the superintendent of banks. OHIO GEN. CODE (Page, 1926) § 710-19.

[19] MICH. COMP. LAWS (1929) §§ 11918, 11919; NEW YORK CONS. LAWS (Cahill, 1930) c. 3, § 112; N. C. CODE ANN. (Michie, 1927) § 220F.

[20] CAL. GEN. LAWS (Deering, 1923) Act 652, § 19; TEX. STAT. (1928) art. 506.

[21] The following statutes merely provide for distribution of assets according to the order of a court; ARIZ. CODE (Struckmeyer, 1928) § 251; ARK. DIG. STAT. (Crawford & Moses, 1921) § 724; CAL. GEN. LAWS (Deering, 1923) Act 652, § 136; MASS. GEN. LAWS (1921) c. 167, § 31; N. Y. CONS. LAWS (Cahill, 1930) c. 3, § 78; OHIO GEN. CODE (Page, 1926) § 710-98. In Kansas the order of the bank commissioner directs the payment of dividends. KAN. REV. STAT. ANN. (1923) c. 9, § 130.

[22] 13 STAT. 115 (1864), 12 U. S. C. § 194 (1926); KY. STAT. (Carrol, 1930) § 165 a-17. A Connecticut statute carefully describes the order in which assets shall be disbursed. The enactment thus marshals the claims: (1) to liquidation expenses; (2) to redemption of circulating notes; (3) to deposits; (4) sums paid in by the state for stock subscriptions, or the school fund; (5) all other liabilities. CONN. GEN. STAT. (1930) § 3935. See Lippitt v. Thames Loan & Trust Co., *supra* note 10, at 190, 90 Atl. at 371.

[23] Scott v. Armstrong, 146 U. S. 499, 13 Sup. Ct. 148 (1892); Spokane County v. Clark, 61 Fed. 538 (C. C. D. Wash. 1894); Hallett v. Fish, 123 Fed. 201 (C. C. D. Vt. 1903); Lucas County v. Jameson, 170 Fed.

have sought to vary this system by providing that unsecured depositors shall have priority over all other claimants, and by giving them a first lien on all the assets of the bank.[24] But the courts have not heretofore shown themselves kindly disposed towards such enactments.[25] Thus, it has been held that the statutory lien of the depositor is junior to that of a judgment creditor acquired against the bank's assets before insolvency.[26] Other cases maintain that the state cannot impair a prior right belonging to the federal government by thus granting a preference to depositors.[27] And recently in *State v. Farmers' State Bank of Polk*,[28] the Nebraska court decided that the depositor's lien statute did not apply to the converted proceeds of a note, as these "were never assets belonging to the bank within the meaning of the statute." This last decision, by granting a preference to the owner of the note notwithstanding the fact that the funds on which his claim was based had never reached the receiver, would appear to reduce materially the effectiveness of the depositors' lien statute. Moreover, in view of the fact that the Collection Code expressly impresses all the assets of a defunct bank with a trust for the benefit of item owners, it seems that when both the Collection Code and a depositors' lien statute have been enacted,[29] the former would take precedence, on the ground that the trust funds do not constitute assets to which a lien may attach.[30]

Logically the initial step in any attempt to ameliorate the

338, (C. C. S. D. Iowa 1908); Elmira Savings Bank v. Davis, 142 N. Y. 590, 37 N. E. 646 (1894); O'Brien v. Grant, 146 N. Y. 163, 40 N. E. 871 (1895). In isolated instances this type of statute has been otherwise construed. Thus in Central Trust Co. of Illinois v. Hanover Trust Co., 242 Mass. 265, 268, 136 N. E. 336, 337 (1922) the court said ". . . the right to preferential payments should not be implied or extended in cases arising under this statute, one purpose of which is to insure prompt liquidation in favor of the numerous depositors . . ."

[24] IOWA CODE (1931) § 9239 (gives preference to depositors). NEB. COMP. STAT. (1929) c. 8, § 1, 102. ORE. CODE ANN. (1930) §§ 22-2003, 22-2004.

[25] But they have been held constitutional and not violative of the due process clause. Upham v. Bramwell, 105 Ore. 597, 210 Pac. 706 (1922).

[26] Guaranty Fund Commission v. Teichmeier, 119 Neb. 387, 229 N. W. 121 (1930).

[27] Mothersead v. U. S. Fidelity & Guaranty Co., 22 F. (2d) 644 (C. C. A. 8th, 1927); United States v. Bliss, 40 F. (2d) 935 (D. Neb. 1930); State v. Thurston State Bank, 237 N. W. 293 (Neb. 1931). But *cf.* In re Cameron, 287 Pa. 560, 135 Atl. 295 (1926).

[28] *Supra* note 5.

[29] NEB. COMP. STAT. (1929) c. 8, § 1102, c. 62, §§ 1801-1815.

[30] See Spokane County v. Clark, *supra* note 23, at 539, where it is said, "Money held by a bank as trustee is not part of its assets nor legally subject to claims of its creditors." See Flint Road Cart Company v. Stephens, 32 Mo. App. 341, 348 (1888).

general depositor's position would be the elimination of unfair elements in the prevailing systems for distributing the assets of failed banking corporations. At present it is the practice of many courts to allow a creditor who has been given collateral for his debt [31] to prove, in the event of insolvency, the full amount of his claim, collect ratably with the general creditors, and then supplement these receipts by the sale of the security to an extent necessary to constitute payment in full.[32] This procedure tends unduly to favor the secured creditor at the expense of the diminishing funds available to the general depositor.[33] Probably greater equality might be obtained between all claimants by a more general adoption of the so-called "bankruptcy" rule, under which a creditor either must first exhaust his security and participate in dividends on the basis of the balance of his claim only, or else surrender his security and receive dividends on the full amount of his claim.[34]

Likewise an abatement of the unreasonable advantage accorded in some jurisdictions, to government claims is much to be desired. In view of the fact that a bond is generally required for the protection of state deposits,[35] the granting of a preference to claims for such funds is largely superfluous.[36] The only benefit occurring from this practice accrues to the surety who, by being subrogated to the preferential right of the state, is

[31] Statutes frequently limit the power of a bank to give collateral. Some prohibit a pledge of assets to secure a general depositor, IDAHO SESS. LAWS (1925) c. 133, § 37, although public funds are generally excluded from the operation of this prohibition. OKLA. COMP. STAT. ANN. (Supp. Thornton, 1926) § 5727; VA. CODE ANN. (Michie, 1930) § 4149 (49). In the absence of statute the authorities conflict as to the permissibility of securing deposits. (1929) 77 U. PA. L. REV. 916.

[32] Aldrich v. Chemical National Bank, 176 U. S. 618, 20 Sup. Ct. 498 (1900); In re Prescott State Bank's Estate, 3 Pac. (2d) 788 (Ariz. 1931); Imperial Irrigation District v. Wood, 292 Pac. 665 (Cal. 1931); Bates v. Paddock, 118 Ill. 524, 9 N. E. 257 (1886); Third National Bank of Detroit v. Haug, 82 Mich. 607, 47 N. W. 33 (1890); People v. Remington & Sons, 121 N. Y. 328, 24 N. E. 793 (1890).

[33] Citizens & Southern Bank v. Alexander, 147 Ga. 74, 92 S. E. 868 (1917); In re Cosmopolitan Trust Co., 241 Mass. 346, 136 N. E. 269 (1922); First National Bank of Seattle v. Mansfield State Bank, 127 Wash. 475, 221 Pac. 595 (1923).

[34] See dissent of Mr. Justice White in Merril v. National Bank of Jacksonville, 173 U. S. 131, 147, 19 Sup. Ct. 360, 367 (1899).

[35] ILL. REV. STAT. (Smith-Hurd, 1931) c. 130, § 29; KY. STAT. (Carroll, 1930) § 4693; N. M. ANN. STAT. (Courtright, 1929) c. 112 § 108; N. Y. CONS. LAWS (Cahill, 1930) c. 57, § 8; PA. ANN. STAT. (Purdon, 1931) Tit. 72, c. 3, § 3791; TEX. STAT. (1928) c. 3, art. 2560. Iowa provides a sinking fund for public deposits. IOWA CODE (1931) c. 352-A1, §§ 7420-a1-7420-b12.

[36] See Arnold, *An Inequitable Preference in Favor of Surety Companies* (1930) 36 W. VA. L. Q. 278, 279.

enabled to minimize the risk which he has been paid to take.[37] Thus many courts have refused entirely to recognize a prior right in the state,[38] or have held that, by requiring security, the state has waived its prerogative.[39]

Clearly, the possibility of materially improving the status of the depositor in bank liquidations by thus eliminating established priorities is definitely limited. Probably better results can be obtained by restricting the resources available for preferential payment. Thus it has been proposed, in a collection code prepared for the Commission on Uniform State Laws, to limit the rights of item owners to the relatively liquid assets of insolvent banks.[40] With the supplementary creation of a national credit reservoir to buy up fixed and frozen assets [41] such a device might succeed in providing funds immediately available for the payment of general unsecured depositors. Judging by the collapse of the Guaranty Funds, however, it would seem that no such system of deposit insurance can survive the strain resulting from a prolonged epidemic of bank failures. The situation will never be satisfactory until some method is devised for strengthening the weaker sections of the state and national banking systems. Directed to the accomplishment of this end is the trade area branch banking system proposed by the Comptroller of the Currency in his report for 1930.[42] By permitting strong city banks to carry their facilities to the surrounding community, this plan attempts to establish a sound banking system in rural districts, where during past periods of depression the banking casualties have been greatest.[43] From the point of view of the depositor this legislation is immeasurably desirable. Although the prevailing methods of distributing the assets of defunct banks leave

[37] United States Fidelity & Guaranty Co. v. Ottowa County National Bank, 32 F. (2d) 368 (N. D. Okla. 1929); National Surety Company v. Oswego State Bank of Oswego, 33 F. (2d) 221 (D. Kan. 1929); Central Trust Company v. Bank of Mullins, 107 W. Va. 679, 150 S. E. 221 (1929).

[38] Andrew v. Munn, 205 Iowa 723, 218 N. W. 526 (1928); Potter v. Fidelity & Deposit Co. of Maryland, 101 Miss. 823, 58 So. 713 (1911); North Carolina Corporation Commission v. Citizens Bank & Trust Co., 193 N. C. 513, 137 S. E. 587 (1927).

[39] State v. Loudermilk, 23 Ariz. 574, 205 Pac. 915 (1922); National Surety Company v. Pixton, 60 Utah 289, 208 Pac. 878 (1922).

[40] See HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS (1930) 304, 321.

[41] The National Credit Corporation Plan recently initiated by President Hoover (See N. Y. Times, Oct. 9, 1931, at 16) in order to secure "the rediscount of banking assets, not now eligible for rediscount at the Federal Reserve Banks, in order to assure our banks, being sound, that they may attain liquidity in case of necessity" (N. Y. Times, Oct. 7, 1931, at 1) is similar in form, but not in purpose, to the device suggested herein.

[42] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY (1930) 4 *et seq.*

[43] *Ibid.* 2.

much room for improvement, it is only by reducing the number of bank failures that deposit interests can be accorded a reasonable assurance of safety.

THE JUDICIAL HISTORY OF THE ANTHRACITE MONOPOLY

IN 1924 the Temple Anthracite Coal Company, a Delaware corporation organized as a holding company, acquired the controlling interest in two large anthracite companies. The Federal Trade Commission charged that such stock acquisition violated the Clayton Act,[1] and ordered the company to divest itself thereof. On appeal,[2] the order was reversed by the Circuit Court of Appeals for the third circuit on the ground that it did not appear that there was any "substantial lessening of competition."

The case represents the most recent episode in the history of governmental attempts to destroy monopoly in the anthracite coal industry. The conflict began early in the present century, when the existence of concentration in the anthracite fields was marked by high, uniform prices, and huge railroad profits.[3] All the market outlets in the anthracite region were in the hands of a half-dozen great, coal-producing railroads, which owned or controlled over ninety *per cent* of the total anthracite resources, and produced seventy-five *per cent* of the annual tonnage. By 1900, substantial agreements had been reached as to the percentage of tonnage to be carried by each road, the market price, and the price to be paid for coal purchased from independent operators.[4]

The need for regulation of the monopoly became apparent in the case of *New York, New Haven & Hartford Railroad v. Interstate Commerce Commission*.[5] The New Haven Railroad had contracted to buy coal from the Chesapeake & Ohio Railroad at a price which was less than the purchase cost, the cost of delivery, and the published freight rate. The Chesapeake contended that the alleged rate discrimination was merely "apparent," as the real consideration for the agreement was the liquidation of a debt owed to the New Haven, but a decree granting an injunction against enforcing the contract was affirmed. The possibilities, as shown by this case, of rate discrimination

[1] 38 STAT. 731 (1914), 15 U. S. C. § 18 (1926).

[2] 51 F. (2d) 656 (C. C. A. 3d, 1931).

[3] For a detailed history of the anthracite monopoly, see JONES, THE ANTHRACITE COMBINATION IN THE UNITED STATES (1914).

[4] *Ibid.* c. 4.

[5] 200 U. S. 361, 26 Sup. Ct. 272 (1906).

through railroad ownership of the goods transported were thoroughly alarming. The then prevailing climate of opinion also led to the sentiment that anything resembling a trust should be incontinently "busted," in order that competition might have free rein. The result was the incorporation into the Hepburn Act [6] of the commodities clause, which prohibited the transportation in interstate commerce by any railroad of goods which it had manufactured, mined, or produced; which it owned in whole or in part; or in which it had any interest, direct or indirect.

The first test of the clause [7] was made in *United States v. Delaware & Hudson Company*.[8] The defendant railroads contended that the clause contravened the Fifth Amendment.[9] The government argued for a broad interpretation which would serve to prohibit the carriers from dealing in the goods which they transported. The Supreme Court, although not insensible to the power of the railroads, was faced by the realization that if the clause were held unconstitutional all further attempts at legislative control would be effectively blocked. Mr. Justice White successfully avoided, however, the "grave constitutional questions" [10] by interpreting the clause as prohibiting transportation by railroads in interstate commerce of (1) articles manufactured, *etc.*, by the carriers and from which they had not dissociated themselves prior to transportation, (2) articles owned in whole or in part by the carrier, and (3) articles in which the carrier at the time of transportation, has some interest, in a legal or equitable sense, "not including, therefore, articles manufactured, mined, produced or owned by a *bona fide* corporation in which the railroad is a stockholder." The clause, thus construed, is not applicable where the railroad itself mines and then sells the coal, or where the coal is mined and owned by one of its subsidiaries. The result is the setting up of an elaborate system of purgatorial rites, whereby the offender may be

[6] 34 STAT. 584 (1906), 49 U. S. C. 1 (8) (1926).

[7] See Lewis, *The Commodity Clause of the Hepburn Act* (1908) 21 HARV. L. REV. 595, written before the Hudson case, *infra* note 8. The clause was directed primarily against the anthracite roads.

[8] 213 U. S. 366, 29 Sup. Ct. 527 (1908).

[9] See Hand, *The Commodities Clause* (1908) 22 HARV. L. REV. 250.

[10] The grave questions, as seen by Mr. Justice White, were first, whether the power of Congress to regulate interstate commerce gives authority to prohibit the production of the commodity, not because of some inherent quality, but because it may become the subject of interstate commerce; and second, if that power does not so extend, whether a railroad can be prohibited from carrying the commodity in interstate commerce because, prior to transportation, it mined or produced it. Subsequent events showed that it would have been better had the Court squarely met the constitutional problems involved in the commodities clause, instead of attempting to sidestep the issue.

cleansed with a minimum of discomfort. The upholding of the clause's constitutionality, after its force had been completely nullified, left to the champions of free competition only a pyrrhic victory.[11]

In *United States v. Lehigh Valley R. R.*,[12] the Court retreated from its stand in the *Hudson* case, and held that where the obvious reason for the ownership of coal company stock by the railroad was to evade the commodities clause, the railroad was to be considered as having a definite interest in the coal transported. Upon the heels of this decision, came the device of organizing a coal company, controlled through stock ownership by the railroad, which contracted to "buy" from the railroad all coal produced or acquired by it. The railroad, in *United States v. Delaware, Lackawanna & Western R. R.*,[13] loudly protested that the coal transported had been sold to the coal company before leaving the mines. The Supreme Court, however, held this also a violation of the clause.

The next step was the creation of a coal company, owned by the railroad, and a sales company, the stock of which was owned by the individual shareholders of the railroad. The sales company contracted to buy all the coal produced by the coal company. The coal was then carried to tidewater by the railroad. The Court, in *United States v. Lehigh Valley R. R.*,[14] held not only that the contract of sale was a violation of the commodities clause, the sales company being neither an independent buyer nor a free agent, but that the corporate combination constituted a violation of the Sherman Act.[15]

During this period from 1908 to 1920, suits were also instituted against anthracite coal companies charging violations of the anti-trust laws. The main source of complaint was the small, independent producers of coal, who, since the anthracite railroads controlled every outlet to tidewater, were forced either to pay prohibitive freight rates, or to sell their coal to the railroads at a certain percentage of the market price. The rate paid by the carriers was uniform, and until 1900, it amounted to only 60 *per cent* of the market price. In that year a strike occurred, and the miners obtained a 10 *per cent* increase in wages. The independent operators threatened to cause a renewal of the strike by withholding the miners' wage increase unless the percentage paid for their coal was raised. The result

[11] The opinion is bitterly criticized in Anonymous, *The Commodities Clause Decision* (1909) 9 COL. L. REV. 523.

[12] 220 U. S. 257, 31 Sup. Ct. 387 (1911).

[13] 238 U. S. 516, 35 Sup. Ct. 873 (1915). Note (1915) 14 MICH. L. REV. 49.

[14] 254 U. S. 255, 41 Sup. Ct. 104 (1920).

[15] 26 STAT. 209 (1890), 15 U. S. C. §§ 1, 2 (1926).

was a uniform rate of 65 *per cent*, set out in perpetual contracts between the operators and the railroads. At this time, one of the largest independent companies sought to secure the penetration into the anthracite region of a new, competing railroad equipped to serve the small collieries. Alarmed by this threat, the railroads jointly purchased the stock of the Temple Iron Company, a small concern possessed of a broad charter, through the agency of which they engineered the purchase of all the stock in the independent colliery. With the support of this mining company withdrawn, the new railroad project was abandoned, and the monopoly was saved.[16]

At this juncture the government intervened and in the first *Reading* case,[17] the dissolution of the combination centering around the Temple Coal Company was secured and the 65 *per cent* contracts were declared illegal. The second *Reading* case[18] was an attack upon specific combinations, against which the charges had been dismissed without prejudice in the former suit. The Reading Company itself was a holding company, owning the controlling interest in the Reading Railway, the Reading Coal Company, and the New Jersey Central, which in turn owned a majority of shares in the Wilkes-Barre Coal Company. The government contended that the Reading group constituted a combination in restraint of trade, and that the transportation in interstate commerce of coal by the Reading Railway and the Central was a violation of the commodities clause. The Reading combination was dissolved and the railroads were carefully segregated from the coal companies under a plan of reorganization approved by the Court.[19]

The attack on the anthracite monopoly has extended over a period of nearly twenty years. With the exception of the dis-

[16] These facts appear in the record of United States v. Reading Company, 183 Fed. 427 (E. D. Pa. 1910).

[17] United States v. Reading Company, 226 U. S. 324, 33 Sup. Ct. 90 (1912) affirming the decision of the lower court as to the Temple Iron Co. transaction, and reversing as to the sixty-five *per cent* contracts.

[18] United States v. Reading Company, 253 U. S. 26, 40 Sup. Ct. 425 (1919), *aff'g* in part, and *rev'g* in part, 226 Fed. 229 (E. D. Pa. 1915).

[19] Continental Ins. Co. v. United States, 259 U. S. 156, 42 Sup. Ct. 540 (1921). The plan involved (a) merger of the Reading Railway into the Reading Company, the latter being prohibited from doing any business other than that of a railroad; (b) the turning over for sale, to trustees appointed by the court, of the central stock, to be sold to others than shareholders in the Reading Company; (c) segregation in the same manner of the Wilkes-Barre Coal Company from the Central; (d) separation of the Reading Coal Company from the Reading Company by issuing certificates in exchange for Reading Company stock, and the creation of a new coal company, the stock of which was issued to the old shareholders, with the understanding that they were to divest themselves of either the certificates or the stock.

astrous setback in the *Hudson* case and the recent holding in the *Temple* case, the government has been consistently victorious in the determination of the legal issues.[20] Every new device of organization has represented a definite retreat on the part of the combination before the advancing line of court decisions. Yet the present situation offers small comfort to the champions of free competition. In 1923 it was estimated that eight "railroad coal companies" owned 78 *per cent* of the remaining anthracite reserve; seven large independents controlled 9.6 *per cent;* and the remaining 12.4 *per cent* was divided among 160 companies.[21] In that year only three independent concerns mined over a million tons.[22] In 1930 there arose as the result of mergers two companies with an annual production capacity together of fourteen million tons, which represents nearly 25 *per cent* of the total output.[23] Moreover, concentration is apparent from the inordinately high profits, out of all proportion to the costs of mining,[24] which have been paid to anthracite investors. In 1924 and 1925, the Glen Alden Coal Company paid dividends of 140 *per cent,* and during the next four years, the investors received 200 *per cent* on their capital.[25]

Nor has the separation of the railroads from the coal companies been so complete as it would appear. True, the suits against the combinations served to abolish crude methods of control through interlocking directorates and direct stock ownership. But it has been indicated that the connection between the railroads and the coal companies is now effected through the medium of large banking firms.[26] Moreover, the four largest railroads in 1930 carried an even higher proportion of the an-

[20] It is interesting to note that the lower courts, perhaps because of proximity to the anthracite region, have never adopted such stringent measures against the monopoly as has the Supreme Court in its reviews of the cases.

[21] LAIDLER, CONCENTRATION IN AMERICAN INDUSTRY (1931) 55.

[22] *Ibid.* 56.

[23] The 1930 production of one of these companies, the Glen Alden, as estimated from POOR, INDUSTRIALS (1931), was over eleven million tons.

[24] Although there are no very accurate data on the costs of mining today, and although the costs have increased because of added difficulty in extracting the coal, it is highly improbable that there has been the sharp increase necessary to justify present prices.

[25] ROCHESTER, LABOR AND COAL (1931) 43. It is charged by this author, though with no authority, that the Hudson Coal Company, whose stock is owned by the Delaware and Hudson Railroad, earned for the latter in 1928 a profit of $12 a share, although operating, according to its own books, at a "loss" of $1,400,000.

[26] BOGEN, THE ANTHRACITE RAILROADS (1927) 240. "Since the 'segregation' in 1923, the coal mining company (Phila. & Reading) has been distinct, tied to J. P. Morgan & Company, who also control the Reading, but with the operations of the coal company technically separate from other interests." ROCHESTER, *op. cit. supra* note 25.

thracite tonnage than was carried by them in 1908, and the proportion carried by each was substantially the same as in 1908.[27] This may be partially explained by the fact that the geographical advantage of each railroad has remained unchanged, but it seems significant that the tonnage has not been reduced by the expected competition from new roads.

It can thus be gathered that free competition is still nothing but an ideal in the anthracite fields. In view of the modern tendency toward concentration,[28] and in view of the small, compact area containing anthracite resources,[29] the choice of monopoly over competition seems inevitable. Attempts to destroy the monopoly by separation of the coal companies from the railroads do not seem to have been well chosen, for it difficult to see how this could have restored competition among the coal companies themselves. The efforts at destruction seem also to have been ineffective, for although the law has consistently triumphed, the situation has remained noticeably unchanged, and the same objections to the organization of the anthracite industry are as valid today as they were thirty years ago.

The first chapter of anthracite regulation opened with the government's defeat in the *Hudson* case, and closed with the monopolists still in control.[30] And the second chapter (also inaugurated by governmental defeat in the *Temple* case) promises to reach the same conclusion. But even in the face of the monopolistic evils which plague the industry at present, one cannot fail to rejoice at the defeat of free competition. The most casual survey of the kindred field of bituminous reveals the "spotted actuality" of the competitive ideal,[31] and it is to be doubted whether the introduction into anthracite of unfettered competition would solve the problems of wages, profits, and price. However, if competition must be had in all events, it might be well to adopt the suggestion of one eminent authority, that a subsidy of $1,000,000 be appropriated for the development of a smokeless bituminous.

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[27] The comparison was made from the tonnage figures of 1908, as appearing in JONES, *op. cit. supra* note 4, at 148, and the tonnage figures for 1930 as computed from POOR, RAILROADS (1931).

[28] One predisposing factor in anthracite is the complete unionization of the industry, which would tend to bring the operators into closer cooperation.

[29] See GILBERT & POGUE, AMERICA'S POWER RESOURCES (1921) c. 3.

[30] Perhaps it is significant that the dissolution suits ceased with the advent of Harry M. Daugherty to the attorney-generalship.

[31] The difficulties of competition in the bituminous field are admirably set out in HAMILTON AND WRIGHT, THE CASE OF BITUMINOUS COAL (1926).

JURISDICTION OF BANKRUPTCY COURT OVER FORECLOSURE IN OTHER COURTS OF MORTGAGES ON BANKRUPT'S PROPERTY

As a result of judicial intermixture of fictional concepts and practical demands, jurisdictional questions relating to the enforcement of mortgage liens against bankrupt mortgagors have been the source of abundant conflict of decisions and endless confusion.[1] It is established that upon adjudication in bankruptcy the title and right to possession of all of the bankrupt's property wherever it may be found[2] vests from the time of the filing of the petition[3] in the trustee subject to the jurisdiction of the bankruptcy court.[4] There is also some consistency in the principles governing the procedure of enforcement of mortgage liens by the bankruptcy court upon application by the mortgagee.[5] Discord arises, however, in the event of an attempt by a lienor

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[1] 5 REMINGTON, BANKRUPTCY (3d ed. 1923) c. 23; GILBERT'S COLLIER ON BANKRUPTCY (2d ed. 1931) 502-549. *Cf.*, for a general discussion on conflicting jurisdiction between federal and state courts in bankruptcy, Note (1928) 42 HARV. L. REV. 119.

[2] The Bankruptcy Act, section 2, as amended in 1910, authorized ancillary proceedings by all courts of bankruptcy in aid of a receiver or trustee appointed in proceedings pending in any other court of bankruptcy. 36 STAT. 838, 839 (1910), 11 U. S. C. § 11 (20) (1926).

[3] 30 STAT. 544 (1898), 11 U. S. C. § 110 (1926); Robertson v. Howard, 229 U. S. 254, 33 Sup. Ct. 854 (1913).

[4] Mueller v. Nugent, 184 U. S. 1, 22 Sup. Ct. 269 (1902). In enforcing this custody by injunction, as discussed *infra*, the bankruptcy courts rely upon Section 2, which generally defines the powers of the bankruptcy courts, and particularly par. 15, which authorizes issuance of such orders as are necessary for the enforcement of the provisions of the Act. 30 STAT. 545 (1898), 11 U. S. C. § 11 (20) (1926).

[5] *Cf.* In re Hasie, 206 Fed. 789 (N. D. Tex. 1913), for a short summary of ordinary foreclosure procedure in bankruptcy court.

The trustee takes only the bankrupt's title and the property remains subject to all valid preexisting liens by Section 57 of the Bankruptcy Act. The mortgagee may apply to the bankruptcy court for sale of the mortgaged property, the proceeds to be credited on his debt, and file claim entitling him to the status of a general creditor in case of deficit on the sale by virtue of general order 28 of the United States Supreme Court. 18 Sup. Ct. VIII. The trustee and bankruptcy court may refuse to administer the property if it should appear that the entire value of the property is insufficient to pay off the incumbrance. *Cf.* In re Keet, 128 Fed. 651, 652 (M. D. Pa. 1903). Or it may conduct the sale free of lien in case the lien is not redeemed. In re Cutler, 228 Fed. 771 (E. D. N. C. 1916). The failure of the mortgagee to file any claim or appear in the bankruptcy court only defeats his status as an unsecured creditor and does not affect his right to rely upon his security and reclaim the proceeds of the lien from the sale by the bankruptcy court. Yeateman v. Institution, 95 U. S. 764 (1877); Ward v. Bank of Ironton, 202 Fed. 609 (C. C. A. 6th, 1913); see In re Goldsmith, 118 Fed. 763, 766 (N. D. Texas 1902).

to enforce the security outside the bankruptcy court, when it becomes necessary to determine the extent of the bankruptcy court's jurisdiction. This question may be decisive (1) when a foreclosure suit has been instituted in another court, usually a state court, before the petition;[6] (2) where foreclosure proceedings are commenced after the petition in a state court with the consent of the bankruptcy court;[7] (3) where such consent is not secured to a foreclosure in another court;[8] (4) where there is a power of sale mortgage,[9] and also (5) where there is a pledge of personalty with a power of sale.[10]

When the decision in *Isaacs v. Hobbs Tie and Timber Co.*[11] was handed down by the Supreme Court last spring, its effect upon foreclosure practice in these situations became a subject of widespread conjecture and some trepidation.[12] The actual decision was not startling, merely providing the trustee with another procedural device, plea in abatement, for checking a foreclosure action instituted in the state court after the filing of the petition in bankruptcy.[13] But in the course of the opinion it was said:

"When this jurisdiction has attached the court's possession *cannot* be affected by actions in other courts.... Thus while valid liens existing at the time of the commencement of a bankruptcy proceeding are preserved, it is solely within the power of the court of bankruptcy to ascertain their validity and amount and to decree the method of liquidation.... The exercise of this function *necessarily* forbids interference with it by foreclosure proceedings in other courts...."

These statements, if literally interpreted, might serve as a basis for nullifying all foreclosure proceedings outside the court of bankruptcy,[14] endanger all land titles thereby obtained, and necessitate radical changes in present foreclosure practice.

The fate of mortgage foreclosure proceedings begun in state

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[6] In re Marts, 38 F. (2d) 283 (D. N. J. 1930).

[7] See In re Zehner, 193 Fed. 787, 790 (E. D. La. 1912).

[8] In re Dyer, 8 F. (2d) 376 (D. N. J. 1924).

[9] Robinson v. Kay, 7 F. (2d) 576 (C. C. A. 9th, 1925).

[10] In re Southern Pharmaceutical Co., 286 Fed. 148 (E. D. Tenn. 1921).

[11] 282 U. S. 734, 51 Sup. Ct. 270 (Feb. 24, 1931); (1931) 31 COL. L. REV. 1036, (1931) 16 MINN. L. REV. 94.

[12] Rintels, *Mortgage Foreclosure under the Hobbs Case*, Commercial Law Journal, July, 1931, at 337; Parsons, National Titleman, June, 1931; Isaacs, Credit Executive, May, 1931; Cranmer, American Bankruptcy Review, Aug., 1931; also see Journal of the National Ass'n of Referees in Bankruptcy, July, 1931 at 175.

[13] The usual method of accomplishing the same result is by injunction issued by the bankruptcy court.

[14] Rintels, *op. cit. supra* note 12.

courts prior to bankruptcy brings the concept of bankruptcy jurisdiction into relief against the more general principle of comity that the court first acquiring jurisdiction over the parties and subject matter should not be interfered with.[15] It has never been supposed that the jurisdiction of the state court could be defeated by the bankruptcy of the mortgagor in the absence of a stay by the bankruptcy court.[16] Nor is it doubted that the bankruptcy court may always temporarily restrain the state court action pending the appointment of a trustee to assume the place of the bankrupt.[17] But whether the bankruptcy court is empowered permanently to enjoin the continuance of foreclosure proceedings begun before the filing of the petition in bankruptcy, or whether, if it have the power, it will be inclined to enjoin at the request of the trustee, is difficult to determine from the previous decisions.[18] In some instances injunctions have been granted expressly on the theory of the exclusive and paramount jurisdiction of the bankruptcy court.[19] Some of these cases either expressly or impliedly ground their injunction on the fact that at the time of petition or injunction the state court had no actual possession of the property.[20] In another early federal decision,

[15] Pickens v. Roy, 187 U. S. 127, 23 Sup. Ct. 78 (1902); Murphy v. Hofman Co., 211 U. S. 562, 29 Sup. Ct. 154 (1909).

[16] Friedman v. Zweifler, 74 Misc. 448, 132 N. Y. Supp. 320 (Sup. Ct. 1911) (action for goods sold and delivered); Hobbs v. Head & Dawst Co., 184 Fed. 409 (C. C. A. 5th, 1911) (mechanic's lien).

[17] In re Morse, 210 Fed. 900 (N. D. N. Y. 1914); *cf.* In re Emslie, 102 Fed. 292 (C. C. A. 2d, 1900).

[18] Cases denying injunction: In re Rohrer, 117 Fed. 331 (C. C. A. 6th, 1910); In re Wagner's Estate, 206 Fed. 364 (E. D. Penn. 1913); In re Schmidt, 224 Fed. 814 (D. N. J. 1915). Cases allowing injunction: In re Dana, 167 Fed. 529 (C. C. A. 8th, 1909); First Savings Bank & Trust Co. v. Butler, 282 Fed. 866 (C. C. A. 8th, 1922); In re Kaplan, 144 Fed. 159 (N. D. Ga. 1905).

The same conflict ensues in regard to judgment and attachment liens. *Cf.* Straton v. New, *infra* note 29, footnote 6. The jurisdiction of the bankruptcy court is supplemented in these cases by the power to enjoin the enforcement of any lien created in state court legal proceedings within four months of the bankruptcy petition while the bankrupt was insolvent. Clarke v. Larremore, 188 U. S. 846, 23 Sup. Ct. 363 (1902). *Cf.* REMINGTON, *op. cit. supra* note 1, at 115 *et seq.*

[19] Loisel v. Dornier, 213 Fed. 396 (E. D. La. 1914), *aff'd* Pugh v. Loisel, 219 Fed. 417 (C. C. A. 5th, 1915); First Savings Bank & Trust Co. v. Butler, *supra* note 17, at 868; In re Knight, 125 Fed. 35 (W. D. Ky. 1903) (holding that bankruptcy court will have exclusive jurisdiction over any property sequestrated by the state court within four months). *Cf.* Coal Land Co. v. Ruffner, 165 Fed. 881 (C. C. A. 4th, 1908); Bothwell v. Fitzgerald, 219 Fed. 408 (C. C. A. 9th, 1915); (1931) 16 MINN. L. REV. 94.

[20] In re Dana, *supra* note 18 (state court receiver had voluntarily surrendered possession of property in question to bankruptcy court at time of the injunction); First Savings Bank & Trust Co. v. Butler, *supra* note 18 (no actual possession taken by the state court receiver until after

the court, while refusing to enjoin, looked upon the granting of the injunction purely as a matter of discretion to be governed by a consideration of the equity of unsecured creditors and the danger thereto in state court proceedings.[21]

The opposing and preponderant authority,[22] however, disapprove the paramount and exclusive jurisdiction theory in favor of one of concurrent jurisdiction, but it is not clear whether they refuse to allow interference as a matter of comity or absolutely deny the power to the bankruptcy court.[23] Furthermore, there is doubt whether a constructive possession by the state court acquired by commencement of the foreclosure action, with jurisdiction of the parties and the subject matter, is sufficient[24] to preclude interference, or whether actual possession by the receiver[25] at the time of the petition is necessary.[26] A recent

adjudication in bankruptcy although foreclosure action was begun before filing of petition).

[21] In re Holloway, 93 Fed. 638 (D. C. Ky. 1899). *Cf.* In re United Graphite Co., 161 Fed. 583 (E. D. Pa. 1908).

[22] Cases cited in Straton v. New, *infra* note 29, at footnote 6.

[23] See Bean v. American Trust & Savings Bank, 271 S. W. 1111, 1114 (1925); see Hooks v. Aldridge, 145 Fed. 865 (C. C. A. 5th, 1906). It should be noted that the so-called paramount and exclusive jurisdiction theory is dominant in situations in which the bankruptcy court has prior custody due to possession in the bankrupt at the time of bankruptcy, when no state foreclosure action is pending. *Cf.* note 43, *infra.* Furthermore, suits to enforce liens acquired by legal proceedings within four months, suits with regard to general assignments for the benefit of creditors within four months, and state insolvency proceedings over which the power of the bankruptcy court is paramount, must be distinguished from the cases involving foreclosure of mortgage liens.

[24] Bryan v. Speakman, No. 6288. C. C. A. 5th, Nov. 2, 1931. The court held that the jurisdiction to adjudicate concerning the subject matter of and the issues arising in the suit filed to foreclose a specific mortgage lien, the validity of which was in doubt, was acquired by the state court when the complaint was sanctioned and filed. Thereafter, as long as the cause was prosecuted no other court could interfere with the *res*, and a state court receiver actually appointed after bankruptcy had intervened was held entitled to possession as against the bankruptcy receiver previously in possession.

This case reversed the district court decision denying possession to the state court receiver because all subsequent proceedings in the state court would be forbidden since the bankruptcy court was the court of primary jurisdiction in whom, according to Isaacs v. Hobbs, was the ultimate decision as to validity. In re Lookout Mountain Hotel Co., 50 F. (2d) 421 (N. D. Ga. 1931).

The circuit court pointed out that Isaac v. Hobbs did not support these conclusions since it applied to actions commenced in other courts after the bankruptcy petition and that in the case at bar the state court had begun the action before bankruptcy.

[25] The status of the state court receiver is often of prime importance. He ranks as an adverse claimant who cannot be ordered summarily to surrender the bankrupt's property where he was appointed before the petition

case[27] denied, however, the operative effect of any actual possession theory that may be implicit in the cases. A well considered state court opinion[28] recognizing the whole question of intervention as unsettled by the Federal Supreme Court, stated the ordinary rule to be that the state court should not be stayed particularly when property is in its actual possession.

That *Isaacs v. Hobbs* marks no radical departure from this particular mortgage foreclosure practice is apparent from the more recent decision of the Supreme Court in *Straton v. New*.[29] There it was held that a creditor's suit to enforce a valid judgment lien filed in a state court was not affected by a bankruptcy petition filed five and one half months later and that the court of bankruptcy had no jurisdiction to enjoin the proceeding. Mr. Justice Roberts, author of the opinion in the *Hobbs* case, clearly indicated that the weight of federal authority was that the bankruptcy court could not enjoin the enforcement of a valid lien more than four months old in any proceeding brought prior

of bankruptcy in an action to foreclose a mortgage lien. In re Iroquois Utilities, Inc., 297 Fed. 397 (C. C. A. 2d, 1924).

Ordinarily a state court receiver may be divested of possession of the property by order of the bankruptcy court if he was appointed as receiver for the benefit of creditors in insolvency proceedings within four months of bankruptcy. *Cf.* REMINGTON, *op. cit. supra* note 1, at 117 *et seq.* Note (1929) 14 MINN. L. REV. 638. But if he is appointed in a suit to enforce a lien with incidental prayer for general insolvency, he is not divested of the assets covered by the lien but may hold them for foreclosure. Carling v. Seymour Lumber Co., 113 Fed. 483 (C. C. A. 5th, 1902). See In re Rathman, 183 Fed. 913, 923 (C. C. A. 8th, 1910).

[26] In First Savings Bank & Trust Co. v. Butler, *supra* note 18, it is held by implication that the institution of a foreclosure suit in the state court before the filing of the petition where the state court does not appoint a receiver until after adjudication though before the appointment of the trustee in bankruptcy, is not such a taking of custody of the *res* as will prevent the bankruptcy court from interference.

Cf. In re Wills, 114 Fed. 222 (W. D. Mo. 1902). The court applied the physical possession test to refuse an injunction against prosecution of replevin in a state court action begun after the filing of the petition but before adjudication, before any bankruptcy officer actually took possession or any restraining order was applied for.

[27] See Bryan v. Speakman, *supra* note 24. Any rule allowing the bankruptcy court to intervene in event it received actual possession after the filing of the foreclosure suit seems unsound realistically since there would be less danger of a loss to the unsecured creditors by state court action when the trustee was actually present so as to be in actual possession than when there was no possession and inertia or absence of trustee might be dangerous.

[28] Bean v. American Trust & Savings Bank, *supra* note 23. The court expressed the feeling that in case of such an injunction against the parties proceeding in the state court, the place of appeal is to a higher federal court and a counter injunction by a state court should be refused as causing an unseemly conflict of jurisdiction.

[29] 283 U. S. 318, 51 Sup. Ct. 465 (April 20, 1931).

to the filing of the petition.[30] And in reliance on this case a subsequent federal decision [31] upheld the foreclosure of a mortgage lien in a state court brought five months before bankruptcy. The preponderant policy of non-interference thus recognized appears desirable because it avoids conflicts of jurisdiction [32] and the additional costs and delay resulting from new proceedings.

Bankruptcy courts sometimes consent to delegate their jurisdiction to foreclose mortgage liens on property in their possession to state courts [33] when the trustee is joined as a party defendant in the state action. This consent, a discretionary matter with the bankruptcy court,[34] may be refused regardless of the increased costs of proceeding in the bankruptcy court,[35] and is often denied for the protection of a probable equity of unsecured creditors.[36] Yet the availability of the device enables the bankruptcy court to rid itself of onerous proceedings,[37] transfer foreclosure proceedings for distant property to a court conveniently located at the *situs* of the *res*,[38] and save additional costs that the bankruptcy court proceeding might involve.[39] The fear that *Isaacs v. Hobbs* denied the power so to consent [40] was removed by

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[30] See Straton v. New, *supra* note 29 at 331, 51 Sup. Ct. at 470.

[31] Russell v. Edmondson, 50 F. (2d) 175 (C. C. A. 5th, May 29, 1931). Accord: McGonigle v. Foutch, 51 F. (2d) 455 (C. C. A. 8th, June 8, 1931) (mechanic's lien over four month's old and the foreclosure of the lien begun within four months of bankruptcy). See Bryan v. Speakman, *supra* note 24.

[32] See Hooks v. Aldridge, *supra* note 23, at 865. This court feels that extreme care should be exercised in any intervention and the principles of comity should be recognized if practicable.

[33] In re San Gabriel Sanatorium Co., 111 Fed. 892 (C. C. A. 9th, 1901); McHenry v. La Société Francaise D' Eparguis, 95 U. S. 58 (1877); see In re Zehner, *infra* note 35, at 789.

[34] In re Southern Florida Realty Co., 15 F. (2d) 171 (S. D. Fla. 1926).

[35] In re Zehner, 193 Fed. 787 (E. D. La. 1912). However, the court attempts to refute these objections on ground that equivalent costs are required in state court proceedings and admits that a more forceful argument might be made in case the mortgagee had a right to enter and sell without judicial proceedings. *Cf.* In re Stewart, 193 Fed. 791 (E. D. La. 1912) (concerning whether costs of sale should be taken out of proceeds where there is a deficiency).

[36] In re Zehner, *supra* note 35; In re Southern Florida Realty Co., *supra* note 34.

[37] *Cf.* In re Hasie, *supra* note 5, at 792.

[38] The economic disadvantage of compelling a mortgagee to intervene in litigation far away from his home (in federal district court of his state with ancillary jurisdiction or in the bankruptcy court) to protect an investment of purely local character is a material consideration.

[39] Practicing attorneys have registered decided objections to the implications of the *Hobbs* case because they would cut off opportunity of avoiding by state court foreclosure the costs that are necessarily entailed in bankruptcy court foreclosure.

[40] See Cranmer, American Bankruptcy Review, *supra* note 12; see also

subsequent federal decisions upholding the power.[41]

Where a foreclosure action has been commenced in a state court after the petition in bankruptcy, and the consent of the bankruptcy court to such action is not obtained, different problems arise. As a matter of constant practice foreclosure proceedings are often initiated and completed in state courts without any formal consent of the bankruptcy court by simply joining and notifying the trustee. If he submits to the action, title passing at the foreclosure sale is not questioned.[42] But if he objects to the state action and petitions for an injunction, it is clearly within the power of the bankruptcy court to enjoin foreclosure proceedings against property in the actual possession of the bankrupt at the time of the petition.[43] These injunctions may be preliminary to a sale by the bankruptcy court [44] or to an investigation of the proceeding by the trustee, and are usually responsive to a petition by the trustee based on the existence of the equity of unsecured creditors.[45] One court refused to uphold a perpetual injunction, modifying the order to one for a reasonable time with leave to the mortgagee to appeal in case of an unreasonable delay by the bankruptcy court.[46] Another court in the presence of a claimed equity, while admitting its power, refused to enjoin the state action, and endorsed the policy of non-intervention except when necessary for protection of the equity, believing the remedy of trustee joinder in the state court action to be normally sufficient.[47]

It has been held that a mortgage foreclosure sale after bankruptcy without the consent of the bankruptcy court and joinder of the trustee as party defendant is illegal and that the trustee

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Isaacs, Credit Executive, *supra* note 12: "Under this decision the bankruptcy courts are held powerless to divide the responsibility of administering encumbered property with other courts. . . Bankruptcy courts cannot surrender their control of the assets to other courts. . ."

[41] In re Schulte United, Inc., 50 F. (2d) 243 (S. D. N. Y. March 24, 1931); In re Parrino, 50 F. (2d) 613 (E. D. N. Y. May 23, 1931). See Straton v. New, *supra* note 29, at 321, 51 Sup. Ct. at 466; In re Wakey, 50 F. (2d). 869, 870 (C. C. A. 7th, June 29, 1931).

[42] See First Trust Co. v. Baylor, 1 F. (2d) 24, 27 (C. C. A. 8th, 1924); see Ward v. Bank of Ironton, 202 Fed. 609, 612 (C. C. A. 6th, 1913).

[43] In re Larkin, 252 Fed. 885 (D. Mass. 1918) (property in possession of bankruptcy receiver); In re Dyer, 8 F. (2d) 376 (D. N. J. 1924) (Trustee and court admittedly had possession of the property from time of bankruptcy); In re Pittelkow, 92 Fed. 901 (E. D. Wis. 1899); First Trust Co. v. Baylor, *supra* note 42. See cases cited in Isaacs v. Hobbs, *supra* note 11.

[44] In re Booth, 96 Fed. 943. (N. D. Ga. 1899); In re Dyer, *supra* note 43.

[45] See cases in notes 43 and 44, *supra*.

[46] First Trust Co. v. Baylor, *supra* note 42.

[47] In re Porter, 109 Fed. 111 (D. Ky. 1901).

may recover the property.[48] But failure to join the trustee as a party defendant may particularize this holding. Nevertheless the *dictum* in *Isaacs v. Hobbs* has been hailed as invalidating any title passing in this type of action.[49] Another view is that consent can be implied from the failure to intervene and that the *Hobbs* case only suggests that formal consent be obtained.[50] But a subsequent case [51] involving a different fact set-up has interpreted the *Hobbs* case as nullifying action in the state courts unless consent of the bankruptcy court has first been obtained. This interpretation, removing as it does from the trustee the burden of interference, would effectuate the general policy of protecting the unsecured creditors by eliminating to some extent the danger of a sacrificial sale and dissipation of the equity of redemption which might follow from a failure of the trustee to resist.[52]

Mortgages issued with a power of sale on default are peculiar in that they entail no conflicting court jurisdiction. Two cases [53] have upheld the right of the holder of the power of sale to exercise it on default after bankruptcy without the consent of the bankruptcy court. Two cases allow an injunction before sale,[54] a third orders surrender of the security deed, [55] while a fourth denies the trustee of the deed of sale rents and profits from the land on the ground that a sale without the consent of the bankruptcy court is void.[56] Varying theories support these diversified results. The view that the power of sale is a contract right [57] to be cut across only in case of its fraudulent utilization [58] contrasts with that fixing it as a remedy which can be impaired by the administration of the bankruptcy court without affecting the contract.[59] Cases upholding the power also utilize a theory of possession, claiming that a notice of sale posted prior to the

[48] In re Brooks, 91 Fed. 508 (D. Nev. 1898). (Court here ordered return of property to trustee calling the sale illegal.)

[49] See Cranmer, *op. cit. supra* note 12.

[50] (1931) 31 COL. L. REV. 1036.

[51] See In re Wakey, 50 F. (2d) 869, 870 (C. C. A. 7th, June 29, 1931).

[52] See Journal of Nat'l Ass'n of Referees in Bankruptcy, July, 1931, at 176.

[53] In re Smith, 3 F. (2d) 40 (S. D. Tex. 1924); (deed of trust); Robinson v. Kay, 7 F. (2d) 576 (C. C. A. 9th, 1925).

[54] In re Jersey Island Packing Co., 138 Fed. 625 (C. C. A. 9th, 1905) (deed of trust); Allebach v. Thomas, 16 F. (2d) 853 (C. C. A. 4th, 1927) (deed of trust).

[55] Cohen v. Nixon & Wright, 236 Fed. 407 (S. D. Ga. 1916).

[56] In re Hasie, *supra* note 5.

[57] In re Smith, *supra* note 53.

[58] Hiscock v. Varick Bank, 206 U. S. 28, 27 Sup. Ct. 681 (1906) (pledge of securities with power).

[59] In re Jersey Island Packing Co., *supra* note 54.

bankruptcy petition transfers constructive possession to the mortgagee.[60] On the other hand, it has been held that such possession was cut across by a creditor's petition for bankruptcy court administration before sale.[61] The only realistic generalization which can be made is that the courts will allow creditors to cut across the power of sale to secure bankruptcy administration, but refuse to disturb the *status quo* where such power has been exercised. This lines up with the result in ordinary mortgage situation leaving the effect of *Isaacs v. Hobbs* as yet undeterminable.

The disposition of pledged securities with a power of sale[62] after bankruptcy was a question of less difficulty prior to that decision. The leading Supreme Court case upheld a sale after bankruptcy by the pledgee in accordance with the power of sale without the consent of the bankruptcy court,[63] limiting the right of the bankruptcy court to interfere to cases of fraud or violation of the provisions of the agreement as to sale. Two lower federal courts have refused to enjoin an exercise of the power.[64] In one case[65] the presence of a bankrupt's equity was alleged, while in the other[66] there was no mention made of the value of the pledge as compared to the size of the lien. These cases viewed section 57h of the Bankruptcy Act[67] as providing an exclusive method of sale through the bankruptcy court only in the absence of an agreement among the parties and as in no wise limiting a power agreed upon.

Recently, however, this procedure was completely disturbed

[60] See cases cited *supra*, note 53. The possession theory was used to effect a transfer of deeds and tracts to the custody of the trustee after bankruptcy in Cohen v. Nixon & Wright, *supra* note 55. In that case a state law of Georgia left the debtor in possession under a deed of trust.

[61] In re Jersey Island Packing Co., *supra* note 54.

[62] In the absence of any power of sale agreement, the bankruptcy court may enjoin sale of the collateral on default, or order it to be turned over to the trustee for disposition subject to the lien. See Wingert v. Kieffer, 29 F. (2d) 59, 60 (C. C. A. 4th, 1928).

[63] Hiscock v. Varick Bank, *supra* note 58. In this case insurance policies pledged as collateral were involved. The strength of the case is heightened by the fact that the pledgees bought the policies on the sale and gave no notice to the pledgor and the court failed to deny them any measure of the deficit still remaining. *Cf.* (1928) 14 VA. L. REV. 223 with regard to the power of the trustee to redeem property pledged after default.

[64] In re Browne, 104 Fed. 762 (E. D. Pa. 1900); In re Mayer, 157 Fed. 836 (C. C. A. 2d, 1907). See In re Pinkett, Douglas & Co., 50 F. (2d) 435, 439 (S. D. Cal. Mar. 30, 1931).

[65] In re Browne, *supra* note 64.

[66] In re Mayer, *supra* note 64. In several other cases where sale was allowed by the pledgee the security was of less value than the lien. See cases cited in (1931) 80 U. OF PA. L. REV. 124, footnote 7.

[67] 30 STAT. 560 (1898), 11 U. S. C. § 57h (1926).

by a federal court decision [68] which, on the strength of the *Hobbs* case, upheld an order of a referee enjoining the sale of stocks and bonds pledged as collateral under a power of sale agreement until the pledgee obtained the authorization of the bankruptcy court. This case ignored all past authority except the *Hobbs* case and emphasized the extension of the *Hobbs* rule from realty to personalty. Such a decision imposes inevitable hardship upon banks and other pledgees. Banks hold billions of dollars worth of these marketable collaterals as a source of liquid assets. Ability to dispose of them quickly after the default of a debtor in case of abnormal cash demands or under favorable market contions is essential to their safety and business technique.[69] The delay and occasional difficulty incurred in gaining the consent of the bankruptcy court would seriously delimit this ability. Likewise, the interest of the bankrupt's unsecured creditors in any remaining equity may be better protected by preservation of the pledgee's freedom to sell under favorable market conditions than by the mythical safeguard of a bankruptcy court's consent. That *Isaacs v. Hobbs* justifies or intended any such radical departure from present practice is highly questionable.

Jurisdictional principles with regard to the foreclosure of liens are not affected by questions concerning the determination of the validity of the liens themselves.[70] The court that first acquires jurisdiction over the *res* may determine all issues of validity connected with the mortgage.[71] A bankruptcy court may therefore enjoin enforcement of all invalid or undetermined liens on property within the possession of the bankrupt at the time of the filing of the petition.[72] When the property is in the possession of a third party at the time of the filing of the petition, the bankruptcy court, apparently has no power to issue an injunction.[73] It receives no constructive possession and

[68] In re Henry, 50 F. (2d) 453 (E. D. Pa. June 10, 1931); (1931) 80 U. OF PA. L. REV. 124.

[69] Paton, American Banker's Ass'n Journal, Sept. 1931, at 125.

[70] GILBERT'S COLLIER ON BANKRUPTCY (2d ed. 1931) pp. 502-552.

[71] In re Oswegatchie Chemical Products Corp., 279 Fed. 547 (C. C. A. 2d, 1922); Karasik v. Peoples Trust Co., 241 Fed. 939 (E. D. N. Y. 1917). The bankruptcy court may consent to a trial of validity in state court where a state law is particularly concerned. In re Johnson, 127 Fed. 618 (D. Nev. 1904). But even where such consent has been given the bankruptcy court can enjoin adverse claimant from proceeding further in the state court action. In re Schemerhorn, 145 Fed. 341 (C. C. A. 8th, 1906). See Bryan v. Speakman, *supra* note 24.

[72] In re Locust Bldg. Co., 272 Fed. 988 (E. D. N. Y. 1921); In re United States Chrysotile Asbestos Co., 253 Fed. 294 (S. D. N. Y. 1918); In re Donnelly, 188 Fed. 1001 (N. D. Ohio 1910).

[73] United Cent. Life Ins. Co. v. Baer Co. Limited, 10 F. (2d) 153 (C. C. A. 5th, 1925) (property was conveyed by bankrupt to his wife less than four months before bankruptcy and not in his possession at the time of the

the trustee's only remedy is a plenary suit to recover possession,[74] over which the state and federal courts have concurrent jurisdiction,[75] distinct from bankruptcy proceedings.

The exact bearing of *Isaacs v. Hobbs* on this whole field of procedural jurisdiction over mortgage foreclosure remains a matter of speculation. The limitations placed upon its *dicta* by Mr. Justice Roberts himself and their interpretation in succeeding federal court decisions indicate a continuance of the previous practices as to suits begun in state courts before the petition and those begun after the petition with consent. The matter of a foreclosure in a state court begun after the petition without consent has not as yet been ruled upon, despite a *dictum* in *In re Henry* to the contrary.[76]

Past litigation on the immediate subject discloses varied results whose ultimate end was the fair and efficient settlement of the bankrupt's estate featured by adequate protection of the equity of the unsecured creditors. The machinery of jurisdiction in vogue seems satisfactory in its realistic and functional results. Yet these results have been accompanied with a confusing juristic rationalization, faithfully illustrated in the *Hobbs* case, which has produced an abundance of costly litigation. It is submitted that the whole problem of foreclosure of mortgages on the bankrupt's property should be a matter within the discretion of the bankruptcy court, which could be exercised so as to secure the most efficient and equitable settlement, in keeping with the spirit of the Bankruptcy Act, and eliminating the procedural tangle that the present jurisdictional approach has produced.

LEGALITY OF MORTGAGE PARTICIPATIONS AS TRUST INVESTMENTS

SINCE the traditional delimitation of legal investments for trust funds has tended to relieve the eligible securities of much of the strain of competing for a market, and thus resulted in consistently lower yields,[1] mortgages on realty, offering greater pro-

petition); Ft. Dearborn Trust & Savings Bank v. Smalley, 298 Fed. 45 (C. C. A. 8th, 1924) (property, at time of the petition, in possession of a third party, who sued in the state court for specific performance of a contract to sell and joined the mortgagee with the bankrupt's trustees. Mortgagee filed cross bill for foreclosure in that suit.)

[74] See United Cent. Life Ins. Co. v. Baer Co. Limited, *supra* note 73, at 154.

[75] Weidhorn v. Levy, 253 U. S. 268, 40 Sup. Ct. 534 (1920).

[76] See In re Henry, *supra* note 68, at 454.

[1] Berger, *Pooling or Participation Mortgages as Investments for Trust Funds* (1929) 48 TRUST COMPANIES 599.

ductivity with equal security, have always been favored as trust investments.[2] But the high realty values frequently existing in the large cities precluded the investment therein of small trust funds,[3] which in themselves are steadily increasing in number, and in addition commonly remain as fractional residues after the investment of large funds.[4] In response to these exigencies, trust companies devised plans permitting investments in mortgage participations.[5] In elementary form the plan involves an allocation of undivided interests either in one mortgage or in a group of pooled mortgages held by the trustee to trust funds in its hands.[6] A more complex plan is introduced when one trust company holds the mortgages, and not only assigns undivided interests to trust funds in its own hands but also sells certificates of participation in which other trustees may invest their trust funds.[7] From these two basic plans innumerable variations proceed.

The widespread adoption of mortgage participation plans by outstanding trust companies undoubtedly argues for their legality.[8] But the paucity of cases and the divergence of opinion among lawyers,[9] as well as the palpable differences existing between various forms of participation plans, render any generalized prediction uncertain.[10]

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[2] By the English common law rule, adopted in many states, only real property and government obligations were considered proper investments. See Simmons v. Oliver, 74 Wis. 633, 636, 43 N. W. 561, 562 (1889).

[3] See *The Handling of Small Estates and Trusts* (1930) 50 TRUST COMPANIES 684.

[4] Sisson, *Survey Reveals Another Record Year for Trust Business* (1930) 50 TRUST COMPANIES 199; Miller, *Allocation of Small Trust Balances to Mortgages and Bonds* (1930) 50 TRUST COMPANIES 581; *cf.* Duffy, *Systematic Review and Analysis of Trust Investments* (1930) 50 TRUST COMPANIES 899.

[5] See editorial comment in (1929) 48 TRUST COMPANIES 718; Chandler *New Problems and Solutions in Investment of Trust Funds* (1928) 47 TRUST COMPANIES 621; LORING, A TRUSTEE'S HANDBOOK (1928) 135.

[6] See Standeven, *Installation and Operation of "Mortgage Investment Trust Account"* (1929) 49 TRUST COMPANIES 663. In New York participations in a single mortgage were early allowed by statute. N. Y. Laws (1917) c. 385.

[7] See Standeven, *op. cit. supra* note 6, at 664, 666.

[8] See MCKINNEY, TRUST INVESTMENTS (1927) 29; *The Handling of Small Estates and Trusts* (1930) 50 TRUST COMPANIES 684. The most recent tendencies in participation are exemplified by the plans of the Lawyers' Title and Mortgage Company and the New York Title and Mortgage Company, both of New York City.

[9] The JOURNAL was advised that on a recent mortgage participation plan two leading firms of New York City gave written opinions reaching diametrically opposite conclusions.

[10] *Cf.* Miller, *op. cit. supra* note 4. For a general presentation of the problems in this connection see *Undermining Integrity of Legal Investments for Trust Funds* (1930) 50 TRUSTS COMPANIES 182; Fenninger, *Cur-*

Since trust funds cannot be invested in the name of an individual and the *cestui* must be enabled to proceed against the security,[11] a declaration of trust in the mortgages is essential to the validity of any such plan of mortgage participation. Requirements for a declaration of trust in realty vary among the respective states, some prescribing that the trust be "created and declared" in writing,[12] others allowing it to be "manifested and proved" by writing.[13] It has been submitted that a mortgage participation plan necessitates a contemporaneous document acknowledging and securing the investment to all concerned,[14] and this is undoubtedly the prevailing practice. Under some existing plans the company issuing the certificates of interest assigns the mortgages in trust to another eligible company.[15]

It has frequently been urged as an objection to mortgage participation for trustees that a commingling of trust funds, proscribed at common law,[16] is inherent in any variation of the plan.[17] The precise evil of commingling trust funds, however, has never been clearly articulated by the courts. In many cases, cited for the common law interdiction, the individual funds of the trustee had been fused with those of the *cestui*,[18] thus offending the requirement that a trustee must not reap personal advantages to the possible detriment of the beneficiaries. These cases are not strictly applicable to a mingling of two or more trust funds, and are weakened by decisions which have countenanced the merger of individual and trust funds when the ultimate invest-

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rent and Prospective Problems Effecting Investment of Trust Funds (1931). 51 TRUST COMPANIES 761.

[11] Matter of Union Trust Co., 219 N. Y. 514, 114 N. E. 1057 (1916); Cornet v. Cornet, 269 Mo. 298, 190 S. W. 333 (1916). By a New York statute, however, a trust company may keep trust funds on deposit in its own name awaiting investment. N. Y. Laws (1917) c. 385.

[12] Gaylord v. City of Lafayette, 115 Ind. 423, 17 N. E. 899 (1888); Hutchins v. Van Vechten, 140 N. Y. 115, 35 N. E. 446 (1893) (early New York rule).

[13] This rule, adopted in the majority of the states, represents a literal interpretation of Section 7 of the Statute of Frauds. BOGERT, TRUSTS (1921) 54 *et seq.*

[14] Standeven, *op. cit. supra* note 6, at 664; Berger, *op. cit. supra* note 1, at 600.

[15] *Cf.* Berger, *op. cit. supra* note 1, at 600.

[16] 1 PERRY, TRUSTS AND TRUSTEES (1929) § 463.

[17] See *Undermining Integrity of Legal Investments for Trust Funds, supra* note 10.

[18] De Jarnette v. De Jarnette, 41 Ala. 708 (1868); The Boston & Colo. Smelting Co. v. Reed, 23 Colo. 523, 48 Pac. 515 (1897); Dunn v. Dunn, 137 N. C. 533, 50 S. E. 212 (1905); Re Edmund Hodges' Estate, 66 Vt. 70, 28 Atl. 663 (1894).

ment is thereby more profitable.[19] In other cases the commingling merely furnishes additional evidence of negligence, which is the ultimate *ratio decidendi*.[20] And in a number, the persuasive facts seem to have been the falsified or incomplete records kept by the trustee, preventing identification and proper division of the separate funds.[21] Perhaps with these distinctions in mind, the New York Court of Appeals, in *Matter of Union Trust Co.*[22] approved trustee's accounts disclosing that the several trusts had been accorded ratable participation in a mortgage, on the grounds that the complete and open records were sufficient answer in a suit upon an accounting, and, while professing to follow the common law prohibition against commingling of trust funds, recognized the legality of commingling under proper circumstances.

Since the majority of states prescribe a ratio between the amount of money loaned on a mortgage and the appraised value of mortgaged property [23] a mortgage participation plan, although originally valid, may be rendered invalid for trust funds by a depreciation of land values. Many recent participation plans, perhaps in view of this contingency, add a guarantee of payment and/or a guarantee of the underlying mortgages running to the participants, and/or a provision allowing substitutions of the mortgages.[24] The guarantee of payment clause will probably prove ineffectual to obviate the necessity of maintaining the statutory ratio, not only because, under some existing statutes, it is debatable whether the issuing companies have the power to make such a guarantee,[25] but also because, to the participant, it would be no more than an unsecured promise of the primary company, which alone could not make an improper investment legal. And since the statutes prescribing the ratio must be construed as mandatory, a guarantee of the underlying mortgages would seem to be of value only if interpreted to provide for the substitution of proper mortgages to maintain the required ratio, plus an assurance of promptness in the readjustment.

[19] Barney v. Parsons, 54 Vt. 623 (1882); Barry v. Lambert 98 N. Y. 300 (1885).

[20] *Cf.* Nance v. Nance, 1 S. C. 209 (1869); Dunn v. Dunn, *supra* note 18.

[21] Lannin v. Buckley, 256 Mass. 78, 152 N. E. 71 (1926); *cf.* Chesterman v. Eyland, 81 N. Y. 398 (1880).

[22] *Supra* note 11.

[23] Statutes are collected in MCKINNEY, *op. cit. supra* note 8.

[24] The plan of the New York Title and Mortgage Company under which certificates series C3 were issued contains typical guarantee and substitution provisions. For a discussion of guarantee provisions see Fenninger, *op. cit. supra* note 10, at 766.

[25] In Pennsylvania the attorney-general ruled that, while mortgage guaranty companies might guarantee participation certificates, banks could not. (1927) Op. Att'y Gen. 46, 70.

But the power of the issuing company to make substitutions for the original mortgages after the inception of the plan, whether expressed or implied, appears to cut across the common law prohibition against the delegation of trust powers. While ministerial and clerical duties of the trustee may be delegated,[26] it is uncontested that control over the security pledged for trust funds does not come within this category.[27] And by investing in participation certificates the immediate trustee clearly forfeits some "control" over the security underlying the investment.[28] It is arguable that the issuing company having itself made a declaration of trust in favor of the participants is qualified to perform trustee's functions in controlling the security. And a possible analogy may be found in those cases which have allowed trustees to invest in corporate bonds secured by realty even in the absence of express statutory sanction.[29] Moreover, since the power of substitution may be construed merely to obligate the issuing company to maintain the proper ratio, delegation within such narrow limits may not vitiate the entire plan.

Some recent participation plans, however, also contemplate the substitution of government or municipal bonds and even cash.[30] This is the result of sales experience which has shown to the issuing companies that prospective customers would be lost unless orders could be accepted pending the appearance of eligible mortgages. To prevent the loss of such orders, the temporary use of allowable securities would certainly not invalidate an otherwise valid plan. Moreover the use of even moneys or cash[31] may prove innocuous if the courts liberally interpret the provisions for the deposit of such non-legals as temporary place-

[26] Annis v. Annis, 61 Iowa 220, 16 N. W. 97 (1883); Olcott v. Gabert 86 Tex. 121, 23 S. W. 985 (1893).

[27] North American Trust Co. v. Chappell, 70 Ark. 507, 69 S. W. 546 (1902); Coleman v. Connolly, 242 Ill. 574, 90 N. E. 278 (1909); Stevens v. Home Insurance Co., 199 Mo. App. 536, 204 S. W. 44 (1918) (power to indorse a draft could not be delegated); Morville v. Fowle, 144 Mass. 109, 10 N. E. 766 (1887); Fowler v. Coates, 201 N. Y. 257, 94 N. E. 997 (1911).

[28] The power of substitution in mortgage participation has been severely criticized on the ground that the funds should have a specific, known security back of them and that even the reputation of the larger and better known issuing companies is not an adequate safeguard against the substitution of less desirable mortgages. *Undermining Integrity of Legal Investments for Trust Funds, supra* note 10.

[29] Green v. Crapo, 181 Mass. 55, 62 N. E. 956 (1902); *cf.* Appeal of Davis, 183 Mass. 499, 67 N. E. 604 (1903).

[30] See note 8, *supra.*

[31] Trust funds may not be invested in certificates of deposit, McKINNEY, *op. cit. supra* note 8, at 42; Baer's Appeal, 127 Pa. 360, 18 Atl. 1 (1889); nor in unsecured promises, Wilmerding v. McKesson, 103 N. Y. 329, 8 N. E. 665 (1886); Conigland v. Gooch, 97 N. C. 186, 1 S. E. 653 (1887).

ments of trust funds pending the investments in legals.[32]

In view of the prevalence of mortgage participation plans and the attendant uncertainty of their validity for the investment of trust funds, it was inevitable that statutory regulations should be passed. Where there is only a general statute permitting the approval of trustee's investments by courts,[33] the investment of particular trust funds in a mortgage participation may win approval, while the legality of the plan as a whole remains undetermined. Another type of statute permits the investment of trust funds in all or part of issues of bonds or notes secured by first lien mortgages or deeds of trust upon real estate,[34] and while literally including mortgage participation the provision might conceivably be restricted to the normal type of bond issue. The third type of statute, found in New York,[35] New Jersey,[36] Pennsylvania[37] and Rhode Island,[38] permits mortgage participations, *eo nomine*, and enumerates the permitted characteristics of the plans.

Even under the third type of statute, however, uncertainty remains. The New York statute does not expressly refer to a power of substitution, and, in designating mortgages as eligible investments, uses the term indiscriminately in the singular and the plural.[39] Yet it was very probably designed to validate both the power of substitution in the issuing company and the pooling of mortgages, in view of the fact that the legislature was aware

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[32] Participation plans might further be contested on the ground that, since the issuing company loans money on the mortgages at a higher rate of interest than the return promised to the participants, it obtains an incidental profit above the allowable commission if a part of the participation is allocated to trust funds in its own hands. It is quite possible that this objection will not be sustained in view of the higher yield accruing to the trust funds. See (1907) 20 HARV. L. REV. 337.

[33] ALASKA COMP. LAWS (1913) §1737; ARIZ. REV. CODE (1928) § § 4136, 4137 (Sections refer to guardians, allowing probate court to order investments); IDAHO COMP. STAT. (1919) § 7709; IND. ANN. STAT. (Burns, 1926) § 13470; MO. REV. STAT. (1919) § 103; MONT. REV. CODE (Choate, 1921) § 10306; W. VA. OFFICIAL CODE (1923) c. 44, § 4.

[34] COLO. COMP. LAWS (1921) § 5269; N. D. COMP. LAWS ANN. (1913) § 5198 (similar general provision); OKLA. COMP. LAWS ANN. (1921) § 4194.

[35] Decedent's Estate Law, § 111; Personal Property Law, § 21.

[36] N. J. COMP. STAT. (1910) Trustees, § 37a.

[37] PA. STAT. (West, 1920) Trustees, § 8570.

[38] R. I. GEN. LAWS (1923) Savings Banks § 1, Clause IX (c).

[39] "...trustee...may invest the same...in bonds and mortgages on unincumbered real property in this state worth fifty per centum more than the amount loaned thereon, and in shares or parts of such bonds and mortgages, provided that any share or part of such bond or mortgage so held shall not be subordinate to any other shares thereof and shall not be subject to any prior interest therein." Decedent's Estate Law, § 111.

of these features of the plans when the statute was passed.[40] There is a further question whether the provision that the interest of no participant shall be subordinate to that of another [41] was intended to preclude the payment of one before another in point of time, as the administration of the different trust estates might well require the prior liquidation of one fund. Likewise, in Pennsylvania the pertinent statute has proved so ambiguous as to provoke repeated calls on the attorney-general's office for clarification.[42] Eventually it was ruled that trust funds could not be placed in participating certificates, although there might be a division of one investment among different estates held in trust by the company.[43] A 1930 amendment apparently fails to remedy the inadequacy of previous legislation.[44]

In view of the demand for mortgage participations and the economic advantages furthered by their existence, it has been argued that even under common law the various plans would be upheld by the courts.[45] Until statutory validation, however, there will remain a degree of uncertainty that should be absent in the proper administration of trust funds. Existing legislation also leaves much to be desired. Provisions for liquidating the trusts when the beneficiary dies,[46] for the designation of the type and location of the mortgaged property, for the protection of "incidental profits" if such profits are permissible, and for recurrent valuations of the mortgaged property are not present in any of the statutes except by implications of debatable conclusiveness. More precise enactments, however, may be expected as the trust companies and other agencies are active in promoting and sponsoring revisions and new legislation.[47]

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[40] See (1928) Op. Att'y Gen. of N. Y. 211, 212.

[41] See note 39, *supra.*

[42] See (1926) Op. Att'y Gen. of Pa. 129, 152; (1927) Op. Att'y Gen. of Pa. 46, 68, 70.

[43] See (1927) Op. Att'y Gen. 57, 63.

[44] Called upon to interpret the amendment, the attorney-general concluded only that trustees could invest trust funds in first mortgages on real estate in Pennsylvania securing a collateral form note given by the individual owner and issued by a trust company organized under Pennsylvania law. (1930) Op. Att'y Gen. of Pa. 47, 54.

[45] McKINNEY, *loc. cit. supra* note 8.

[46] Where one bond and mortgage is held in trust by a company which allocates undivided interests to various trust funds in its own hands, the New York statute permits repurchase by the company; but where participation certificates are issued, no express provision is made. N. Y. Laws (1917) c. 385.

[47] The fact that banks, trust companies, and title and mortgage companies in the larger cities, where realty values are higher, had favorable experience with mortgage participation plans on improved urban property even during the drastic realty depreciation in recent years, will undoubtedly prove a persuasive influence on the first courts called upon to review the legality of the plans as investments for trustees, even when they include powers of substitution, renewal or extension of the mortgages pledged.