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Railroad Receivers

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--RAILROAD RECEIVERS--

THESIS

PRESENTED FOR THE DEGREE OF BACHELOR OF LAWS

-BY-

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The equitable remedy of a receiver is an exceedingly useful, and quite a necessary remedy in any period of active and extended business operations. It may reasonably be expected to be found developed to a greater or less degree of perfection and convenience wherever and whenever such activity and growth of business are to be found.

This is demonstrated by the fact that the Romans of long ago, having been a progressive and industrial people, found it necessary to have in connection with the great mass of business, and their relations with one another, a remedy similar to that of a receiver.

They therefore gave to their Praetors the extraordinary jurisdiction to appoint "persons in the nature of receivers".[1] This is probably the earliest mention of anything analogous to this most valuable, yet severe remedy that is to be found in the reports.

While in England though it is somethat difficult to determine the exact, or even an approximate date of the first use of this peculiar remedy, yet it seems safe to say that it was not extensively used in that country much before the reign of Elizabeth.(1558-1603)

However during the reign of Elizabeth, the appointment of sequestrators and receivers of rents and profits became

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(1) Spences Equitable Jurisdiction, Vol.I,p.673,n(f).

very common. And as little or nothing is said, or is to be found concerning this remedy or its use prior to that time, we may naturally conclude that that is about the origin or beginning of the law of receivers, as we find it set forth in the law of the present time.

One of the first reported English cases on receivers, is the case of Jordan v. Armes,[1] where certain property was sequestered"into the hands of the Chamberlain of London and one of the Aldermen pending the trial of the right of law, " and a receiver of real and personal property was appointed on May 20, 1588,[2] and again in 1590 a case is reported, where an order was given to show cause why a receiver, of a moiety of the rents and profits of a theatre, should not be appointed at the plaintiff's request.

The power of the Court of Chancery in England to appoint receivers, has very frequently been called into action since that time ; and all the leading principles in relation to it, may be said to have been well established there long before our Revolution ; and it was then and has ever since been considered as a power of as great utility as any of those belonging to the Court of Chancery. It is one of the oldest remedies in the Court of Chancery, and is founded on the inadequacy of the remedy to be obtained on the law side of the

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(1) Reg. Lib. 5 P. & M. fol.48.
(2) Spences Equitable Jurisdiction, Vol.I,p.673,n (f).

court.

During recent years the subject of receivers has come to be one of very great importance, both in this country and in England. This increased importance may be said to be largely due to the recent extended application of this remedy to the winding up of corporations, and especially railroad corporations. The vast importance of the subject may be more clearly comprehended by knowing that from the year 1875 to the year 1887, no less than (392) three hundred and ninety-two railways, having a capital stock and bonded indebtedness of more than twenty-three hundred and ten millions of dollars, and representing nearly (40,000) forty thousand miles of road have been sold in the United States under foreclosure proceedings. In the aggregate the interests of many thousands of persons were affected, and from one to nearly a dozen receiverships were involved in each case of these foreclosures.

This remedy is purely an equitable remedy and cannot therefore be obtained on the law side of the court. Pomeroy puts this remedy, under his classification, in what he styles the first class. His reason for assigning it to this class is, that the remedy of a receiver is entirely a provisional or ancillary remedy. It may be said to affect the nature of primary rights neither directly nor indirectly, but is only the method or means of the more efficiently preserving and protecting these primary rights, or of enforcing them in judicial proceedings.[1]

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(1) Pomeroy's Equity Jurisprudence, Vol. I, sec. 171.

A receiver is not the remedy, but only the method or means to an end. He may be said to be analogous to a sheriff in other cases.

A receiver is an indifferent person between the parties to a cause, appointed by the court to receive and preserve the property or fund in litigation pendente lite, when it does not seem reasonable to the court that either party should hold it.[1] He represents neither party to the action but is regarded as an officer of the court, and all that he may do is for the benefit of all parties in interest. Being an officer of the court, all property or funds entrusted to his care are considered as being in custodia legis, and such funds or property will be turned over to whoever eventually establishes title thereto.

Every kind of property of such a nature, that if legal it might be taken in execution, may if equitable, be put into the possession of a receiver ; and hence the appointment has been said to be an equitable execution. All statutes for the appointment of receivers must be strictly construed.

The causes for the appointment of a receiver are numerous, either to prevent fraud ; to save the subject of litigation from material injury ; or to rescue it from inevitable destruction. The power given to an equity court to grant a receiver pendente lite is regarded as one of the highest nature, and will not be used in cases where it would produce

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(1) High on Receivers, sec.1.

serious injustice, or injure private rights.

The duty of appointing a receiver is one of great delicacy and responsibility, and is discharged by the court only with the greatest caution, and only under such extraordinary circumstances as demand summary relief. The measure is a peremptory one and has the effect of temporarily depriving the defendant in possession of his property, before the court finally determines the rights of the parties in a decree or final judgment. Such an interference with the rights of a citizen, before a regular hearing and without the verdict of a jury, might be considered as a very grievous offence, and in contravention of the Constitution of the United States unless it was clearly exercised to prevent a manifest injury or wrong, or unless it be the only way of saving the plaintiff from irreparable loss.

A receiver appointed to preserve the fund or property pendente lite and for its ultimate disposal according to the rights or priorities of the parties entitled, such remedy instead of being looked upon as an attachment of the property, is regarded as being in the nature of a sequestration, and the person at whose instance the appointment is made, gains no advantage or priority over the other parties in interest.[1] Generally the object and purpose of appointing a receiver pendente lite is that of a provisional remedy ; as an aid or adjunct to the principal relief sought, and not necessarily

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(1) Beverley v.Brooke, 4 Grat. 187.

the ultimate object of the action. The appointment of a receiver pendente lite is to a great extent a matter resting in the judicial discretion of the court to which the application was made, unless the power is conferred by an enabling statute, and is governed by considering all the circumstances of the case.

As to the appointment of a receiver pendent lite over the mortgaged premises in a mortgage foreclosure suit against a natural person, it has long been well established that a court of equity has jurisdiction to appoint a receiver over such mortgaged premises, for the purpose of protecting the mortgagee, and in aid of actions for the foreclosure of mortgages.

But where adequate relief may be obtained by any other remedy or where such a proceeding is not deemed imperative by the court, this remedy or relief will not be granted. And when the court deems such remedy necessary it will always act with the utmost caution in appointing a receiver.

Mr. High states a rule in general terms as follows :-- "that in actions for the foreclosure of mortgages equity will not interfere by the appointment of a receiver, unless it is clearly shown that the security is inadequate", and that the mortgagor or other person primarily liable for the debt is insolvent and unable to make good any deficiency, "or that there is imminent danger of waste, destruction, or removal of the property from the jurisdiction of the court". 1

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(1) High on Receivers.

The court will not as a matter of course interfere by appointing a receiver in aid of foreclosure proceedings, first if the plaintiff fails to allege that there will be a deficiency, and if he is at liberty to obtain a decree of sale ; for this alone would be an adequate remedy and an equity court will not grant a receiver when any other adequate remedy exists. Second, where the mortgagor holds the legal title and is entitled to possession, the court will not appoint a receiver and disturb such possession, except in a clear case of fraud on the part of the mortgagor, or where the mortgagee's rights would be in great danger if a receiver was not appointed. Third, the court will not interfere with such possession of the mortgagor, if there is existing doubt as to the amount actually due under the mortgage, or if the defendant's answer denies the plaintiff's allegations of inadequacy of security.

The English doctrine makes a distinction between legal and equitable mortgages, in the appointment of receivers. Now since an equitable mortgage gives only an equitable interest and not a legal title, a receiver will be granted in behalf of an equitable mortgagee, when it would not be granted if such mortgagee had been a legal one. This is true for the reason that the legal mortgagee has other adequate remedies while the equitable mortgagee is without such remedy.

Lord Eldon's reason for this difference was that inasmuch as the legal mortgagee was entitled to immediate possession,

and could himself at once take possession and protect his interests, he therefore stood in no need of the aid of equity. Where there are several mortgages all subsequent to the first mortgage, the subsequent mortgages are regarded as equitable mortgages. The English doctrine has not been generally followed in this country, though it has been recognized.

But while under the English doctrine a receiver will not usually be appointed in behalf of the legal mortgagee, yet even under this rule if the legal mortgagee is unable to take possession, the reason for the rule has failed and he may have a receiver appointed in such a case.[1]

In Michigan it is provided by statute that the mortgagor is absolutely entitled to possession and no receiver will be appointed until the foreclosure becomes absolute.

The general rule as to rents and profits of a mortgaged premises pending a litigation is, that "in the absence of any especial equities, the mortgagee, as against the mortgagor in possession and those deriving title under him subsequent to the mortgage, is not entitled to a receiver of the rents and profits pendente lite, and a court of equity will usually leave the mortgagee to his action at law to recover possession for the rents and profits".2

A receiver pendent lite will not be appointed to collect and care for the rents and profits, where the mortgaged premises are an adequate security for the payment of the indebted-

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(1) Ackland v.Gravener, 31 Beav.484.
(2) High on Receivers, sec. 642.

ness, or when the mortgage indebtedness is not yet due.

But if the mortgagee obtains a receiver of the rents and profits, upon foreclosure proceedings and the amount received upon the sale of the premises proves insufficient to pay the indebtedness, he may have so much of the rents and profits in the receiver's hands as is necessary to make good such deficiency. We have already seen that the court must be convinced that the mortgage security is inadequate, before it will appoint a receiver at the request of the mortgagee. Such inadequacy is composed of two elements, namely the insufficiency of the mortgaged premises per se as a fund for cancelling the debt, and secondly, the fact of insolvency of the mortgagor or other person primarily liable for the debt, or of the fact of such persons being out of the jurisdiction of the court.

Generally speaking the term "inadequacy of security" includes both these elements, and the burden of proof is upon the plaintiff to prove the existence of both of these elements, else he will not be entitled to a receiver. If only one or the other of these elements is proved there will not be sufficient ground for the receiver's appointment. The inadequacy here mentioned means the inadequacy to discharge the particular mortgage of the plaintiff and not some other and subsequent mortgage. But this rule may and does include various other conditions in some of the states.[1]

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(1) Warwick v. Hummell,32 N.J. Eq.427.
Hill v. Robertson, 24 Miss.368.

In New York although statutes have changed the nature of mortgages from a conditional sale to that of a lien, yet the courts hold that these statutes do not affect the power of the court to appoint a receiver pendente lite. And if the mortgagor has allowed the taxes on the mortgaged property to remain unpaid so that such premises are liable to sale for the unpaid taxes, or if the mortgagor has covenanted to pay taxes and keep the premises insured but fails to do so, whereupon the mortgagee pays them, in such a case a receiver may be appointed to save the property.

And as frequently happens when the mortgaged property is so badly managed as to cause it to deteriorate in value, or where such deterioration arises from natural causes alone, a receiver will be appointed in these cases.

RECEIVERS IN JUDGMENT CREDITOR'S SUIT.

One of the most frequently invoked branches of the law of receivers, is that in aid of judgment creditors, in order that their judgments may be enforced after the usual legal remedies have failed. In such cases the aid of equity is necessary to protect the creditor.

The origin of this branch of the law of receivers was in the old English Court of Chancery, but the main instrument in developing the law into its present state, has been the decisions of the American courts.

The basis or fundamental reason for granting this remedy is beaause of the inadequacy of a legal remedy, and the consequent necessity of supplementing the legal remedy by the aid of equity.

The fact of the judgment creditor's inability to execute his judgment at law, was sufficient to entitle him to a receiver over the debtor's estate.[1] This principle may be regarded as the foundation for the entire equity jurisdiction, concerning receivers in creditor's suits, and in all probability underlies all the decisions in this country on this question. The courts of New York have had the greatest influence on the growth of this branch of the subject. Under the former Chancery practice in this state a receiver was appointed almost as a matter of course, to preserve the debtor's property pending the litigation, after return of execution unsatisfied.

If the judgment creditor filed a sworn bill, showing his equitable right to all the funds and property of the debtor, and if the defendant debtor did not deny this right, no reason existed for refusing the appointment of a receiver, even if the defendant answered that he had no property to protect.

And it was even considered to be the duty of the creditor, within a reasonable time after filing his bill, and obtaining an injunction to keep the debtor from interfering, to ask to

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(1) Curling v.Townshend,19 Ves.628.

have a receiver appointed to take charge of the debtor's assets, in order to further secure the collection of the debt.

In New York under the code this has been superseded by appointing a receiver on proceedings "supplemental to execution". Under this proceeding the debtor may be compelled to apply his concealed property, or such as might not be levied upon by execution, to the paying of the judgment.

But the judgment creditor must not be guilty of "laches" in asserting his rights and must file his bill within a reasonable time after the return of the execution unsatisfied, if he would have a receiver appointed. The judgment creditor must also fully and completely exhaust his legal remedies for the collection of the judgment before equity will appoint a receiver in his behalf.[1]

It is not now considered sufficient ground for appointing a receiver, where the execution is returned nulla bona before its "return day", because the court cannot know until that day whether or not the legal remedy will be adequate. And since the legal remedy of execution may accomplish payment the equity court will not interfere, until that remedy has failed.

As to general creditors who have acquired no lien upon the debtor's property, the weight of authority holds, that "in the absence of statutory provisions to the contrary, a general contract creditor before judgment, is not entitled

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(1) Parker v.Moore, 3 Edw.Ch.234.
Starr v. Rathbone,1 Barb. 70.

either to an injunction nor a receiver against his debtor, on whose property he has acquired no lien".[1] This is true even in case of fraud on the part of the debtor.[2]

There is an apparent exception to this rule in New York, in the case of an undisputed indebtedness due from a co-partnership, which is insolvent. And if the plaintiff creditor pursues this remedy in behalf of all the creditors a receiver will be granted before his debt is reduced to a judgment. And one more exception may here be noted, as where a creditor has advanced money for the necessary repairs of a vessel, or for necessary supplies and the master has in consequence of the advance assigned all his interest and lien as master, and all of the freight to the creditor. If such creditor shows to the court, the insolvency of the owners of the vessel, he will be granted a receiver and an injunction, to protect this assigned lien, to collect freight due and to apply the same on his debt.

Where a judgment debtor has fraudulently assigned his property for the purpose of hindering and delaying his creditors ; or where he assigns to a known insolvent assignee ; or where the debtor retains possession of the property after assignment, in all these cases a receiver will usually be appointed in behalf of the judgment creditor.

But the court while willing to aid judgment creditors will always proceed with extreme caution where the title to

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(1) High on Receivers, sec. 406.
(2) Rich v.Levy, 16 Md.74.

real estate claimed by and in the possession of third parties is the subject-matter contested. "As against the legal title the interposition is made with reluctance, and will only be done in case of fraud clearly proved, and danger to the property".[1]

The character of property over which a receiver may be appointed in behalf of judgment creditors, varies more or less with the jurisdiction of the court. In New Jersey a receiver may be appointed to take charge of rings, jewelry and etc.,[2] while in New York a receiver has been appointed over the notes of an insolvent firm,[3] so that it appears that a receiver appointed in aid of a judgment creditor may be extended to real or personal property or to property of almost any nature whatsoever.

RECEIVERS OVER PARTNERSHIP PROPERTY.

The power of a court of equity to appoint a receiver over partnership property is not to be questioned, for it is well settled that such power is fully vested in the court.

The purpose of appointing receivers in actions between partners, is to have an accounting and settlement of the partnership affairs, also to collect the debts, hold the

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(1) Vause v. Woods, 46 Miss. 128.
(2) Frazier v.Barnum, 4 C.E.Green 316.
(3) Webb v. Overman, 6 Abb. Pr. 92.

assets, in short to close up and bring to an end the business of the partnership.

When a receiver is asked for in such a case, the court is confronted with an exceedingly difficult problem, and has a very delicate duty to perform. If it grants a receiver on the one hand it puts an end to the partnership which one of the partners claims a right to have continued ; while on the other hand, if the court refuses a receiver, the defendant is at liberty to go on with the partnership business, at the risk and perhaps to the prejudice or loss of the partner praying for a receiver.

But sometimes it so happens that one thing or the other must be done, consequently the court has determined that certain circumstances will be sufficient ground for it to proceed one way while certain other circumstances will cause it to proceed differently. Under the English doctrine to entitle one to a receiver, the suit must be so framed that at the hearing a decree could be made, directing that the partnership be completely dissolved ; or that the business was carried on in violation of some instrument agreed upon by the parties as to the manner of carrying on the business.

In this country, however, the essential and controlling element necessary to the appointment of a receiver, is the probability of a decree for dissolution. The circumstances most readily allowing of the appointment of a receiver over partnerships may be divided into four classes, namely,

First, where the partner applying for dissolution is barred by the other partner or partners from participating in the profits, or in the management of the firm.

Second, in the case of any material violation of the partnership contract.

Third, in case of fraud.

Fourth, in the case of dissolution by death where the property is being mismanaged by the survivors.

But aside from these four general heads a partnership agreement, like any other lawful contract, is binding upon the parties and they must adhere to its terms. No partner may recede from such a contract without sufficient grounds for so doing.[1] The mere dissatisfaction of one partner is not sufficient ground for dissolution ; nor is the mere unprofitableness of the business if none of the elements under the four general heads above mentioned are present.

And a receiver will not be granted in any case unless an actual partnership inter se existed between the parties. The burden of proving such partnership is upon the plaintiff, where its existence is denied by the defendant. And if the agreement states that they are not partners though a firm name is used, a receiver will not be appointed.

A general test for determining the existence of a partnership is, whether or not there is a right to participate in the profits. If the plaintiff establishes such a right,

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(1) Henn v. Walsh, 2 Edw. Ch. 129.

the receiver will usually be granted. But if the plaintiff's interest is comparatively small ; or if the defendant gives ample security to insure payment to the plaintiff of such sum as may be found to be due to him at the final settlement; or if the appointment of a receiver would greatly impair the business,,no receiver will be appointed in these cases.

"As it is not the province of the court to create a co-partnership, so it is equally foreign from its functions to conduct its business."[1] The function of the court is only to wind up the business of the firm when the partners cannot properly do so themselves. Yet though this principle is true in most cases, the court may sometimes when actually necessary direct or carry on the business through its receiver or some one appointed by him. The court will never presume to carry on or have the continued management of any partnership business, even through its receiver.

But if it is necessary to preserve the "good will" of the business the loss of which would cause great injury to a purchaser, the court will, through its receiver, manage the business pending legal proceedings for dissolution.[2] When dissolution of a partnership would result disastrously to the interests of the parties, or where the defendant partner strenuously objects to the appointment of a receiver, the courts are extremely reluctant to act and usually will not act at all, unless the case clearly falls within the principles

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(1) Allen v.Hawley,6 Fla.164.
(2) Jackson v. DeForest, 14 How. Pr. 81.

laid down by the authorities.

In addition to the four general classes above mentioned as sufficient grounds for the appointment of a receiver, is the fact of an irreconcilable disagreement between the partners which will cause great injury to their interests. In the consideration of the conduct of one partner as to whether or not it is such as will entitle the other to dissolution, the duties and obligations implied in every contract of partnership, as well as the specific terms of the particular partnership must be taken into account and weighed. And where the conduct of the defendant is entirely inconsistent with that of a partner, and such that the plaintiff should be entitled to dissolution, a receiver will usually be appointed.

Unless the court is quite positive that dissolution will soon occur it will not interfere, as it is unusual for it to assume the responsibility of continuing or managing the business. Ocassionally a receiver may be appointed over a partnership even though dissolution is not sought nor justifiable, as where the parties have deviated greatly from their agreement as to how the business should be conducted.[1]

While a receiver may be granted as a part of a final decree, he is usually appointed upon an interlocutory application on filing a bill for a dissolution and an accounting.

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(1) Const.v.Harris, Turn., & R., 496.

RECEIVERS OF RAILWAYS.

The jurisdiction of equity in appointing receivers of railways has been in recent years greatly enlarged and extended by various statutes, which are based upon and governed by substantially the same principles as those which govern the jurisdiction of the court in the appointment of receivers in foreclosure proceedings against natural persons, or in behalf of judgment creditors, or in cases of the dissolution of a partnership. But the courts are much more reluctant to exercise this power over railways, than over the other cases just mentioned.

The reason for such reluctance on the part of the court seems to be on account of the quasi public nature of a railway, also because of the peculiar nature of its franchises and property and the great importance of a railroad corporation.

Whenever any of the ordinary remedies of the law side of the court are available to the railway creditor for the enforcement of his claim, the court will refuse to appoint a receiver, if the company is well managed, receiving large earnings and the creditor's judgment is comparatively small, unless it is clear to the court that justice can be done in no other way, and that a receiver is an absolute necessity. A prayer for the appointment of a receiver pendente lite over a railway can only be made incidentally by a party who

is plaintiff to an existing action. The receiver is here appointed for the purpose of preserving and protecting the property for the benefit of all those interested, until such time as the court can determine who is properly entitled to a judgment.

But there is one notable instance, and seems to be only one, that of the well-known "Wabash Cases",[1] where receivers were appointed over this railway, upon its own application. This corporation was a consolidation of a number of existing railway companies that were created by several states. The company applied to the court for the appointment of receivers, alleging insolvency and declaring that if its property was attached by its numerous creditors, or broken into fragments by being placed into the hands of various receivers, irreparable injury would result to all who were interested and the court granted the receiver asked for.

This seems to have been a very unusual and unprecedented proceeding throughout, and it is to be hoped that it will not become a precedent for other cases. An individual when he finds insolvency threatening him, is not allowed to fly to a court of equity and ask the court to protect him and keep

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(1) Wabash,St.L. & P.Ry.Co.v.Cent.Trust Co.22Fed.Rep.272.
Ibid, 23 Fed.Rep.513.
Ibid, 23 Fed. Rep. 863.
Ibid, 29 Fed. Rep. 181.
Ibid, 29 Fed.Rep.618.
Little Warrior Coal Co. v. Hooper,17 So. 118.

off his honest creditors. It would not be common justice for the court to do so. And a railroad should not be allowed to ask the court for such protection, any more than an individual is allowed to do so. It would at once open a wide door to fraud and gross injustice to creditors.

Receivers will, however, be appointed on a bill by a share holder to set aside an unauthorized lease. Also to protect a vendor's lien in case of the insolvency of the company ; or where several railroad corporations have had an easement of the same tunnel at the same time, and a conflict arises as to the easement between any two or more of the companies, if the rights of the parties cannot be protected in any other way, a receiver will be appointed to care for them. And many other instances out of the ordinary course might be mentioned where receivers will be appointed.

Sometimes two receivers have been appointed over the same railway concurrently, but this is deemed to be a bad practice, a single receiver being preferable on account of harmonious action and economy.

Unlike the appointment of a receiver over a partnership, the appointment of a receiver over a railway does <u>not</u> operate as a dissolution of the railroad corporation. "Notwithstanding the appointment of a receiver" says Mr. Justice Scott,[1] "the corporation is clothed with its franchises and such corporation still exists. The effect of the appointment of the

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(1) Ohio & Miss.R.R.Co. v.Russell,115 Ill.52.

receiver is simply to give him the temporary management of the railroad under the direction of the court,instead of the manager appointed by the directors of the corporation. It is that and nothing more. As the corporation still exists it may exercise as before, its franchises, so that it does not interfere with the rightful management of the road by the receiver, so far as his duties are defined by the court appointing him. No doubt it may do many corporate acts, and certainly it can do all things necessary to preserve its legal existence notwithstanding the appointment of the receiver to whom the temporary management of the road is given--otherwise the appointment of the receiver would be tantamount to a dissolution of the corporation."

Receivers are appointed over railway corporations for the protection of bond holders and mortgagees, whose securities are a lien upon the road, when the corporation has failed to pay the principal or interest thus secured. This is the most frequent ground for the appointment of receivers over railways. In actions for the foreclosure of railroad mortgages where a receiver is applied for, the courts are governed by the usual principles which govern them in appointing receivers over partnerships, for judgment creditors, or in foreclosure proceedings against natural persons.

Here, as in those cases, proof of the inadequacy of security and insolvency of the mortgagor is sufficient ground for the appointment of a receiver.

The courts do not appoint receivers, as a matter of course. The power of appointing rests in the sound judicial discretion of the court and depends on the rights, and facts of the case as they are made to appear before the court.[1] Where the court thinks the appointment of a receiver is the proper measure, it will not hesitate to appoint one, even though the proceedings of the corporation issuing the bonds and mortgages is impeached by negative testimony, such as an affidavit of the secretary setting forth his inability to find a record of the authority for issuing the bonds and mortgage.[1] At the preliminary hearing the court refuses to pass upon the validity of the bonds. But if the court is of the opinion that by the appointment of a receiver, all parties would be subject to greater injury than by allowing the road to be operated by the company itself during the foreclosure proceedings, then no receiver will be appointed.

The order of appointment given by the court prescribes all the functions and duties of the receiver appointed therein. These duties and functions may be either enlarged or diminished by the further and future orders of the court. The receiver must comply with these directions, and acts outside of them at his peril.

The main duties of a railway receiver pendente lite, are the operation and management of the road, the payment of

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(1) Keep v.Mich.& Lake Shore R.R.Co.,U.S.Circuit Ct. W. Dist.Mich. 6 Chicago Legal News, 101.

current expenses and the application of the residue of the earnings to the extinguishment of the debt. Inasmuch as the primary object in appointing a receiver is for the purpose of having him take charge of, hold and control the property in a manner most beneficial to the mortgagees, bond holders and creditors generally, it is very seldom that the court will authorize the receiver to extend the line of the road except where such action is necessary to successfully maintain and operate the road, or in order to prevent the forfeiture of valuable land grants or franchises.[1]

When such extension or enlargement of operation is permitted by the court, the receiver will also be authorized to issue certificates to meet the expenses necessarily incurred, and such certificates will be a first lien upon the road, even ahead of a first mortgage. This feature of railway receivership is a most exceptional one, and cannot be said to be found developed to such an extent if at all, in any other class of receivership.

In order to be binding all contracts, such as those just mentioned, made by a receiver, must be sanctioned by the court. If this is not done all persons contracting with the receiver do so at the risk of such contracts being disapproved by the court.[2] But since a receiver pendente lite of a railway, has very different and far more responsible duties thrust upon him, than has a passive receiver, the former

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(1) Kennedy v.St.Paul & Pacific R.R.,2 Dillion 448.
(2) Lehigh C. & N. Co. v.Central R.R., 35 N.J. Eq. 426.

is allowed a wider discretion,in making expenditures necessary to operate the road, and all outlays made in good faith by him in the ordinary course of business, promoting the interests of the corporation will be sustained and authorized by the court. Some expenditures of this kind which the court will authorize, are the keeping of the road, of its buildings and rolling stock in repair ; also charges for drayage and wharfage ; for office room and general advertising.

Some of the most perplexing questions arising in railway receiverships are those concerning the indebtedness incurred in managing and operating the railway and further those concerning the extent to which certain classes of pre-existing debts may be preferred in payment, out of either the income of the receivership or the proceeds of foreclosure, as against the mortgage bond-holders and other creditors.

While it may not be wholly in accord with sound legal reasoning, yet the fact remains that through a court of equity, mere contract debts of a railway company unsecured by any lien and incurred before the appointment of the receiver, may be given priority over antecedent mortgages. But debts allowed this peculiar privilege are usually only those made from actual necessity in running the road, such as those incurred for labor, material-men, supplies and equipment.

Such practice has been said to impair the obligation of the mortgage contract, but it is so strongly upheld by authority that it can no longer be questioned. And it may be

defended upon the ground, that the mortgagee impliedly contracts to allowing the payment of all necessary and actual running expenses before the payment of his own claim. And this because of the extra personal benefit derived by keeping the road in operation. This is sometimes known as the doctrine of"diversion of the income". It is only doing in effect through the receiver what the corporation should have done, and is therefore justifiable. For it is surely no more than just that the corporation should pay its necessary running expenses before declaring any dividends whatever.

The leading case on this question is that of Fosdick v. Schall,[1] In that case Waite, C.J. says : "the income out of which the mortgagee is to be paid, is the net income obtained by deducting from the gross earnings, what is required for necessary operating expenses, proper equipment and useful improvements. Every railroad mortgagee in accepting his security, impliedly agrees that the current debts made in the ordinary course of business, shall be paid from the current receipts before he has any claim upon the income".

But here the question arises which is this, within what time before the appointment of the receiver must such current debts have been incurred, in order that the receiver pendente lite, may be authorized to pay them before the claims of the bond-holder and mortgagee are paid ? It may be said in a general way, that these debts must have been incurred within

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(1)Fosdick v.Schall, 99 U.S. 235.

the length of time, prior to the appointment of the receiver, equal to the usual time of credit given for the particular articles. For instance, in a case of the sale of coal to the railroad company, for its consumption, with three months' credit. Here the receiver may pay for such coal if it was purchased during the three months immediately preceding his appointment. Different lengths of credit being allowed for different articles would necessarily vary this rule. It is more desirable, however, to have it uniform, therefore some jurisdictions[1] have claimed that no debts incurred prior to six months before the appointment of the receiver shall be paid by him. This has been termed the "six months' rule", but it has not been generally adopted and claims have in some instances been allowed, though they were incurred within a much longer period than six months before the appointment of the receiver.

It may be questioned whether under this rule, the unpaid salary of the president of the road shall be paid by the receiver, before paying the claim of the bond-holders and mortgagee. There is some difference of opinion on this matter, but the solution of the question would seem to depend on whether or not the president is deemed to be an actual necessity in running the road.

Concerning the indebtedness incurred by the receiver pendente lite, in operating the road, there seems to be little

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(1) Blair v.St.L.,H.& K.R.R.Co.,22 Fed.Rep.271.

or no question, as to the power of the court to authorize the reeeiver to incur all actual and necessary running expenses. The bond-holders should agree to such expenditures ; and they should be reasonable and of such a character as to prove beneficial to the corporation. But the receiver must not pay these expenses out of the corpus of the property unless he is specially authorized so to do by the court.

Receivers pendente lite may be held liable in their official capacity for personal injuries received during their management, in such cases as those in which the corporation would have been held liable if it had been in control of the road. But leave of the court must first be obtained in order to recover for personal injury caused by negligent management of the road. All such claims should be filed with the receiver. By virtue of a United States statute a receiver may be sued in the United States Court appointing him, without the consent of the court. Receivers are generally held to a common carrier liability.

In New York a rather peculiar state of affairs exists as to ability to sue receivers of railways. The courts of this state have held that where the receiver has used reasonable care in the selection of his employees, the doctrine of respondeat superior does not apply, and therefore the receiver is not liable for personal injuries inflicted.[1] The same court has also held, that while the road was in the hands of

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(1) Cardot v.Barney, 63 N.Y.,281.

a receiver, the company was not liable for such injury,[1] and so one is puzzled to know whether or not he can recover for personal injuries, while the road is in the hands of the receiver. The only method would seem to be to file claims against both the receiver and the road.

The court has in some instances compelled the road to assume the liability for injuries inflicted during the management of the receiver, as a condition of turning the road over to the company again. But this seems to be an exceedingly harsh rule, and one which cannot be justly enforced.

The New York doctrine above laid down is not the generally accepted doctrine, however, and ordinarily the railroad corporation is not to be held liable for injuries caused by the negligence of the receiver's employees.[2] But statutes in the various states may cause the liability for personal injury to be placed either upon the receiver or the corporation.

In the English and American courts receivers were originally appointed for the purpose of closing up the business, or of holding the property until the rights of contesting parties could be determined finally by the court. Receivers were not supposed to carry on the business and improve it, nor were they supposed to contract any debts in behalf of the property which they held, until judgment was given in favor of either one party or the other.

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(1) Metz v.B.,C.& P.R.R.Co.,58 N.Y. 61.
(2) Ohio & Miss.Ry.Co. v. Davis, 23 Ind.553.

The receiver of a farm in foreclosure proceedings was not allowed to purchase seed, or work the farm thereby causing expenditures to be made, until judgment was rendered.

Receivers of partnership were followed by dissolution of the firm, and no expenditures were allowed unless there was a contemplated sale of the business and some expenditures were absolutely necessary to preserve the business and its good will for the benefit of the purchaser. Here it was necessary to carry on the business to preserve its value, and in order to carry it on debts were necessarily incurred. But such action on the part of the receiver was always more or less restricted. And in other cases as creditor's suits no receiver would be appointed upon the application of a creditor until his claim had been reduced to the form of a judgment or decree which gave him a lien upon the debtor's property.

Now consider the case of a receivership in a railway mortgage foreclosure. A railroad mortgage covers all the profits and franchises,which is an exceptional feature not found in the case of other mortgages. Here the road is put up for sale, but purchasers for a railroad are not always to be readily found, and since the court will not allow a peremptory sale, a receiver is appointed to manage it for and in compliance with the orders of the court. Theoretically the receiver should act only for a definite period, but practically he acts indefinitely.

In foreclosure proceedings of a railroad mortgage,re-

ceivers have come to be appointed as a matter of course. This is so because of the quasi public nature of the railroad, and also for the obvious reasons that if the road is not operated continuously, the property will greatly deteriorate in value. And furthermore railroads usually have government contracts for carrying the mail which must be done regularly and without interruption. Therefore on account of these and other similar reasons, a receiver pendente lité of a railway must necessarily be given a greater freedom of action and allowed to do certain things which other receivers would not be permitted to do.

The exceptional features of a railroad receivership seem to be :--

First, a tendency of the railroad to ask for a receiver. But this has only been granted in one case, which will probably be the last one.

Second, that the court takes charge of the property, operates and continues the business through its receiver. But this cannot be strictly called an exceptional feature, for a court will under certain circumstances allow a receiver to continue a partnership or other business.

Third, the appointment of a receiver of a railway does not work a dissolution of that corporation as it does in the case of a partnership. This may be said to be a really exceptional feature of railway receiverships.

Fourth, the issuing of receiver's certificates to em-

ployees and material-men, for labor, equipment and supplies, which certificates are a first lien upon the property even ahead of a first mortgage.

Compare with this the rights of general creditors who have acquired no lien upon the property, in creditor's suits. And in railroad receiverships such certificates may be issued for antecedent debts, under the so-called "six month's rule". It has been said that this is allowed in order to prevent strikes and keep the men at work so that the road may continue to operate, but this seems to be carrying the doctrine a trifle too far. This last feature of paying antecedent debts ahead of the claims of the bond-holder and mortgagee may be said to be a really exceptional feature of a railway receivership at present, but there is a tendency to extend the same to the receivers of water and gas companies, on account of their beneficial and public nature, so that it may not be long before this feature must cease to be called an exceptional one in railroad receiverships.

But notwithstanding all these facts, it is obvious that railroad receivers are less restricted, and have a much broader and more extended field of action at the present time, than is allowed to any other class of receivers.

Henry L. Green