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# The Duties of the Trustee of a Mortgage Given to Secure Bondholders

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## THE DUTIES OF THE TRUSTEE OF A MORTGAGE GIVEN TO SECURE BONDHOLDERS

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The expressions of our Supreme Court with reference to the status of a banking institution, to which a borrower executes a mortgage to be held in trust for the holders of the bonds to secure which the mortgage is given, do not appear to be entirely consistent. Some expressions suggest that the liability of the trustee rests only in contract, while others recognize that the general rules of law applicable to trustees may be invoked to impose liability on the trustee under such an indenture.

A long line of cases recognizes the effectiveness of exculpatory clauses contained in the indenture which expressly negative the obligation of the trustee to do this, that, or the other thing, which a mortgagee would certainly do if he were making a loan of his own money, for example:

> "In the case of Bell v. Title Trust & Guarantee Co., 292, Pa., 228, it was held that where under the express provisions of the trust the trustee was relieved of seeing that the mortgage was recorded, the trustee could not be held liable because the mortgage was not recorded, and the same conclusion was reached in the case of Benton v.Safe Deposit Bank of Pottsville, Pa., 255 N. Y. 260, in construing a Pennsylvania contract and applying Pennsylvania law; and in Newhall et al v. Norristown Trust Co., 280 Pa., 195, a provision exempting the trustee from liability to see to the disposition of the proceeds of the sale of bonds was upheld; and in Bell et al. v. Scranton Trust Co., 261 Pa. 28, where the property which was covered by the mortgage held in trust was destroyed by fire without insurance it was held that the trustee was not liable, where he was relieved from the duty of seeing that the premises were insured by the specific

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> provisions of the trust agreement; and in Byers v. The Union Trust Co., 175 Pa. 319, it was held that the trustee was not responsible where the mortgage which was the subject of the trust was not a first lien on the premises where the instrument specifically exempted it from seeing that it was a first lien."[1]

The lower court in the *Gouley* case, after noting the decisions mentioned, observed:

> "It is apparent that in all the above cases a *different conclusion would have been reached* if it was not for the specific provisions in the trust agreement exempting the trustee from liability for failure to perform the acts which form the basis of several actions, and the exemption of liability in each case was grounded specifically on the express provisions of the trust agreement which exempted the trustee from liability.
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> "It is unfortunate that under the principles of law by which this court is bound no relief can be given to plaintiff. Undoubtedly as a result of the investigation of the Sabbath Committee some legislation may be passed that will make it compulsory for trustees to assume more active duties. We are bound by the provisions of the contract and must hold that under its express provisions the trustee is relieved from taking notice of any default, and as a corollary thereto we think it is relieved from notifying bondholders of default."

When this case reached the Supreme Court, Justice Barnes made the statement:[2]

> "The nature and extent of the duties of a corporate trustee are primarily to be ascertained from the trust instrument. Such duties are those assumed under the terms and conditions of the contract itself, rather than inherent in the general law governing trust relationships."

If this statement is limited in its application to sustain the validity of exculpatory clauses, so long as they are not forbidden by legislation or contrary to public policy, it would appear to be a correct statement of the law, but it appears to say that no duties are imposed on the trustee except those specified in the indenture and that the trustee, as such, is not subject to the general rules applicable to other trustees and, so interpreted, the statement is out of line with a number of other cases.

In *Moyer v. Norristown-Penn Trust Co.*, 296 Pa. 26, Justice Walling said:[3]

> "Furthermore, the defendant was trustee for all the bondholders, and they, including plaintiff, were beneficiaries: 3 Fletcher, Cyclopedia Corporations, section 1337, p. 2312. Trustees for bondholders are governed by the general rules that govern trustees in the ordinary

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[1]Gouley v. Land Title Bank & Trust Co., 27 D. & C. 663, 664, 665.
[2]329 Pa. 465, 468.
[3]All italicts herein are ours.

> performance of the duties of a trust: 2 Perry on Trusts and Trustees (6th ed.), section 760. In no event could a trustee avail himself of the negligence of the cestui que trust without proof that he had sustained loss thereby, of which there was no evidence in the instant case. Mere delay by the beneficiary in requesting payment from the trustee will not relieve the latter: Kittel's Estate, 156 Pa. 445; Bruner v. Finley, 187 Pa. 389. The *duty of vigilance is upon the trustee* rather than upon the cestui que trust."

In *Drueding v. Tradesmens B. & T. Co.,* 319 Pa. 144, 152, Justice Linn said:

> "The trustee was required to act in good faith and, as required by the rules stated, to exercise that degree of *care, skill and intelligence* required in the circumstances."

Since the decision in the *Gouley* case, Justice Barnes, who wrote the opinion in the *Gouley* case, has written the opinion in the *Commonwealth Trust Co. Case,* 331 Pa. 569, in which he said:

> "This case presents no novel question of law. The *loyalty which a trustee owes* to his beneficiaries is the basic factor of trust relationship. Once the trust is accepted it must be administered solely in the interest of the beneficiaries. The application of this principle is determinative of all issues presented by these appeals: Quell v. Boyajian, 90 Pa. Superior Ct. 386; Restatement, Trusts, section 170; Bogert, Trusts and Trustees, sections 484, 543. This rule is stated in Story's Equity Jurisprudence (14th ed.), section 446, in the following language; 'In short it may be laid down as a general rule that a trustee is bound not to do anything which can place him in a position inconsistent with the interests of the trust, or which have a tendency to interfere with his duty in discharging it.' See also Raybold v. Raybold, 20 Pa. 308; Restatement, Trusts, section 203. It is a corollary of this rule that a *trustee may not profit at the expense of the beneficiaries nor assert any adverse interest in the trust property*: Krauczunas v. Hoban, 221 Pa. 213, 224: Harris v. Silvis, 86 Pa. Superior Ct. 222."

Again in *Klein v. Dunn,* 337 Pa. 480, 485, the same Justice made this statement:

> "The Reading Bank violated its *duties as a fiduciary to inform the cestuis fully of all matters affecting their interest* and accordingly it must be held to have assumed the risk that the particular installments of interest advanced might never be repaid."[4]

It was accordingly held that the bondholders were entitled to be paid in full before the bank could recover any of the interest which it had advanced. These later decisions appear to make it clear that, in so far as the indenture is silent as to the duties of the trustee, these are to be gathered from the rules governing trustees of all types. Duties which a trustee could be supposed to have assumed

[4]To like effect is Media-69th Street Trust Company's Case, 344 Pa. 223, 234.

may be expressly negatived by the provisions of the indenture, so long as such provisions do not purport to exempt the trustee from liability for acts not done in good faith or involving gross negligence.

In addition to the cases giving effect to exculpatory clauses above mentioned, the case of *Kelly v. Girard Trust Co.*, 328 Pa. 353 may be noted.

It would seem to be contrary to public policy to permit a reputable financial institution to have its name used as a trustee for bondholders and so to give confidence to the purchasers of the bonds and at the same time to permit it to escape liability, though it failed to do a variety of things all of which must be done by somebody, if the bondholders are not to lose their investments. Accordingly Congress passed the Trust Indenture Act of 1939,[6] c, 411, 15 USCA section 77 aaa et seq. This act invalidates exculpatory clauses in such instruments but the act only applies when the bond issue exceeds a million dollars. Needless to say, if the holders of bonds issued in a smaller aggregate are to be protected, such protection will have to come from our own legislature or from a changed attitude on the part of our courts.

From the passages quoted above it is apparent that our Supreme Court has recognized the following duties as imposed by the general law of trusts upon trustees for the bondholders, in the absence of provisions in the indenture negativing such duties, to wit: vigilance, loyalty, to refrain from profiting at the expense of the beneficiaries, to refrain from asserting any interest in the trust property adverse to the beneficiaries, to inform the beneficiaries fully of all matters affecting their interests which may come to its notice, and to exercise that degree of care, skill and intelligence required in the circumstances.

In the *Gouley* case there had been defaults of which no notice was given to the bondholders, but the court held that the provisions of the mortgage relieved the trustee of the duty to give notice of these defaults. The bonds were guaranteed by the The Philadelphia Company and it was made the agent of the bondholders under the terms of the guarantee. It appeared that the same persons were officers of both the trustee company and the guarantor company and they had numerous directors in common. Furthermore, the trustee had an interest in avoiding trouble for the guarantor company, because the trustee bank had made large advancements to it. The court held that this situation was sufficient to awaken suspicion, but that the situation alone was not enough to constitute proof of bad faith in withholding notice of default from the holders of the bonds. The court recognizes that there may be limitations in the trust instrument of the duties of a trustee which are opposed to public policy, but it could not see that this rule had been violated by the provisions of the mortgage in question.

As the law now stands, purchasers of bonds secured by a mortgage to a trustee are put on notice of all limitations upon the obligations of the trustee

[6]See *Indenture Securities and The Barkley Bill*, 48 YALE L. J. 533.

contained in the recorded mortgage and investors should realize that the prevailing practice is to negative in this instrument most, if not all, of the normal duties which it might be expected that a trustee would perform.

When a customer comes to a banking institution with cash or securities seeking to create a voluntary trust, the proposed trustee has a perfect right to stipulate the terms on which it is willing to accept the trust and the rate of compensation which is agreed upon should be proportionate to the responsibility assumed.

On the other hand a trustee for bondholders does not make its bargain with them but bargains with the mortgagor, who is expected to pay for the services of the trustee. The mortgagor is interested in securing the services of the trustee as cheaply as possible and the trustee is interested in assuming as few responsibilities as possible. The proposed trustee accordingly specifically eliminates by exculpatory clauses everything that its learned counsel can think of as matters it could be expected to attend to and, as the purchasers of the bonds rarely read the mortgage itself, this does not seriously affect the sale of the bonds. The trustee collects a fee for the use of its name and expects the bondholders to look out for themselves.

As stated by Justice Kephart in *Northampton Trust Co., Trustee v. Northampton Traction Co.,* 270 Pa. 199, 202:

> "A trustee of a corporate mortgage has little actual work to perform; selected in part *to give tone* to the obligation *and encourage the sale of securities,*—as a sort of certificate of the mortgagor's standing,—its duties are to a large extent passive until some default occurs, when they become active."

The above quoted statement that the duties of a trustee for bondholders only becomes active after a default is, of course, only partially true. The subject of the mortgage may be destroyed by fire, in which case the trustee has the problem as to what to do with the proceeds of the insurance, for the mortgage may be silent on the subject. This was the problem facing the trustee in the case of *Bell v. Scranton Trust Co.,* 282 Pa. 562. In this case the trustee only escaped a surcharge because the court held that the bondholders by their conduct had ratified the application of this money by the trustee and that the trustee was protected from a surcharge by conduct on the part of the bondholders which created an estoppel. There was a provision in the mortgages exempting the trustee from all liability except for willful and intentional breaches of the trust but the court declined to express an opinion as to the effect of this exemption when a mortgage fails to authorize the appropriation which the trustee actually makes of the fund.

Furthermore, it is not infrequent to provide for the release of portions of the mortgaged premises by the trustee, upon the payment of all or a stated por-

tion of the selling price of portions of the mortgaged premises which the mortgagor may have an opportunity to sell to advantage. This is a power the exercise of which requires the greatest care or a surcharge will result. In *Commonwealth Trust Co. Case,* 331 Pa. 569, the mortgage was for only $100,000.00 but the surcharge imposed on the trustee by the lower court amounted to $87,050.82, an amount which was later somewhat reduced in *Neely's Appeal,* 339 Pa. 265. Again the trust may consist of securities held by the trustee as collateral for the benefit of the bondholders and the borrower may be authorized to make substitution of collateral, if certain conditions are met. Of course the trustee must be very vigilant in seeing that such conditions are strictly compiled with. Obviously, in any case, there may be active duties to be performed by a trustee for bondholders, notwithstanding the fact that no default has yet occurred.

That exculpatory provisions should be strictly construed is indicated in *In Re: Beaver Trust Company,* 146 Pa. Super. Ct. 545, 22 A. (2d) 111 (1941). It was held that a provision in the trust instrument that the liability of the trustee should be limited to the amount realized did not relieve the trustee of the duty to use care in preserving the subject of the trust by taking proper steps to foreclose a mortgage before it became worthless.

> "We agree with the learned court below that 'the purpose of the agreement was to protect the trustee against any assumption of liability for the full face value of the securities taken over in kind. Having taken the securities it was bound to use common skill, common prudence, and common caution in the administration and collection of the securities, being liable, however, for supine negligence or wilful default'. See Drueding et al. v. Tradesmen's National Bank and Trust Co., 319 Pa. 144, 179 A. 229; and 3 Bogert, Trusts and Trustees, sec. 592.
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> "In Section 174 of the Restatement of the Law of Trusts it is stated: 'The trustee is under a duty to the beneficiary in administering the trust to exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property; and *if the trustee has greater skill than that of a man of ordinary prudence, he is under a duty to exercise such skill as he has.*' See, Also, Kline's Estate, 280 Pa. 41, 45, 46, 124 A. 280."

Some courts are realistic, e. g. in *Marshal & Ilsley Bank v. Guaranty Inv. Co.,* 213 Wis. 415, 250 N. W. 862, it was said:

> "It would be intolerable to limit such a trustee merely to the obligation imposed by the terms of the contract made and drafted by it, and rarely ever seen by the bondholders. It is our conclusion that the trustee under a bond issue does owe to the bondholders certain duties independently of the terms of the trust deed, and that these duties will be imposed regardless of any exculpatory provisions in the trust deed. Such a trustee has an obligation to exercise good faith as well as ordinary vigilance and intelligence in protecting the interests of the bondholders."

The distribution of money which comes into the hands of a trustee for bondholders, if made without an order of court directing the distribution as made, is at the peril of the trustee. In *Colonial Trust Company's Appeal,* 241 Pa. 554, 88 A. 798, the mortgage was "for the equal pro rata benefit of the holders of the bonds issued under the mortgage without preference or priority of one bond over another." Instead of making a pro rata distribution, the trustee paid certain bonds in full and gave no notice to the holders of other bonds which were known to be outstanding. It was held that the trustee was bound to ascertain how many bonds were outstanding and that the voluntary distribution made by it exposed the trustee to a surcharge in favor of the holders of the outstanding bonds for the amount of their distributive shares of the sum so misapplied.

Again in *Moyer v. Norristown-Penn Trust Co.,* 296 Pa. 26, it was held to be the trustee's duty to see that money in its hands was paid to the right party and that it was liable for a mistaken payment to the wrong party though made in good faith.

In *Com. v. Susquehanna & Del. R. R. Co.,* 122 Pa. 306, 320, it is said:

> "The trustee takes the title in trust. . . . The bonded debt is a unit so far as his duties and powers are concerned. He must regard the bondholders as a class, and not as individuals. *He cannot permit,* and if so wanting in fidelity to his trust as to be willing, *the courts will not permit, the least discrimination between members of the same creditors class."*

In this case, at page 319, it is said:

> "Until default is made in the payment of the bonds, or the interest falling due upon them, the trustee has no active duties to perform but is simply the repository of the title to the property mortgaged, in trust for the whole creditor class secured thereby. . . . But *when a default occurs, the duties of the trustee become active and important.* He represents all the bondholders, and is under obligation to protect them so far as the property in his hands in trust for them will enable him to do so."

Again in *Armstrong Co. Trust Co. v. Freeport Water Works Co.,* 291 Pa. 188, 139 A. 856, at page 193, Justice Walling said:

> "While so far as we know the precise question raised here has not heretofore been passed upon, yet the authorities are uniform that, *when the mortgagor makes default, it becomes the trustee's duty to take steps for the protection of the bondholders, without request from them.* Assuming, therefore, that the pledgee of Guffey's bonds and not he was the proper party to give the notice in question, it does not affect the validity of the foreclosure proceeding; for when the mortgagor defaults, the duties of the trustee become active, and he may properly take steps to foreclose, with or without notice from the bondholders. See Com. v. Susq. & Del. R. R. Co., 122 Pa. 306."

In *McDougall v. Huntingdon and Broad Top R. & C. Co.*, 294 Pa. 108, 126, it is said:

> "If legal action is necessary to protect the bondholders, it is the duty of the trustee to take such action. If the trustee refuses to perform his duty, the court will compel him to act or to resign his trust: See Bradley v. Chester Val. R. R. Co., 36 Pa. 141, 154. . . . A trustee, in performance of his trust, cannot permit the minority to be unfairly dealt with in the payment of interest or principal. He must take steps to protect their rights or suffer the consequences of removal or payment out of his own pocket. The trustee's duty is not a negative one. In accepting the position of trust to act to a given end, certain circumstances may arise where action on his part becomes necessary and can be enforced."

It is also said:

> "As to judgments recovered on the bonds covered by the mortgage, the bondholder gains no higher status in relation to the property because his claim is reduced to judgment. It is a bond, and nothing more. Issuing an execution on the judgment did not increase its value; it is still a claim on a bond and has the same status as another bond on which no suit is brought."

In *Smith v. Girard Trust Co.*, 320 Pa. 412, 413, Chief Justice Kephart said:

> "The terms of the mortgage did not prohibit the trustee from promptly foreclosing upon default for the benefit of all bondholders and, unless such prohibition did appear, it was its duty to do so. A trustee must take such action as he deems necessary for the protection of the bondholders unless the instrument explicitly restricts his power: McDougal v. Hunt. & Br. T. R. Co., 294 Pa. 108, 126. The trust company, representing many beneficiaries, was not compelled to seek authority from all before proceeding to foreclosure. A single dissent could not block proceedings which were for the benefit of all bondholders, and foreclosure of part of the mortgage could not be had."

The reason the obligation is imposed upon the trustee to begin foreclosure proceedings upon the mortgagor's default is because of the rule established in the *Susquehanna & Delaware Railroad Co.* case, *supra,* that while a bondholder may sue and recover judgment, any execution on such judgment must be levied on property other than that which has been conveyed to a trustee by mortgage or deed of trust duly executed and recorded.

Of course, what is realized by foreclosure proceedings belongs to the bondholders as a class and must be distributed among the bondholders pro rata.

In *Frey v. Union Traction Co. of Pittsburgh,* 320 Pa. 196, 200, the court said:

> "Neither bond nor mortgage prohibits suit by a bondholder on his bond. But, as the mortgage was made for the protection of all the bondholders, ratably, the plaintiff, by the terms of the contract, is

> not entitled to execution against any of the property mortgaged or pledged so long as other bonds secured by the same property are unpaid and entitled to the benefit of the security. Execution, if any, must be controlled accordingly: Com. v. Susquehanna & D. R. R. Co., 122 Pa. 306, 15 A. 448; Western Pa. Hospital v. Mercantile Library Hall Co., 189 Pa. 269, 42 A. 183."

A trustee for bondholders should always be free from the embarrassment of being compelled to deal with itself in a dual capacity. This principle makes it improper for the same institution to become the trustee of several mortgages on the same property. In the case of *Northampton Trust Co. v. Northampton Traction Co.*, 270 Pa. 199, the trust company was the trustee not only of the first mortgage but also of two junior mortgages. When it began foreclosure proceedings on the first mortgage, the holder of bonds secured by one of the junior mortgages sought to restrain a sale. Justice Kephart said:

> "Public policy requires, where controversies are brought into court, that each party should be represented by someone whose single object it is to secure all to which such party is entitled, unhampered by personal relations to an adverse party, who is bound in conscience to be a loyal and vigorous champion, without any obligation to a conflicting creditor or party; it is because of this anomalous situation between the several independent sets of creditors that equity, always jealous of her impartiality, should have acted in this case. . . . The power to do harm was there and might be exercised, and, to prevent the possibility of such exercise, the trustee should have resigned and permitted the court below to appoint successor trustees for the two junior mortgages."

The most instructive case on this point is *Commonwealth Trust Company Case,* 331 Pa. 569. In this case, after becoming trustee for the first mortgage bondholders, the trust company made loans to the mortgagor and took a second mortgage as security. Later it was called upon to make further advances and took a third mortgage from the debtor. Then it took a deed for the property mortgaged and agreed to manage the property for the purpose of discharging all indebtedness and to return to the debtor any excess realized.

Commenting on this situation, Justice Barnes said:

> "Here it is apparent that the Trustee's difficulties are due to the fact that it attempted to act in several antagonistic capacities at one time. It was the trustee for the holders of the first mortgage bonds. It marketed the entire issue of bonds and sold a large portion of them to estates of which it was trustee. It took junior mortgages upon the same property. It then took title to the property and attempted to hold and manage it for the benefit of the original owner, the mortgage debtor. It would not be surprising if the Trustee, torn between such divergent interests, failed at times to discern the direction in which lay its duty of loyalty. There is afforded here a striking example of the truth of the ancient maxim, still deeply rooted in

> the law, that no man can serve two masters. . . . It could not at the time be trustee of the same property under two different trusts for different beneficiaries, whose interests were conflicting. Having undertaken originally to act as trustee under the first mortgage, its primary obligation at all times thereafter was to the bondholders."

One of the embarrassing features in the case of *Gouley v. Land Title Bank and Trust Co,*. 329 Pa. 465, was the fact that the trustee bank was a creditor in a large amount of the mortgagor and, of course, this gave it a motive to delay performing its duty to foreclose the mortgage promptly after default. The bank escaped liability in this situation only because of the exculpatory provisions contained in the mortgage.

It not infrequently occurs that an individual gives a blanket mortgage to a financial institution as trustee for the holders of bonds secured thereby and then names the same institution either as executor of his will or as trustee thereunder. Obviously, the executor or trustee must either resign as trustee for the bondholders or it must renounce the office created by the will, for it cannot represent both debtor and creditor in the same transaction.

The penalty for self serving is strikingly illustrated in *Austin's Estate,* 44 D. & C. 249, at page 253. The National Bank of Fayette County was trustee of a mortgage on property on which the commercial department held a judgment junior to the lien of the mortgage. At the sheriff's sale on the bank's judgment, the bank bought in the property subject to the lien of the mortgage, thus indicating that it felt that there was some equity beyond the amount of the mortgage.

Commenting on this situation, the court said:

> "When the bank sold the property at sheriff's sale, it was its duty to decide whether there was any equity in it for the liquidation of its judgment lien. The bank did decide that there was an equity. It proceeded on its judgment and not on the trust department mortgage. It paid the costs and taxes and purchased the property for the commercial department. Thereupon, it became the duty of the bank to pay the underlying mortgage. *A trustee cannot hold in one hand a mortgage for the benefit of his trust, and in the other hand the legal title to the mortgage property for the benefit of himself. This is definitely self-dealing.* He may desire to retain the property for an advantageous sale for his personal benefit, yet it may be his duty to the trust to sell it. Certainly, when he does retain it under such circumstances and a loss to the trust occurs, he should be chargeable with it."

Granting that it be the duty of a trustee for bondholders to proceed with the foreclosure of the mortgage upon default, the question arises as to the further duties of the trustee when the property is offered for sale by the sheriff. This subject was discussed at length in two related cases, *Nay Aug Lumber Co. v. Scranton Trust Co.,* 240 Pa. 500 and *Watson v. Scranton Trust Co.,* 240 Pa. 507.

Of course, if the mortgage contains express provisions defining the duty of the trustee at this stage, such provisions will control, but the cases mentioned decide that the trustee has an implied power to bid an amount equal to the principal and interest due on the mortgage and that it is the trustee's duty to attend the sale and protect the rights of the bondholders, and if necessary, bid in the property. "It is the duty of a mortgage trustee to protect the security he has taken for the bondholders to the utmost of his ability."

The trustee in the cases mentioned bought in the property for $26,000.00 and being the mortgagee, it gave its receipt for the amount of the bid, less costs, etc. The court also held that, having properly purchased the property, it had the right to make sale of it and that it was entirely unnecessary to ask the court for authority to sell, as the land still continued personalty, when acquired under such circumstances.

It was also said:

> "If a trustee buys the trust property even at a public sale, which is brought about, or in any way controlled by himself, he will be presumed to buy and hold for the benefit of the trust."[6]

Watson was the holder of a bond secured by the mortgage of which the Scranton Trust Co. was the trustee. He filed a petition under the Act of June 14th, 1936, P. L. 628, 633, to secure an accounting by the trustee. The trustee, though it had refused to permit the property to be sold in the foreclosure proceedings to an outside bidder for $25,500.00, had resold the property to an attorney representing a faction of the bondholders for $8,095.00. It was shown that the buildings and fences on the property had not been kept up while the trustee had title and the real value of the property at the date it was sold by the trustee does not appear in the record.

The Supreme Court held that, when the best price offered at the trustee's sale was only $8,095.00, it was the duty of the trustee to adjourn the sale and that it was gross negligence not to do so, for which the trustee was liable. The difference between the two figures was said to be

> "So great as to justify an inference of supine negligence in not adjourning the sale and attempting to realize more for the property either at private sale or by another public sale. Or an effort to divide the property among the bondholders might have been made."

It was held that the trustee would have to account for the fair and reasonable value of the property as of the date when it was resold by the trustee.

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[6]See also Harris v. Silvis, 86 Pa. Super. Ct. 222; Kenworthy v. Equitable Trust Co., 218 Pa. 286, 291; Church v. Winton, 196 Pa. 107, Michoud v. Girod, 4 Howard (U. S.) 503.

In *Continental Bank & Trust Co. of New York v. Oak Lane Manor Corp.*, 30 D. & C. 454, 455, 456, it is said:

> "As to the fixing of an upset price, the chancellor feels that for the best interest and protection of all parties interested in this property an upset price should be fixed. In the case of Northampton Trust Co., Trustee, v. Northampton Traction Co. et al., 270 Pa. 199, there seems to be some authority that a chancellor has not only the right but perhaps the duty in certain cases to fix an upset price. The ideal situation, perhaps, would be to have the trustee buy the property and form a corporation, issuing stock to each of the bondholders in amounts sufficient to give each stockholder the same proportionate interest in the corporation that his bonds bear to the total bond issue. It may be, however, that a purchaser will appear at the sale and bid a price that will make it appear to be for the best interest of the bondholders to accept such offer. If an upset price is fixed, the trustee will be protected against any claims for negligence in failing to perform any duty that may be imposed upon the trustee to bid for all the bondholders at the foreclosure sale: Nay Aug Lumber Co. v. Scranton Trust Co., 240 Pa. 500, 504, 505; Watson v. Scranton Trust Co., 240 Pa. 507.
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> "The upset price for the protection of the trustee may be particularly necessary in the present case because of the fact that the Continental Bank & Trust Company, as trustee under the mortgage, is also, in another fiduciary capacity, acting as depository for a bondholders' protective committee which is said to represent 51 percent in amount of the outstanding bonds. The trust company may, therefore, be acting in two capacities and be unable, as a matter of law, faithfully to discharge its obligations in both. . . . The diverse interest of the trust company is illustrated by the fact that as depository for the protective committee it has a list of the bondholders who have deposited their bonds, yet if we grant the prayer of the intervening defendant directing the trust company as trustees to furnish a list of such depositing bondholders it would cause the trust company, as depository, to violate the confidence of the bondholders' protective committee for which it is acting under the depository agreement. The chancellor feels, however, before any upset price should be fixed, that a hearing must be held to allow the production of testimony by any party interested as to the present value of the mortgaged premises."

The mere fact that the mortgage runs to a trustee does not operate to change in any way the normal remedies available to a *mortgagee,* unless the mortgage itself contains a power of sale. If the mortgage does contain such a power, it is important to remember that a sale by a trustee under a power of sale in a trust mortgage is not a judicial sale, so that this power should only be used when there are no other liens upon the mortgaged property.[7]

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[7]Bruckman Lumber Co. v. Ins. Co., 307 Pa. 561 (1932).

The trustee of course has the same right possessed by any mortgagee to the possession of the mortgaged premises after default.[8]

If the trustee neglects to exercise this right and also neglects to perform its duty to foreclose the mortgage, a court of equity will compel it to take action or resign the trust.

In *Bradley v. The Chester Valley Railroad Co. et al.*, 36 Pa. 141, 155, Justice Woodward said:

> "We nevertheless take jurisdiction of the trusts created in the mortgage, and compel trustees to execute whatever powers have been vested in them for the benefit of creditors, even to a sale of the mortgage premises."

In *Ashhurst et al. v. The Montour Iron Company*, 35 Pa. 30, 42, 43, (1860) it is said:

> "From this analysis of the document, it is apparent, that whilst the relation of trustee and cestui que trust is established and accurately defined between the trustees and the purchasers of the bonds, the relation between the trustees and the Montour Company is that of mortgagor and mortgagee simply. This latter relation is, indeed, attended with some stipulations that are unusual in the ordinary Pennsylvania mortgage, but which are not unknown to the law of mortgages, and which are very necessary where, as in this instance, a marketable security was to be created as the means of borrowing money. This class of instruments, quite unknown to the framers of our old Act of 1705, have become very common in our day. They are tripartite in substance and effect. Besides the two contracting parties, there are the creditors, unascertained, indeed, when the instrument is made, but well known as a party when the remedies come to be discussed. *Between them and their trustees it is nothing but a trust—between the trustees and the mortgagor it is nothing but a mortgage.* And if the creditors be regarded as the substantial plaintiffs on this record, then, as between them and the mortgagor, the instrument can be regarded as nothing else than a mortgage. Acting through their trustees, they have all the remedies they have stipulated for, and all which the law has provided for mortgage-creditors against mortgage-debtors, but they have not, either on their own account, or in behalf of their trustees, the right to come into chancery for a decree of sale. The reason is, that power to decree a sale in equity against the mortgagor has not as yet been given to the courts."

If the trustee receives any money as the result of taking possession of the mortgaged property or as the result of a sale of the same, the remedy available

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[8]See *Collection of Rents by a Mortgagee in Pennsylvania*, by Harold S. Irwin, 45 DICKINSON L. REV. 193 and *The Pennsylvania Mortgagee In Possession*, by Ronald A. Anderson, 11 TEMPLE L. Q. 491 (1937).

to any person interested and it would appear, the only remedy, is by a proceeding at law and not by bill in equity. The nineteenth section of the Act of June 14th, 1836, P. L. 628, 20 P. S. 2833, provides an adequate remedy and for this reason, equity refuses to take jurisdiction. This question was discussed at length by Judge Von Moschzisker in the case of *The Merchants Trust Co. vs. The Real Estate Trust Co. et al.,* 14 D. R. 199 (1905) and by Justice Brown in the same case on appeal reported in 215 Pa. 56. The trustee of a second mortgage was held to be a person interested, as are of course the bondholders or any co-trustee, and so entitled to a citation requiring the trustee to file an account and perform such other duties as attach to the trust. The account is then referred to an auditor who examines the trustee and the court can compel the production of all books and papers "necessary to a just decision", 20 P. S. secs. 2851 and 2852.

In *Reading National Bank and Trust Company's Account,* 22 D. & C. 654, it was held that the Act of June 26th, 1931, P. L. 1384 does not confer upon the Orphans' Court jurisdiction over the account of a trustee for holders of bonds secured by a mortgage.[9]

In *Independent Brewing Co. v. Colonial Trust Co.,* 273 Pa. 12, the mortgagor company sought to use a writ of mandamus to compel the corporate trustee to apply money in the sinking fund to the purchase of bonds held by the debtor in its treasury. It was held that the acceptance of the trust imposed duties to be performed but as they were not statutory or public duties, they could not be enforced by mandamus. Justice Kephart said:

> "The fund in appellee's hands in a trust fund and the dispute is over its management. A court of chancery has exclusive supervision and control of trustees in the management or administration of their trust, and, while this was not directly ruled, it was accepted in Struthers Coal & Coke Co. v. Union Tr. Co., 227 Pa. 29."

In the *Struthers* case a bill in equity was filed for an injunction. The debtor sought to control the trustee in the exercise of its discretion as to the method of retiring bonds under the sinking fund clause in the mortgage, and it was held that a court of equity could assume jurisdiction to settle the dispute, as the trustee had abused its discretion by purchasing at a premium certain bonds, when others could be redeemed at par, though the mortgage failed to specify the class of bonds to be redeemed. Justice Potter said:

> "Common business prudence would suggest that if the way is open to obtain bonds at par, they should be taken, rather than others whose purchase would involve the payment of a premium. Unless there is something in the contract which requires the trustee to do otherwise, clearly it is bound to use the fund to the best advantage, by making it go as far as possible, and this would require it to apply it to the

[9]See as to construction of "trusts inter vivos", Remick on *Jurisdiction of The Orphans' Court,* 47 DICKINSON L. REV. 1, at pages 14 to 16.

> retirement of the serial bonds. There is no reason to discriminate against them. The serial bonds are entitled to the same protection under the mortgage as the long term bonds. We find nothing in the provision for the creation of the sinking fund, which makes it applicable to the retirement of one class of bonds, as against the other."

In the same case, it is also said:

> "The trustee is bound to deal fairly and equitably with all parties to the transaction, and the discretion which it may use is a legal discretion, and not an individual or arbitrary judgment. Any abuse of discretion upon the part of a trustee is clearly a matter for correction in a court of equity."

Section 11 of the Practice Act of 1915, P. L. 483, 12 P. S. 393 and the Act of May 26, 1937, P. L. 895, amending this section, appear to make assumpsit an available remedy to a bondholder who avers that the trustee has received moneys as trustee for which he is bound to account to the one desiring it, whether plaintiff or defendant, and such party is unable to state the amount due him because of a failure of the trustee to account. However, no case has been found in which a bondholder has proceeded under this section and it would seem that a petition under section 19 of the Act of 1836 is still the most satisfactory remedy.