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THE OPEN FUTURE

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(An address delivered at the 1955 Annual Meeting of the United States Chamber of Commerce.)

You have gathered here today as representatives of many hundreds of business communities in every state in the Union. Each one of you has brought to this meeting an intimate knowledge of at least one of the thousands of different kinds of business activities that keep our country prosperous and on the move. Unlike that other representative body that meets about two miles east of here, you have not assembled to pass laws, though you will express yourselves on laws, regulations and the management of public affairs.

What you do here as businessmen and as citizens should help keep this country moving ahead into an ever greater future. In this country, doing what we can to make the future we want the future we get is a duty we cherish.

I come down here from a manufacturing community where big and exciting things have been happening. The volume of business we have been doing in recent months has exceeded our most optimistic forecasts. It looks now as if this can be one of the motor industry's best years—if not its best year.

Many people have asked why automobile sales are so high this year. The answer has two parts. In the first place, competition in the industry has never been more intense. This has forced more changes and more improvements in our product than in any year for a long way back—and the public has responded by buying these new vehicles in great numbers. In addition, people are showing confidence in the economy and confidence in the future. Buying automobiles is just one way they express that confidence.

Contagious

People are confident because they see business acting with confidence. Throughout the postwar years they have seen business investments in new plant and equipment soaring to unheard-of levels. Within the past ten days we have learned that in 1955 business investments in new plant and equipment are likely to set another all-time record. People are confident because they know they have an administration here in Washington that is conscious of the dynamics of the American economy—an administration which has formed and executed many policies making for stability and encouraging forward-looking business action. People are confident in the future because they understand better than ever before the virtues of our system of private enterprise. They know it has been a major force in creating the kind of civilization we enjoy. They know it has opened up new possibilities for growth. They know our American business economy is an open economy which is geared to exploring and developing the unfenced frontiers of the future.

Ours is an open economy because it gives every man a choice of a thousand roads toward the kind of life he wants for himself and his family. It is an open economy because it is built on a belief in constructive change—and upon all the freedoms that make change possible. It is an open economy because it is always headed toward an open and unscheduled future.

No Standing Still

What I am urging today is a reconsideration and a rededication to the firm faith that the principal force moving us all ahead into that open future is the creative force of competition. At no time in the past have the values of competition been more obvious than in the present period. Competition presents itself to the

American people as a continuous process of creation and change—in which competence and progressiveness are rewarded for bringing us new and better ways of living. The speed of this process permits no business to remain static.

In this competitive world of innovation, of new products and services, no one, big or little, can stake out a claim and hold his ground by virtue of squatter's rights. Gains can be held only by performance.

I speak of the virtues of competition with conviction because of current experience. Many of you know that our own company has helped to set the pace this year in the automobile business. But we know that to consolidate the gains we have made we must move hard and fast—and keep right on moving. This is the reason for our nine-figure investment this year in the company's future—not only expanded plants for building engines, bodies and transmissions—but also sharp increases in research and engineering facilities and manpower.

Our own program of expansion is evidence of our belief that the next twenty years will be one of the industry's greatest periods of accomplishment. Beautiful and efficient and useful as the modern automobile is, the cars of tomorrow will be even more responsive to people's needs. Research will continue to create new markets in this as in other industries.

Whatever happens to the design of the automobile and its power plant, we are confident that its use will increase greatly. By 1975 the one-car family could be in the minority—and a large proportion of families may be using three or more cars.

Ups and Downs

All of us feel optimistic about the long-range prospect for the economy —but at the same time we all recognize that there is no ironclad guarantee that it will gor giht on becoming stronger and stronger and bigger and bigger. Our free and open economy has a wide open future. In that future there is always the possibility of both failure and success, for individuals and for companies. There will be ups and downs for the economy as a whole. But there need not be anything like a serious and prolonged depression in this country if competitive business continues to do its work in the atmosphere of confidence.

One of the best reasons for being confident about the future is of course our rapidly growing population. It will continue to make heavy demands on business — demands which will keep our economy driving ahead to new records. A very important record was set last year when four million sixty thousand babies were born in the United States. This was the biggest baby crop in our history, but it was only the most recent of a long line of bumper crops in the years during and since World War II. And when those youngsters born in the war years grow up and begin to marry and have their own children a few years from now, the population will really begin to grow. The census experts say it will reach 190 million by 1965 and 221 million by 1975.

All of this means that American business has its work cut out for it. The challenge is big and exciting. But there is one aspect of the growth in our population that presents us with a more than ordinary challenge. That is the fact that the working population, those from 20 to 65, will increase much more slowly than the population as a whole. The young men and women now coming of age and entering the working force were born in the depression years when the birth rate was low, and it will be ten to twenty years before those born since the war become workers. In other words, we will add many millions of older people and children to the population during the next twenty years, but not many people of working age. The population is growing fast at both ends and slow in the middle.

Ingenuity and Vision

The job ahead is to produce enough goods and services to meet the needs of a rapidly growing population with a slowly growing force of productive

workers. To do this job successfully will take the ingenuity of our engineers, the vision and hard work of management, farsighted policies on the part of labor, and heavy investments of capital. It will also require a continued understanding and constructive attitude by government toward the needs of the business community.

We have heard a lot about automation lately. Some are concerned about its threat to employment. Automation is really nothing new. It is only a new name for the constantly improving use of machinery and power so as to perform work more efficiently. The result of this continuous development is to raise productivity, multiply opportunity, and raise the general standard of living. Any advances we make in our production methods in the years immediately ahead will help us to expand the economy and, at the same time, support a greatly increased population. So automation—if we want to use that word to describe recent progress in efficient production—is far from being a threat of any kind. Instead, it is a timely blessing—a very timely blessing indeed.

Automation is only one of a thousand avenues of opportunity that are opening out into the future. In the field of atomic energy new developments are coming so fast that it takes a specialist to keep up with them. Just a few weeks ago the Atomic Energy Commission announced that four groups of electric power producers are planning to build atomic power plants for the strictly commercial production of electricity. What this means is that the nation's newest industry—the atomic power industry—is moving out from under the wing of government control. From now on the country is going to watch with the greatest interest as competitive private managements test the comparative efficiency of rival methods of power production.

New Markets

We are now being told that before too many years have passed, the use of atomic energy to make steam to make electric current will be followed by the use of atomic batteries which will convert nuclear energy directly into electricity. Think of the new markets that will be opened up by this one development alone. Think of the revolution it will cause in the way we design and equip our homes and the way we build and operate our factories and offices.

In every other branch of science and technology similar gains are being made. We are on the verge of harnessing solar energy. We are tapping the ocean floor for petroleum. Within the lifetime of some of us in this auditorium it is possible that the great deserts will be irrigated with water from the sea—made fresh by processes yet unknown.

The most significant of all the advances made in recent years are those made by medical science. The recent announcement about the Salk vaccine and its great victory in the fight against infantile paralysis thrilled all of us. Other equally important victories over other diseases are sure to follow.

Every achievement we make as a nation—whether in science, the arts, education, or the general welfare—will depend in part upon the strength of the economy. And the better the performance of business—the faster our advance is likely to be in those other fields.

Nowhere is the importance of our contribution as businessmen more visible than in the defense program. The reliability and to a great extent the design of the weapons of defense depend upon the ingenuity and efficiency of private industry. And the size of the defense program we can afford is related directly to the size of the nation's economic base. The national defense will remain strong as long as we continue to have an industrial community made up of strong companies that compete and compete hard.

It is not our job as businessmen to expert the defense program. But it is our job to produce defense goods and services. And every time we succeed in cutting the costs of producing

tanks or planes or shoes or rations or any of the other million and one defense goods and services the government buys from business we are helping our country to get more for its defense dollar. Here as elsewhere it is competition that provides the principal incentive for bringing costs down—and in this sense competition itself is one of our most powerful weapons of defense.

Schools and Highways

Helping to build a strong national defense is only one of the nation's great challenging tasks to which competitive business makes a major contribution. Another task which is high on the agenda of the nation's unfinished business is the task of providing an adequate education for our rapidly growing population. Here again, our ability to do this job depends directly upon the performance of the competitive business community of America. The new products we create, the efficiencies we achieve, the selling job we do, the economic activity we generate—all these will determine how much the nation can accomplish in building school facilities and attracting a continuing flow of talent into the teaching profession.

To their everlasting credit, businessmen from Coast to Coast are giving strong support to the drive for better schools. They know that good schools make for a good society. They know that the real dynamics of the future are generated in the minds of the young. But business support for schools is not entirely altruistic. It makes good sense from a practical standpoint. Forward-looking businessmen know that the greatest asset of any organization is people — well trained, well balanced people who can carry responsibility and generate ideas. They also know that well educated communities make better markets for the goods and services of business.

Another item high on the list of unfinished business is the building of an adequate system of roads and highways. Those of us who are in the business of building and selling automobiles have a deep and immediate business interest in better highways. We speak on this subject often and we speak from conviction. Great as our interest is, however, it is small compared with the nation's interest in a large-scale, soundly conceived program of highway building.

Year after year we have seen the number of cars and trucks in use grow steadily and rapidly. We have seen tremendous advances in the mechanical excellence of our products. We have seen great technical progress in the fuel that powers the modern vehicle and the rubber it rolls on. And here and there we have seen remarkable advances in the design and construction of superhighways and expressways and traffic controls. Wherever these advances have been made they have generated new values —for industry, for suburban development, for interstate travel and trucking, and for the tourist and resort business. They have made highway travel safer. They have given people a new sense of freedom.

We have made a start toward building the kind of roads and streets and highways we need. Some states and cities have made an excellent start. But in the nation as a whole we are still operating with a highway plant that is hardly an improvement on the facilities we had twenty years ago. And this out-of-date highway system is costing us money—big money.

Needless Costs

In his message to Congress on our highway needs President Eisenhower said that the present highway inadequacies are costing motorists an average of one cent for every mile they drive. This means that as a nation we are spending needlessly about $5 billion a year—in the costs of accidents, the waste of time and fuel, and the many other expenses of operating vehicles on crowded roads and streets.

Far more important than the money we would save with adequate roads is the certainty that well engineered roads would mean a tremendous reduction in the number of lives lost in highway accidents. On the

basis of safety records established on a number of highways of modern design, highway engineers estimate that up to 40 per cent of all traffic accidents could be eliminated automatically if an adequate road program were carried out.

The present administration has roused the nation to the urgency of the highway problem. It has sounded the call to action. At last the people of this country have been made aware of the enormous cost of our obsolete road system. At last they know the tremendous advantages to the economy of a road program on the scale the President has recommended. At last we are thinking big enough about one of our biggest challenges.

I believe that anything less than the size of the program suggested by the President is less than enough to fill the country's needs. Many of the nation's wisest heads have concluded that this is a charge against the future which the country can safely finance now. It is a sound investment if there ever was one.

Encouraging Atmosphere

This country will be able to invest in highways, schools, an adequate defense, and all the other things that are being demanded by our great and growing civilization — if business is permitted to do its job in an atmosphere that encourages competition. I know I speak for you businessmen here today when I say that American business asks no favors from Washington. You are not here to demand special consideration. What you want is the right climate for continuing to do the work that American business has been doing so successfully up to now.

What you are advocating is more reliance on the tried and proven system of free and private enterprise. You are not interested in promoting a system of sheltered and guarded enterprise. You and I have seen strength and efficiency being forged in the heat of competition. We know this has meant risk and venture and courage. You know and I know that in the business life of this country no company—no individual—ever has it made for keeps. No man, no company is beyond the reach of a competitor with a fire in his heart and a big idea in his head. And this is the way we like it .

One Security

As a people we Americans know that there is only one kind of security that means anything. That is the security you gain when you know you are growing and advancing—the security you gain by moving out into the open future—by exploring the tremendous range of possibilities in this Twentieth Century world — and by acting fast on good opportunities when they appear.

There may be a few people in our midst who would build a closed society in America — who would limit competition—who would prescribe the products of industry and plan the level of production and consumption —who would try to determine the future in advance.

I for one do not believe they will succeed. They are singing a song that strikes no response in the American soul. We have been lovers of liberty for a long time. For an equally long time we have been exploring the fabulous possibilities of the universe we live in. And as far ahead as you can see we are going to be showing the world what it means to be dedicated to a free and open and wonderful future for men.

THE STATUS OF LIENS ON REAL ESTATE IN BANKRUPTCY

ELLIS BRODSTEIN, ESQ.

Reading, Pennsylvania

(Presented at the Thirty-Third Annual Convention of the Pennsylvania Title Association.)

Although I have never been accused of having an inferiority complex, I must confess to a certain uneasiness in addressing expert title men on this subject: "The Status of Liens on Real Estate in Bankruptcy."

In the first place, you know all about real estate, because you are specialists in that field, and secondly, you know all about liens on real estate for the same reason; and thirdly, since every good title man has read and digested the Bankruptcy Act of 1800, created by commercial losses in land and in dealings with France, the Bankruptcy Act of 1841, fathered by Daniel Webster, — the Bankrupcty Act of 1867, resulting from Civil War financial stress,—the Bankruptcy Act of 1898, the major Bankruptcy Act, known as the Torrey Bill, and the Chandler Amendments of 1938, plus the one hundred Amendments up to 1953,—I frankly don't have anything to say!

And that should be my cue to say "Thanks, very much," and sit down!

The Law of the State Governs, Generally Speaking, as to Real Estate Liens:

The Bankruptcy Act is the paramount law of the land, and supersedes the State Law on matters connected with the administration of bankruptcy. As to liens on real estate, the Bankruptcy Act and procedure follows the law of the state as to the validity or invalidity of the lien[1].

Of course, there are always exceptions to any such dogmatic statement; but exceptions always exist to prove the rule!

The liens on real estate with which my subject is concerned include the lien of a mortgage, a judgment, a mechanic's lien, a tax lien (municipal, state and federal), a preliminary caveat or lien resulting from the initiation of certain equity proceedings (such as fraudulent conveyances) and other kindred liens; for the life of me, I can't recall any others!

The Lien of Federal Taxes:

Paramount in the discussion of any liens on real estate is the lien of Federal Taxes. There, in the Majesty of Government, stands the Rock of Gibraltar, the immovable and unremovable obstacle, the sovereign's privilege, and all the forces of the Internal Revenue Department—a union of forces that makes for despair and resignation to Fate! For the status of a Federal Tax Lien on real estate in bankruptcy is just as complete and binding as though no bankruptcy exists. Under Section 3670 of the Internal Revenue Code, the all-embracing tax claim of the United States becomes a lien on all property,—real and personal—on the day that the tax assessment list is received by the Director of Internal Revenue: (Sec. 3671) Provided notice thereof is given by the Director: (Sec. 3672). And notice means, in Pennsylvania, recording the lien in the Office of the Prothonotary, in the special docket pertaining to United States tax claims.

Whether the Pennsylvania state lien is obtained by confession of judgment, or by verdict of a jury, or by mortgage, or mechanic's lien, or by arbitrator's award, or by levy on execution, the Bankruptcy Act will honor the validity and priority of the lien, as construed by the law and courts of Pennsylvania. An exception to that statement, if it may be called an exception, is Section 67 of the

Bankruptcy Act, which makes a lien on real estate, obtained through legal proceedings within four months of bankruptcy, null and void as against the trustee in bankruptcy. Section 67 presents a complete set of problems that could not be fully encompassed in this treatise.

Suffice to say, though bankruptcy follows the law of the state on state liens, it follows the law of the Internal Revenue Code on Federal liens; it couldn't very well do otherwise.

Thus, the recorded notice of the federal lien, whether in or out of bankruptcy, constitutes a valid lien on real estate, **subject to priority of payment** only to prior recorded valid liens, duly entered of record, under Section 3672 of the Internal Revenue Code[2]. I emphasize subject to priority of payment, because the foreclosure on a prior lien in the state court will cause a distribution of the fund to be made to the lien creditors in the order in which their liens have been entered of record,—and, at the same time, their liens will be divested and discharged as against the real estate. But the Rock of Gibraltar,—the Federal Tax Lien—will not be budged or moved from its majesty and tenacity unless the fund produces enough to pay the United States in full!

Though Pennsylvania law says that a judicial sale shall divest liens from real estate, our legislature would be powerless to construe the law or enact a law which would divest the lien of federal taxes by a judicial sale. No state can legislate to the detriment of the Federal Government[3] and, by the same token, the purchaser of real estate, sold by due process of foreclosure on a first mortgage, acquires an asset free and clear of all liens, but subject to every unpaid federal lien on the same record! And, therefore, no title company could or should insure the title to that property, without an exception as to unpaid federal liens.

Bankruptcy is the only forum that can do what the state court cannot do. The lien of the Government against the same property may be divested and discharged of its lien if the owner of that property becomes a bankrupt. Courts of Bankruptcy are Courts of Equity, and the equitable nature and powers in bankruptcy vest jurisdiction in the Bankruptcy Courts to order real estate to be sold, not only free and clear and divested of state liens[4], but also divested of any and all federal liens![5]

And the Federal liens may be divested in bankruptcy, irrespective of whether or not the fund created by the sale pays any amount or no amount to the Commissioner of Internal Revenue! Though the conclusion may be startling, it merely illustrates the philosophy of States Rights, vested unto the states by the Federal Constitution and the philosophy of central government under the Constitution, wherein all rights not given to the states, are properly retained by the Federal Government. The Bankruptcy Act, being a Federal Statute and a direct creation of the Constitution, can speak with authority that is paramount not only to any state statute, but is paramount, **in its own field,** to other Federal Legislation such as the Internal Revenue Code!

Where notice of the Federal Tax Lien has been filed by the Director in the Prothonotary's Office, assuming the taxpayer's Pennsylvania real estate is in the county of the Prothonotary—the lien ranks as of the date it was filed; and therefore takes precedence over any mortgagee, pledgee, purchaser or judgment creditor of the taxpayer if those cerditors filed liens after the federal tax lien was filed. Otherwise, if the liens of those creditors were filed before the Federal tax lien was filed, the Federal tax lien will be inferior, as to proceeds of distribution, to those other creditors.[6]

Divesting the Lien of Federal Taxes in Bankruptcy:

Within the limits of this discussion, it would be unwise to go into the many ramifications of the Federal tax lien. Fortunately, my subject does not deal with liens on personality, for on that subject, there is much confusion, if not uncertainty, as to the

practical result of the lien of Federal taxes. Since the Federal lien covers everything, as soon as notice thereof is filed, I have often wondered the effect thereof on goods, such as a can of beans, in the taxpayer's grocery store. Clearly, the United States has a lien on that can; and the purchaser buys it, and eats it, subject to the Government lien. I know of no instance where the Government attempted to follow the can or the beans; what would happen, if it did, presents a stimulating and interesting situation.

Suffice to say, the Pennsylvania Title Association received, in 1951, at the Claridge, in Atlantic City, an erudite and comprehensive lecture on "United States Liens" by the distinguished Chief of the Federal Tax Legal Section, Ira Hirschberg, Esq., of Philadelphia. And I could not possibly give you more, or as much, as Mr. Hirschberg then did!

I have read with much interest an article that appeared in "Taxes," the Tax Magazine, in June, 1952, published by CCH. The author, J. Walter Feigenbaum, Esq., an attorney in the Bureau of Internal Revenue, at Washington, D.C., makes the statement to the effect that in bankruptcy, if the Court orders the real estate sold free and clear of all liens, the liens attach to the proceeds of the sale. With that statement I agree. But I cannot agree with his next statement, to wit:—

> "Suppose . . . that property subject to Federal tax liens is sold through the processes of the bankruptcy court, but the items of Federal taxes secured by the liens have not been paid in full. In such a situation, there has certainly not been effected either a release of the Federal tax lien or the discharge of the property from the effect of the Federal Tax lien through administrative action . . ."

I must dissent from that last statement: If the "administrative processes" in bankruptcy resulted in an order of Court, specifically naming the Federal tax liens of record, and specifically ordering the property sold, free and clear and divested of those tax liens, those tax liens would be divested as liens against the real estate, whether the fund paid the tax liens or not!

Mr. Feigenbaum admits, in the same article, that the Bankruptcy Court has the inherent power to order a sale free and clear of any tax liens —state or federal—and cites the leading case of Van Huffel v. Harkelrode, Treas., 284 U.S. 225 (1931) as authority for such power in the Bankruptcy Court, and for authority that the purchaser at such sale will receive the property "free and clear from Federal Tax Liens."

But, like all lawyers who represent the Government, especially in Internal Revenue, he refuses to admit flatly that the Supreme Court of the United States is one hundred per cent proper when the decision is against the Bureau, and suggests to the purchaser that "he should endeavor to secure the discharge of the property . . . from the effect of Federal tax liens pursuant to provisions of Section 3674 (b) and the regulations applicable thereto"!

That, in my opinion, is putting an unnecessary burden and expense on the purchaser, the title company, the title searcher and the parties who are interested in the real estate sale and purchase! The burden and expense of divesting the tax liens has already been borne by the Bankruptcy Court, and its decision is so complete and final that no other rigamarole is either necessary or proper! The constitutional powers vested in the Bankruptcy Courts were not designed to aggravate the honest citizenry of the United States and prevent, instead of assure, life, libery, due process, etc.

A notorious rabble-rouser once complained to Benjamin Franklin that the Constitution of the United States was a mockery. "Where is all the happiness it is supposed to guarantee us?" he demanded.

"All the Constitution guarantees, my friend," Franklin answered, "is the pursuit of happiness. You have to catch up with it yourself."

Bankruptcy Jurisdictions in the Divestitutes of Liens:

The extraordinary power of the Bankruptcy Court to divest the lien of Federal taxes includes the power to divest all liens—even the lien of a first mortgage. To those of us who have grown up in the real estate and mortgage field under Pennsylvania law, that comes as a startling statement. The Pennsylvania first mortgage has been the bulwark of investment, the sturdy income-producer for the retired gentleman, the sacrosanct in the regard of judges, lawyers, bankers and financiers. But the statement, though startling, is quite true, and first mortgages, along with other liens, are often divested through sales of real estate in bankruptcy. Courts of bankruptcy are extremely careful, however, to enter no order divesting any liens against real estate unless the evidence indicates a definite probability that the fund realized from the sale will realize enough to pay all liens and expenses, and also leave a surplus for unsecured creditors. Otherwise, the court would not be doing "equity."

But let it be clear,—that the order of Court, after due consideration, directing a sale, free and clear of all liens, the purchaser will get whatever title the bankrupt had, free and clear of the liens specified in the trustee's petition **whether or not the price paid is sufficient to pay all or any lien creditors!**

While speaking of the sanctity of the Pennsylvania mortgage, it is well to note the full protection afforded by the Federal Courts of the Third Circuit. A bankrupt, either as debtor in possession, or his trustee, may operate an income-producing parcel of real estate for a limited period. However, that will be no detriment or loss to the mortgagee: He is entitled to receive, without prior demand, and without having entered into possession before bankruptcy, the net income from the property, if needed to pay the amount owing on the mortgage. Of course, net income is gross income less appropriate administration expense, operating expense, and taxes, as fixed by the Court. The mortgagee need not wait until the completion of the bankruptcy case before receiving such net income.[7]

As in all court proceedings, the sale of the real estate must be confirmed by the Bankruptcy Court; and the Court, in its discretion, may refuse to confirm the sale for any of the reasons that immediately come to mind—to wit, gross inadequacy of the price compared to the value of the real estate, restraint in permitting competitive bidding, fraud, improper outside interference or disturbance detrimental to the sale, and so on, and so forth. But mere failure of the purchase price to be in excess of the discharged liens is no ground for the court's refusal to confirm! And the Court will confirm the sale, generally, where the price realized is adequate in relationship to the appraised value of the real estate.

Other reasons may exist whereby the Court will, with propriety, order a sale free and divested of all liens even though the evidence indicates no equity for unsecured creditors: Liens may overlap, blanket mortgages may cover two properties, but the entry of judgment on the bond becomes a lien against three properties; the entry of mechanics' liens may be questioned as to their technical validity; liens entered within four months may be void, or they might be voidable and perhaps set aside as a preference, etc.[8] In such a case, it is not only equitable but good practical business to convert the real estate into cash and let the conflicting liens litigate against the fund. Everybody gains by this method: The real estate stops being idle, the plumber and the carpenter go to work, the place is repaired and occupied, and the new mortgagee and the taxing authorities start to draw an income; the title insurance company gets a client, collects its modest premium, and the buyer's lawyer earns a fee, and, incidentally, the attorney for the trustee profits by this example.

In other words, the equity powers and jurisdiction of the Bankruptcy Court creates a practical asset to the community; and the delay, if any, of

marshalling liens and making distribution of the fund to lien creditors is considerably less harmful to the community than depriving the community of a useful piece of real estate!

Lien Foreclosure Before and After Bankruptcy:

In recognizing the validity of the lien according to the law of Pennsylvania, the Bankruptcy Law recognizes the exclusive jurisdiction of the state court, where the court has taken jurisdiction before any bankruptcy intervened. The classic example is that of the mortgagee whose mortgage was entered of record about two years ago, finds his mortgagor in hot water, with no money, and with inability to pay his mortgage installments as they become due. Reluctantly, the mortgagee tells his lawyer to foreclose. The lawyer, in accordance with usual practice, enters judgment by confession on the mortgage bond, and the Sheriff levies on the mortgaged real estate.

One week later, before the foreclosure sale could possibly take place, the mortgagor is forced into bankruptcy. The trustee in bankruptcy petitions the Federal Court to restrain the sheriff from proceeding on the **plausible** ground that title to the real estate has vested in the trustee on the date of adjudication in bankruptcy; that the true value of the property is $25,000.00, whereas all liens are only $15,000.00; that an equity exists for unsecured creditors, and therefore the real estate should be administered and sold in bankruptcy, and further, that the judgment on which the execution has issued was entered within four months of bankruptcy and is therefore null and void under Section 67 of the Bankruptcy Act.

All of which sounds **plausible**—but it isn't reasonable nor is it an equitable argument: Although legal title vested in the trustee as of the date of adjudication, the state court was entitled to retain exclusive jurisdiction because the judicial process of the state court had already taken over; and taken over based on a valid lien, since the lien of the judgment entered on the mortgage bond dates back, two years, to the date of the mortgage entry; and if the property is as valuable as the trustee says, then it becomes the duty of the trustee to attend the sheriff's sale, bring purchasers and bidders, and claim the fund from the sheriff that is in excess of all valid liens![9]

But what happens to the mortgagee who has the temerity to foreclose his mortgage **one week after** bankruptcy? He gets slapped, and slapped hard and vigorously, by none other than the Supreme Court of the United States. That august and venerable court has declared, in no uncertain terms, that such a mortgagee is a very bad boy, legally speaking; that when the Bankruptcy Court has acquired initial jurisdiction over the bankrupt's assets, no other court, but **no** other court, could step into the picture; and not even another Federal Court; that the jurisdiction of the Bankruptcy Court, in its field, is paramount, and that court must and shall administer the real estate, unless the Bankruptcy Court itself voluntarily relinquishes its own jurisdiction![10]

The Validity of Liens Obtained by Judicial Proceedings, Within Four Months of Bankruptcy:

Probably the most important section of the Bankruptcy Act, dealing with liens, is Section 67:

At first I had hoped that its inclusion herein would not be necessary, but it really can't be avoided. It's a complicated section: it contains twenty long paragraphs, and many long sentences, and many restrictions and exceptions.

Briefly, its importance to the subject is stated in the first paragraph:—

> "Every lien against the property of a person obtained by attachment, judgment, levy, or **other** legal or equitable process . . . within four months (before bankruptcy) . . . shall be deemed null and void.
>
> "(a) If at the time when such lien was obtained such person was insolvent, or (b) If such lien was sought and permitted in fraud of the provisions of this title . . ."[11]

So that every lien, obtained by legal process, is void, if entered within four months of bankruptcy, if the facts are as set forth in the first paragraph.

But the section doesn't stop with a mere declaration of "null and void"; The third paragraph says that the

"Property affected by any lien deemed null and void . . . shall be discharged from such lien . . . and such property . . . shall pass to the trustee (in bankruptcy) . . . and the court may direct such conveyance as may be proper . . . to evidence the title thereto of the trustee . . . Provided, however, that the title of a bona fide purchaser of such property shall be valid, but if such title is acquired otherwise than at a judicial sale held to enforce such lien, it shall be valid only to the extent of the present consideration paid for such property."

Now here, you can very well see, is a pretty kettle of fish for the title insurance company, especially caused by the later paragraphs of Section 67, to wit, (d) 2 and 67 (d) 3.

Let us confine our present discussion to the lien of a mortgage on real estate.

A mortgage lien on real estate is **not** a lien created by "legal proceedings"; such a lien is **contractual** and does not fall into the prohibition of Section 67 (a) as to "liens obtained within four months by legal or equitable process."[12]

Section 67 Can Make a Good Lien —Bad, Nevertheless.

Sections 67 (d) 2 and 67 (d) 3 are possible causes for a mortgagee to lose a good investment, and for a grantee to lose a bargain in real estate.[13]

67 (d) 2 makes "every transfer made and every obligation incurred by a debtor within **one year"** prior to bankruptcy,—

"fraudulent (a) as to creditors existing at the time of such transfer or obligation, if made or incurred without **fair consideration** by a debtor who is . . . insolvent, without regard to his actual intent . . ."

Section 67 (d) 3 says that

"Every transfer made and every obligation incurred by a debtor who is . . . insolvent, and made **within four months** prior . . ." to bankruptcy is fradulent "as to **then** existing and **future** creditors (a) if made or incurred . . ." in contemplation of bankruptcy "with intent to use the consideration obtained for such transfer or obligation . . . to enable **any creditor** of such debtor or to obtain a . . ." preference, and "(b) if the transferee or obligee . . . at the time of such transfer or obligation, knew or believed that the debtor intended to make such use of such consideration."

And Section 67 (d) 6, which makes the above transfers or obligations null and void as against the trustee in bankruptcy, nevertheless protects the transaction, and keeps it inviolate, as "to a bona fide purchaser, lienor or obligee for a **present fair equivalent value"**; and, as to "such purchaser, lienor or obligee, who without fraudulent intent has given a consideration **less than fair** . . . may retain the property, lien or obligation **as security for repayment."**

To start at the end, What is a "fair consideration?" 67 (d) 1 defines it:—

"Consideration given for the property or obligation of a debtor is "fair" (1) when, in good faith, in exchange and as a fair equivalent therefor, property is transferred or an antecedent debt is satisfied, or (2) when such property or obligation is received in good faith to secure a present advance or antecedent debt in an amount not disproportionately small as compared with the value of the property or obligation obtained."

Where a bona fide mortgagee has advanced a present consideration for the mortgage lien, of course he will be protected to the amount actually advanced.[14]

Title insurance is not the cure-all or complete protection for all matters involving real estate, not only because of bankruptcy, but for other obvious reasons. It goes as far as humanly and legally possible to insure real

estate ownership and ownership of mortgage liens. But it stops short when bankruptcy intervenes under certain situations, created by the language of Section 67!

The Lien Insured By the Title Policy:

A title policy is a contract of indemnity insurance which covers the risk of loss through defects that might cloud or invalidate the insured's title.[15]

And where one in possession of land and claiming title in fee applied for title insurance in good faith, and thereafter it was decided in partition proceedings that he had only a one-half interest, the insurance company was held liable and it could not claim that, as the assured never had title to the one-half interest he had suffered no loss.[16]

An excellent definition of the title policy is recited in Trenton Potteries v. Title Guarantee & Trust Company, 176 N.Y. 65:—

"The contract is one of insurance against defects in title, unmarketability, liens and encumbrances. The risks of title insurance end where the risks of other kinds begin. Title insurance, instead of protecting the insured against matters that may arise during a stated period after the issuance of the policy is designed to save him harmless from any loss through defects, liens or encumbrances that may affect or burden his title when he takes it. It must follow, as a general rule, therefore, that when the insured gets a good title, the covenant of the insurer has been fulfilled, and there is no liability . . ."

The title of a mortgagee may also be insured against defects, and such a policy is construed as insuring the title, and not the security."

And title companies have discovered, to their dismay, that the insuring of a mortgage, which resulted in a preference under the Bankruptcy Act, made the title company liable to the mortgagee for the loss of his security.[18]

The usual exceptions in a title policy, "excepting defects and incumbrances assumed or agreed to" by the insured, are of no aid to the title company, said the same court in First National v. N.Y. Title Insurance Co., —supra,—; the court held that the exceptions were not applicable to the invalidity of the insured's mortgage because a **preference was created under the Bankruptcy Act.**[19]

Invalidity of the Mortgage Lien Under 67 (d) 2.

But let us not be unduly alarmed by these alarming quotations and court decisions and statutory enactments! Title insurance will still continue to earn enough to pay the salaries of all the title officers,—and, after all, what else matters?

To get back to the subject of real estate liens in bankruptcy, may I just pin point an example of possible loss to the title company, through loss to its assured, the real estate mortgagee, and its assured, the real estate purchaser!

Take the case of an owner of real estate having an undisputed fair value of $25,000.00. He tells his purchaser that he is broke and insolvent and he needs $15,000.00 to move his sick wife to the dry climate of Arizona. The purchaser, realizing the great bargain, agrees to buy and places title insurance; since the purchaser has only $5,000.00 in cash, he applies to the bank for a $10,000.00 mortgage. **The bank and the title company are made acquainted with all the facts.** The title company issues its routine policy to protect both the mortgagee and the purchaser, and, at the settlement, all parties are present and all the facts are recited as above.

The settlement goes through, the mortgagee acquires a valuable investment of $10,000.00, payable in twenty years, with interest at **6%**, and the purchaser acquires a bargain in the house and happly moves in, and the seller gets his $15,000 to cure his wife.

All the facts are truthful, all the actions are bona fide, all parties know the facts, and there are no other facts which the title insurance company could or should know.

However, bankruptcy of the seller takes place eleven months after the

settlement; and the undisputed fact is that the seller, at time of settlement, was definitely **insolvent!** Now, what could happen to affect the mortgage lien, or the purchaser's title to his property?

Let us confine ourselves to **Section 67 (d) 2,** and forget about the complications under 67 (a) 1, 67 (a) 3, or 67 (d) 3.

Remember that 67 (d) 2, in effect, makes every transfer, and every obligation, "incurred by a debtor within one year" before bankruptcy FRAUDULENT

> "(a) as to creditors existing at the time of such transfer or obligation, if made or incurred without fair consideration by a debtor who is . . . insolvent, without regard to his actual intent . . ."!

And the seller's creditors existed at the time of settlement for the property, as well as on the date of his bankruptcy!

The diligent trustee in bankruptcy moves swiftly: He finds another buyer for the house—for $25,000.00—and the original purchaser has lost his bargain and lost his house! True, he must get his $5,000.00 back, plus expenses, because Section 67 (d) 6 permitted him to retain the property as security for repayment! The $5,000.00 return to him is cold comfort: His wife plays bridge with desirable neighbors, and his children are at school in the next block! The title company has insured his title, and is there anything he can do to the title company?

Frankly, I don't believe there is a thing he can do—except regret his "Bargain"!

I am not forgetting the bank mortgagee who holds a valuable investment of $10,000.00, payable in twenty years, at 6% interest. The interest over a period of twenty years that the bank mortgagee would receive would amount to exactly $7,196.00. That's a lot of interest, **not** to get! Especially with 100% security. Of course, the trustee in bankruptcy would have to repay to the mortgagee the face amount of the mortgage—$10,000, with perhaps eleven months' interest, if the interest had not been paid—but the $64 question is: Could the mortgagee properly sue and collect from the title insurance company the "unpaid" interest of $7,196.00? After all, says the mortgagee, you insured me against any defects that might "cloud or invalidate" the title of the property; and the existing facts, existing at time of settlement, openly stated and known to all parties, made the transfer of the real estate legally fraudulent, and therefore, void, as to the seller's later trustee in bankruptcy.

Frankly, I know of no case decided on this exact set of facts; but if the Foehrenbach case is good law today, and I believe it is, and if the case of First National Bank v. N.Y. Title Insurance Company is good law today, and I believe it is, I would recommend to my client, the mortgagee, to endeavor to sue the title company for $7,196.00!

May I summarize my reasoning for for that conclusion:—

The title policy did not indemnify the mortgagee that either the principal or interest would be paid; but it did indemnify the mortgagee that the known existing facts, at time of settlement, were such as to vest an undisputed and absolute title in the purchaser. And therefore, if the known facts then existing were such as to divest the purchaser's title, then the title policy should make the mortgagee whole; and the only way to make the mortgagee whole is to pay the interest as well as the principal!

Assuming, of course, that the value of the real estate is greater than the mortgage plus interest thereon.

The Foehrenbach case is cited with approval by the Supreme Court of New York in First National Bank v. New York Title Insurance Company (12 N.Y.S. 2d 703, at Page 711) in these words:

> "In that case the plaintiff supposed that he was the owner of the entire interest in certain real property. He applied to the defendant for title insurance. The policy was issued. Subsequently, others claimed an interest in the premises. They

brought an action in which it was held that the plaintiff possessed only a half interest and not the whole of the property. The trial court dismissed his complaint against the title company upon the ground that he had lost nothing. Upon appeal, the plaintiff was awarded judgment in his favor. It was said that 'failure to keep that which one has is loss." Also, "The estate or interest of the insured which was covered by the policy was that of owner in fee of the entire property and any defect in title which reduced his interest below that point was, it seems to us, just that much loss, or damage, for which he was entitled to be indemnified'.

"That decision is directly applicable here. Applying these principles, the plaintiff here certainly sustained a loss and damage within the meaning of the policy."

The New York title case makes an interesting comment on the nature of a title policy, and cites the Foehrenbach case in support thereof:—

"The quality of a title is a matter of opinion, as to which even men learned in the law of real estate may differ. A policy of title insurance means the opinion of the company which issues it, as to the validity of the title, backed by an agreement to make that opinion good, in case it should prove to be mistaken, and loss should result in consequence to the insured."

Invalidity of the Mortgage Lien Under 67 (d) 3.

We have just considered 67 (d) 2 which might void a mortgage if given within twelve months of bankruptcy. However, 67 (d) 3 creates a situation that might void the mortgage **only** if bankruptcy occurred within four months after giving the mortgage, on the ground that it constituted a preference to a creditor.

May I call your attention to a set of facts where the title company insuring the mortgage may again be compelled to pay the mortgagee for his loss?

Let us go back to the same insolvent debtor who owns a house worth $25,000.00—and whose wife needs a trip to Arizona for her health. This debtor owes the bank $10,000.00 on a note endorsed by his father-in-law. The note is in default, the father-in-law is worthless, the bank examiners are coming tomorrow, and the finance committee is alarmed! So the President calls in the debtor and says, "Brother Jones, I know you're broke and insolvent, your wife is sick, your creditors are pushing, and if you go into bankruptcy, the bank and your other creditors won't get ten cents on the dollar. But you can't do this to me,—me, your best friend, who helped you before, and who played golf with you, etc., etc. My finance committee has told me—either get the bank a mortgage on your house, or find yourself another job!"

So the debtor, grateful to his friend, the President, agrees to give the bank a mortgage for $10,000.00, to secure the debt.

The President and the debtor reveal all the above facts to the title company and the bank requests a policy on the proposed $10,000.00 mortgage. The record is clear, the mortgage is written, duly recorded, and the policy issued to the bank. Three months later the debtor becomes adjudicated a bankrupt.

Of course, you know the answer: The trustee in bankruptcy has acquired a valuable asset for all the creditors, to wit, a house worth $25,000.00—free and clear of the bank's $10,000.00 mortgage!

And why? Because all the elements of a voidable preference exist under 67 (d) 3:—[20]

(a) The obligation was incurred within four months by an insolvent debtor.

(b) In contemplation of bankruptcy.

(c) With intent to give a preference to the bank.

(d) And the bank knew all about it.

Understand, please, I find no fault with the bank or the debtor! There is nothing wrong, legally or morally, in a debtor preferring one creditor over

another.[21] There is no fraud involved on either side and the impulse of the bank to seek protection for its depositors and stockholders, and the impulse of the debtor to protect his good friend, the President, is human and understandable. And if no bankruptcy ever occurred, the transaction could not be questioned.

At common law and in the absence of statutory prohibition, an insolvent debtor has the right to prefer one creditor over others. A preference is malum prohibitum only to the extent that it is prohibited by the Bankruptcy Act.[22]

But bankruptcy did occur within four months, and the Federal Court has declared the $10,000.00 mortgage as null and void! So where does that leave the title company, who insured the mortgage for the bank, who earned a small premium for the policy of insurance, who efficiently and thoroughly cooperated with its client, the bank, **with full knowledge of all the facts,** who searched the records for mortgages, judgments, mechanic's liens, adverse conveyances, the equity and appearance docket, tax liens, etc., etc., and found everything on the record even whiter than the driven snow?

It leaves the title company holding the bag to the tune of $10,000.00, payable to the order of the bank! Again, I cite the Foehrenbach case, and especially, First National Bank v. New York Title Insurance Company.

Can the Title Company Exclude Liability to the Mortgagee If the Seller Becomes a Bankrupt?

That question is pertinent, and provokes a thoughtful problem.

The Policy Form of the American Title Association (Standard Loan Policy) contains some strong language for the protection of the title company. In Paragaph 8,

"The company will not be liable for loss . . . by reason of defects . . . created subsequent to the date hereof . . . or for defects . . . created or suffered by the Insured . . . or **existing at the date of this policy** and **known to the insured . . . at the date such insured claimant acquired an insurable interest but not known to the company or disclosed to it in writing by the Insured . . .**"

I don't know how you could strengthen that clause. It directly avoids liability for any facts, known to the assured, which are not disclosed to the company; and, by the same token, properly implies that the company should and will be liable, if the company has full knowledge of all the facts that might result in loss. No contract can absolve the company of blame and liability by any statement to the effect that the company is excused from liability even though it knowingly and negligently wrote a policy that would result in liability. That would be equivalent to no contract at all.

The New York case of First National Bank v. N. Y. Title Insurance Company, supra, contains some dicta to the effect that the title company might have inserted a clause in the policy saving itself harmless from any future events that might cause loss under the provisions of the Bankruptcy Act. It was a passing comment, and I don't believe the judge put much faith in that statement. It is true that a debtor can waive his privileges under many laws, such as waiver of exemption in a note confessing judgment, waiver of inquisition and condemnation as to real estate, etc., etc., and agree that his bankruptcy might accelerate the time of payment of an obligation; but I know of no authority that would permit anyone, either a debtor or a title insurance company, from waiving the legal effects under bankruptcy.

If the title policy sought to protect itself by inserting such a clause as the New York case intimates, I believe it would be futile. It would be comparable, though not analogous, for the title policy to insert a clause stating—"If the President of this title company runs away with all our money, we won't be liable for any loss or damage to the assured"!

The Title Searcher's Problem on the Divested Lien:

Under the Equity Powers of the

Bankruptcy Court, real estate may be ordered sold by the trustee, free and clear and divested of liens.

When the title searcher traces the chain of title, he will find a deed on record from the trustee, as grantor, to a grantee who acquired the real estate under order of the Bankruptcy Court. The deed, being a trustee's deed, will briefly recite the proceedings resulting in the order of sale. And the recital in that deed will furnish information as to how it was acquired by the bankrupt. The trustee's existence is evidenced by the record in the Recorder's Office, because the trustee, under Section 47-c of the Bankruptcy Act, is required to file with the Recorder a certified copy of the order approving the trustee's bond.

It is, therefore, more or less routine for the title searcher to establish the chain of title.

But how can he establish as to whether or not the liens of record against the bankrupt have been divested by the trustee's sale of the real estate? No lienholder may have his rights divested without due process, and, unlike a judicial sale, such as a foreclosure sale by the sheriff on a first mortgage, which divests by operation of law all junior liens (excepting Federal tax liens), no lien will be divested in the bankruptcy sale unless the trustee's petition and the order of court

(a) Specifically mention and fully describe the lien, and

(b) Due notice of the proposed divestiture is given to each lienholder, and

(c) The sale order of court specifically mentions each lien, and

(d) Due notice of the order must be given to the lienholder, and

(e) The order of court in confirmation of the sale is especially important.[23]

These five steps in the process of sale constitute "due process," and adequately provide the notice which will give the lienholder his day in court.

The title searcher, from a check of the lien record, knows what liens existed. Where can he find whether each lien was divested by "due process"? Obviously, he will examine the pleadings in the Referee's office and find all the answers there, provided the Referee still has the pleadings. In most cases, by the time the title man gets on the job, the bankruptcy case has been closed, and all the pleadings have been deposited with the Clerk of the United States District Court.

Thereupon, the title searcher draws on his expense account, travels to the Clerk's office, and inspects the record in Philadelphia, if the property is in the Eastern District, or in Scranton, if it's in the Middle District, or in Pittsburgh, if it's in the Western District of Pennsylvania!

There can be no short cut for assurance that the liens have been divested, unless the "due process" pleadings have actually been checked! And the pleadings must reveal that each lien is specified, for divestitute!

If the lien is **not** mentioned, the sale, free and clear and divested of liens, will not divest the lien of the unmentioned one!

It would be helpful if the title companies would get the Bankruptcy Act amended, or have the Supreme Court of the United States adopt a General Order in Bankruptcy, compelling the trustee to record, as a minimum, the petition to sell, which lists the liens, and the order of court directing the sale, which also lists the liens to be divested. That would save considerable leg work as well as mental anguish on the part of the title searcher, as well as obviating the delay caused by a visit to the metropolis housing the District Court!

It would even be more helpful, when bankruptcy discharges a lien, to have some method directing the Prothonotary to note on record that the lien has been discharged.

In Fuhrman v. Guarantee Trust, 80 D. & C. 116, the court refused, in quiet title proceedings, to order the divested mortgage to be marked "satisfied" because it was not paid in full. Judge Troutman, in the above Nor-

thumberland County opinion, clearly implied that he had jurisdiction to direct the Recorder to mark the mortgage record "Discharged", by virtue of the bankruptcy sale.

LIENS ON REAL ESTATE AFTER ADJUDICATION:

Liens on real estate created after adjudication in bankruptcy are invalid for the simple reason that Section 70 (a) of the act vests the trustee "by operation of law with the title of the bankrupt as of the date of the filing of the petition . . ." I know of no law in any State of the Union which will permit a lien to be filed against the property of a stranger who is, in no sense, the debtor against whom the lien was obtained. The Trustee is the legal owner of the bankrupt's property as of the date of bankruptcy, and a lien **thereafter** entered against the name of the bankrupt would be meaningless.

STATUTORY LIENS:

There is, of course, an exception to this rule, and that is in **67 (b)**. Quoting the pertinent phrases, **67 (b)** provides that

> "Statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons . . . created or recognized by the laws of the United States or any state, may be valid against the trustee even though arising or perfected while the debtor is insolvent and within four months of . . . (bankruptcy). Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may, nevertheless, be valid if perfected within the time permitted by and in accordance with the requirements of such laws . . ."

As far as real estate is concerned, especially under Pennsylvania law, statutory liens would be primarily those liens created under the Mechanic's Lien Law of Pennsylvania, and covering building contractors, subcontractors, material-men, architects, construction engineers and the like. They are definitely liens created by statute.

It isn't always easy to label a lien as statutory or non-statutory. Common law liens, equitable liens, contract liens and similar liens are clearly not statutory and therefore would not be saved by Section 67 (b).

THE LIEN OF THE PURCHASE MONEY MORTGAGE:

But take the purchase money mortgage which, though contractual in nature, is supported in its lien properties by the Pennsylvania Act of April 27, 1927, P.L. 440 (21 P.S. 622,) to the effect that

> "Any mortgage, given by purchaser to seller, for any part of the purchase money of the land so mortgaged, shall have a lien from the time of the delivery of said mortgage, provided the same **be** recorded within thirty days from the date of the mortgage."

I would call to your attention that a "statutory lien" within the purview of Section 67 (b) even though it is purely contractual in nature; and if the mortgagor became bankrupt on the 28th day and the purchase money mortgage was recorded on the 29th day after the date of the mortgage, it seems obvious that the mortgage lien has been "perfected" properly and "within the time permitted by and in accordance with the requirements of such laws."

The Pennsylvania Act of 1927, supra, was repealed, **as to inconsistencies only,** by the Act of June 28, 1951, P. L. 927 (68 P.S. 601), known as the "Lien Priority Law." However, the Act of 1951 merely re-emphasized that recording of a purchase money mortgage must take place within thirty days after the date thereof, and broadened the definition of "purchase money" by eliminating the phrase "given by purchaser to the Seller."[24]

THE LIEN OF A NON-DISCHARGEABLE DEBT:

Unlike Gaul, the Bankruptcy Act is divided into seventy-two parts, instead of three. And those parts, excluding the various later Chapters X to XV, are known as stright bankruptcy law and comprise seventy-two sections. One Section, Section 17, lists

a number of "delightful" Shenanigans which will not and cannot be discharged in bankruptcy. Parenthetically, there is not much relevancy under my subject for a discussion of the discharge of debts section, because the vast majority of liens, in bankruptcy, are based on debts which would normally be discharged as to personal liability, even though the lien is not divested from the real estate.

A lien on real estate, obtained through the process of legal action by suit at law, and **based on a cause of action, non-dischargeable in bankruptcy, is just as much a valid lien as the lien obtained for a debt that is discharged in bankruptcy.** And, by the same token, both liens may be divested by an order of the Bankruptcy Act, directing a sale free and clear of liens. It should be emphasized, however, that the divesting of the lien of the non-dischargeable debt does not discharge the bankrupt from personal liability. The goal of every bankrupt is to receive a discharge from his debts; otherwise, there would be very little point to his being adjudicated a bankrupt in the first place.

Congressional sentiment and progressive economic philosophy in the fortunes and misfortunes of man has culminated in a worthy goal, and that is, primarily, to enable creditors to share equally and proportionately, under the law, in the assets of a debtor, thus eliminating the spoils that go to the swiftest runner, and secondarily, to enable an honest debtor to be discharged from his debts, and to start life anew, and unburdened by his old debts, and take his place in the community of his working fellow men, with the privilege of acquiring many and varied debts![25]

But the debtor, honest as he may be, is not discharged from every obligation. Section 17 lists twelve kinds of debts which are not dischargeable; briefly, without listing all twelve, he cannot be discharged from debts or claims or judgments resulting from his embezzlement of money, from willful and malicious injuries to person or property, from obtaining money under false pretense, from unpaid alimony, from tax liability, from money withheld from an employee, and, for no good reason that the philosophy of bankruptcy should be concerned—from breach of promise accompanied by seduction, or for seduction of an unmarried female. Or for criminal conversation!

So, in conclusion to this irrelevant paragraph, may I simply repeat, the lien on real estate, obtained through a non-dischargeable claim or debt, is just as valid and binding as any other lien obtained through legal or equitable proceedings; and though the lien may be divested as against the real estate, the debtor's personal liability continues for as long as the Statute of Limitations will permit.

CONCLUSION:

Any discussion involving bankruptcy should emphasize that the equity powers of the Bankruptcy Court are fundamental and basic, even to the extent of overriding the State Law.

> "The court of bankruptcy is a court of equity to which the judicial administration of the bankrupt's estate is committee; and it is for that Court, not without appropriate regard for rights acquired under rules of state law, to define and apply Federal law to determine the rights of parties litigant."[26]

There a defendant in a state court invokes Federal Bankruptcy law as justification for the defendant's refusal to comply with the order of the state court, any conflict of jurisdiction must be resolved in favor of the paramount Federal law; Securities v. Louisville & N. R. Co. (1953), 94 Ohio App. 323.

A bankruptcy court is a court of equity and is guided by equitable practices and principles, except insofar as they are inconsistent with the bankruptcy act itself: Re Jensen (1953), 200 F. 2d, 58.

The United States Supreme Court has said "The theme of the Bankruptcy Act is equality of distribution." But this theme is barely suggested by the terms of the Act.

> "The Act does not say what constitutes equality of distribution;

determination thereof is left to the Bankruptcy Court, as a court of EQUITY, on a case to case basis. But the equity power of the Bankruptcy Court is essentially the power to carry out bankruptcy objectives. The problem is not the scope of equity but the scope of bankruptcy . . . Once the bankruptcy objectives are defined in a given situation, the equity jurisdiction of the bankruptcy courts affords a flexible and effective instrument for attaining them."[27]

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DISCUSSION

PRESIDENT BURLINGAME: Thank you, Mr. Brodstein.

I know there must be questions. Who has one? Well, I do.

Mr. Brodstein, you touched on the situation of the mortgagee who started execution, and there was a selling order in the sheriff's hands, and then the issuance of a restraining order on the sheriff. I don't recall that you carried that to a conclusion. You hinted it was wrong, but is it effective?

MR. BRODSTEIN: The procedure of foreclosing of the mortgage lien before bankruptcy, based on the mortgage which is more than four months old, will not be restrained by the Federal Court, if bankruptcy intervenes. Therefore the state court will continue to take jurisdiction and have its sale by the sheriff in the usual manner.

I say that the trustee in bankruptcy can only come to the sheriff's sale and bring debtors and purchasers in the hope there will be realized more than the valid liens against the real estate.

PRESIDENT BURLINGAME: Not to prolong the discussion but recently we witnessed in Montgomery County a case where there were a series of mortgages entered by a debtor more than four months prior to bankruptcy. There was a default. Judgment was taken on the warrant of attorney; properties were advertised, posted by the sheriff's office and the sale date was fixed. In the meantime there was bankruptcy — first it started under Chapter 11 and then went into bankruptcy, and the trustee at Federal Court in the Eastern District issued a restraining order on the sheriff not to sell and there was no sale.

MR. BRODSTEIN: Those mortgages were all more than four months before the bankruptcy, and the rea-

son the Federal Court issued restraining order was because the mortgagee did not object. If the mortgagee would have objected, the Federal Court would not have issued that restraining order.

PRESIDENT BURLINGAME: Sometimes the mortgagee does not have the time to object.

MR. OLIVER: Speaking about the ability of the bankruptcy in Court to discharge a first mortgage by a proper order, properly entered, even though the fund created was not substantially in excess of the mortgage obligation: They pointed out that they could do it even though the amount in the bankruptcy sale was not adequate to pay the mortgage, but you didn't touch on the interesting problem as to the priority of payment, as to the mortgagee and bankruptcy costs, the trustees fees, auctioneer's expenses, etc.

MR. BRODSTEIN: Bankruptcy costs always have priority. They even have priority over Federal tax liens, and they have priority over a divested first mortgage. That is not my own opinion; that is so stated in the Bankruptcy Act, as to what shall be the first cost and first payment made, and either No. 1 or 2 says the Costs.

Now of course you can always make a deal where your mortgagee makes a deal with a reasonable trustee and can say "If you are going to divest my first mortgage, o.k., but don't charge me more than $200, what it would have cost to foreclose at the sheriff's sale" and the reasonable trustee will agree.

PRESIDENT BURLINGAME: Are there any other questions?

Mr. Brodstein, another question was raised in the case of the gentleman who had to send his wife to Arizona. Is the burden on the trustee to prove the insolvency or is the burden on the debtor to prove he was solvent?

MR. BRODSTEIN: The burden is on the trustee to prove the debtor insolvent at the date the mortgage was given.

PRESIDENT BURLINGAME: Then if the title company had accepted an affidavit that the transaction didn't come within the provision of the Bankruptcy Act, wouldn't the title company be protected?

MR. BRODSTEIN: There would be some evidence on the part of the title insurance company to say to the court "We knew nothing except what is in this affidavit." That would be some evidence, but if the bank president and the debtor all stand up and say "We told Jim Schmidt all about this, and he knows all the facts, and in spite of that he went ahead and insured the mortgage," I would say the title insurance company is liable.

PRESIDENT BURLINGAME: Don't be so "nosey."

QUESTION: Back to the question of the sale and the divestitute of the first mortgage, would you say the administration expense would be generally administration expense covering other properties in the conduct of a business, would that all be ahead as far as distribution of the fund is concerned?

MR. BRODSTEIN: No, the actual expenses of the sale in this particular property alone.

In the good old days many years ago, when title men and mortgagees were not quite on their toes as much as nowadays, the courts would often allow all expenses against the first mortgage, but today they don't do it.

QUESTIONER: Isn't the test whether or not the mortgagee objects to the sale?

MR. BRODSTEIN: That is about the best possible test.

1955 NATIONAL ADVERTISING CONTEST, RULES AND REGULATIONS (Revised)

WARREN THOMPSON

Chairman, Committee on Advertising and Publicity, American Title Association
Public Relations Officer, Chicago Title & Trust Company, Chicago, Illinois

(Revised 1955)

1. Advertising to be entered in the contest shall be mounted ready for display **by the member company,** in the following form:

   All material must be attached to uniform cardboard or illustration board panels of standard 30"x40" size. The name of the company must be clearly indicated on the top of each panel. The contest classification (see classifications [a] to [g] below) in which the material falls must also be clearly indicated on each panel. As many panels as desired may be prepared and entered.

   All material should be mounted in the actual size and form in which it was or will be used. Only exception to the use of these 30"x40" panels should be in the instance of such things as window displays, home show displays, or other advertising materials which may be too large or heavy to be thus mounted; such material may be entered as a separate display under a specified classification but must be submitted and displayed in the physical form that it was, or will be, actually used.

2. The only additional information required beyond the designation of contest classification on the panels would be such data, if you consider it necessary, that might help the judges to understand **how** the advertising was used. Such data should be in the form of typewriter copy and should be mounted on the panels adjacent to the advertising itself.

   It is not necessary to supply any data concerning cost, time of advertising, circulation or results, nor is it necessary to indicate whether advertising agency counsel was used.

3. All entries must be shipped **prepaid** to the Statler Hotel, Cleveland, Ohio, marked "Attention of: Carl F. Ferguson, Hold for American Title Association Convention." Ship in time to arrive in Cleveland not later than September 15, 1955.

4. By letter, prior to September 15, 1955, all companies entering the contest must inform Carl F. Ferguson, Lawyers Title Insurance Corporation, 39 Public Square Building, Cleveland 13, Ohio, of the number of panels being shipped as well as approximate shape and size of any other special displays being entered in the contest that will not be mounted on standard panels.

5. Factors considered in making the awards will include content, character, originality, appearance and general effectiveness of the advertising.

   A five-man judging committee will vote on the material submitted and determine the contest winners. The committee will consist of three title men (including the Chairman of the Advertising and Publicity Committee); an advertising art director; and an advertising agency representative.

6. The contest is divided into the following classifications: (A member company may enter one, several, or all classifications.)

   a) **Newspaper and Magazine Advertising:** Either proofs or actual advertisements clipped from the publication may be mounted, but material must be the same size as actually published.

   b) **Direct Mail:** Booklets, pamphlets, series of letters, blotters,

series of other printed messages, etc.

Mount actual copy of booklet or other material in a manner that permits inspection of inside pages.

Indicate adjacent to samples nature of mailing list used—(lawyers, mortgage institutions, etc.)

c) **Publicity:** Mount actual clippings from newspapers or periodicals as published.

d) **Radio and Television:** Use photographs, sample scripts, and adequate typewritten information mounted on the panel to provide the judges with reasonable knowledge of the nature of the program, its frequency, and general objective of radio or television advertising.

e) **House Organ or Company Publication:** Mount at least four issues of each publication so that inside pages can be inspected; indicate whether for employees or external distribution; if external, indicate nature of mailing list.

f) **Posters, Billboards, Window Displays, Signs and Exhibits:** Enter the actual exhibits or displays in the form used, or, if size makes this impractical, mount photographs of the exhibit or displays on the standard panels, with adequate typewritten information mounted on the panel to provide the judges with reasonable knowledge of the nature of the display and the location or event at which it was used.

g) **Miscellaneous Advertising: Novelties**, gifts, calendars, etc. Mount samples on panels, with sufficient information to provide judges with an understanding of how these novelties are used for advertising purposes.

7. PRIZES—Prizes will be awarded at the Annual Banquet of the National Convention. The prizes will be as follows:

A. A Grand Prize for the most effective total advertising program of the year carried on by any abstract, title or title insurance company in the Association. This trophy will be a perpetual trophy and will be held by the winning company through the following year. The company's name will be inscribed on the trophy and the company will also receive a plaque or certificate which it may retain permanently, as evidence of having received the award.

B. Four Capital Prizes, consisting of bronze plaques to be held permanently by the winners, for the best single advertisement or series of advertisements produced during the year, by:

1. An Abstract Company whose county of domicile has a population of not more than 100,000.
2. An Abstract Company whose county of domicile has a population of over 100,000.
3. A Title Insurance Company whose combined capital and surplus total not more than $3,000,000.
4. A Title Insurance Company whose combined capital and surplus total more than $3,000,000.

C. Certificates of Merit will be awarded to Abstract Companies and Title Insurance Companies in each of the four categories specified above which place second and third in the contest for the Capital Prizes.

D. Certificates of Merit will be awarded to the Abstract Companies and Title Insurance Companies in each of the four categories specified above which place first, second and third in the contest classifications described in Section 6 (b) to (g).

8. No panels or other exhibits entered in this contest will be returned unless the member company specifically requests that this be done.

COMING EVENTS

DATE	MEETING	WHERE TO BE HELD
June 10-11	Idaho Title Association	Bannock Hotel Pocatello, Idaho
June 15-18	Oregon Land Title Association	Eugene Hotel Eugene, Oregon
June 19-20-21	Colorado Title Association	Colorado Hotel Glenwood Springs, Colo.
June 23-24-25	Michigan Title Association	Hidden Valley Ski Club Gaylord, Michigan
June 27 28-29	California Land Title Association	Hotel del Coronado Coronado, California
July 8-9	New Mexico Title Association	The Lodge Cloudcroft, New Mexico
Aug. 26-27	Montana Title Association	Yellowstone Nat'l Park
Sept. 2-3-4	Washington Land Title Association	Davenport Hotel Spokane, Washington
Sept. 9-10	North Dakota Title Association	Fargo, North Dakota
Sept. 10-13	New York State Title Association	Lake George Sagamore, New York
Sept. 25-29	National Convention—American Title Association	Statler Hotel Cleveland, Ohio
Oct. 9-10	Kansas Title Association	Allis Hotel Wichita, Kansas
Oct. 13-14-15	Wisconsin Title Association	Northernaire, Wisconsin
Oct. 31-Nov. 1	Missouri Title Asociation	Statler Hotel St. Louis, Missouri
Nov. 6-7-8	Ohio Title Association	Netherland Plaza Cincinnati, Ohio
Nov. 17-18-19	Florida Title Association	Tampa Terrace Hotel, Tampa, Florida

OTHER MEETINGS OF INTEREST

Aug. 22-26	American Bar Association Convention	Bellevue-Stratford Hotel Philadelphia, Pa.
Oct. 31- Nov. 1-2-3	Mortgage Bankers Association of America	Statler Hotel Los Angeles, California