private persons, or to a particular corporation, property or rights in which the whole public is interested, cannot be presumed, unless unequivocally expressed or necessarily to be implied in the terms of the grant, and because the grant is supposed to be made at the solicitation of the grantee, and to be drawn up by him or by his agents, and therefore the words used are to be treated as those of the grantee; and this rule of construction is a wholesome safeguard of the interests of the public against any attempt of the grantee, by the insertion of ambiguous language, to take what could not be obtained in clear and express terms. Charles River Bridge v. Warren Bridge, 11 Pet. 420, 544–548; Dubuque & P. R. R. v. Litchfield, 23 How. 66, 88, 89; Slidell v. Grandjean, 111 U. S. 412, 437, 438, 4 Sup. Ct. 475." Central Transp. Co. v. Pullman's Palace-Car Co., 139 U. S. 24, 49, 11 Sup. Ct. 478, 484.

But in the present case we think that there are no reasonable grounds for doubt. The company's rights are derived only from the town council, and the company has only such rights as the town council could confer.

As we find that the waterworks corporation had no rights which would be impaired by the building of town waterworks, it becomes immaterial to decide the point made by the defendant that the vote of the town council passed April 11, 1895, was not a "law," within the meaning of the constitutional inhibition of state laws impairing the obligation of contracts, though we find strong support for the complainants' contention in the authorities cited upon their briefs. To the claim of the complainants that the charter of the company recognizes and validates its exclusive privilege, we are unable, upon examination of the charter, to give any weight. We agree with and adopt the language of the state court in the Smith-Westerly Case upon this point: "An examination of said charter, however, fails to show any ratification or adoption of said contract, or any reference thereto." What have been termed the "equities" of this case have been presented to us by counsel for the complainants, and the hardship to the company and to the stockholders which will result from a denial of their claims has been urged as a matter relevant to a determination of the legal rights. While we may regard with sympathy the failure of enterprises to meet the expectations of their promoters, we cannot permit such sympathy to cause us to depart from rules of law which impose limitations upon the powers of public officials and municipal corporations. Recognizing the limitations imposed upon corporations and individuals by the national and state constitutions, and by the laws which the people enact through their representatives in the national and state legislatures, it is the duty of the federal courts to support the state courts by a full recognition of their right and duty to maintain in their respective jurisdictions the rights of the public against claims in derogation thereof based upon an uncertain and doubtful construction of acts of the legislature or of agents or officers acting under powers delegated to them by the legislature. In the case of Hamilton Gas-Light & Coke Co. v. Hamilton City, 146 U. S. 258, 13 Sup. Ct. 90, it was strongly argued by counsel, as it has been urged in this case, that not competition, but confiscation, was sought (see pages 263, 264), but the court met such suggestions in the following language:

"The statutes in force when the plaintiff became a corporation did not compel the city to use the gaslight furnished by the plaintiff. The city was empowered to contract with the company for lighting streets, lanes, squares, and public places within its limits, but it was under no legal obligation to make a contract of that character, although it could regulate, by ordinance, the price to be charged for gaslight supplied by the plaintiff and used by the city or its inhabitants. It may be that the stockholders of the plaintiff supposed, at the time it became incorporated, and when they made their original investment, that the city would never do what evidently is contemplated by the ordinance of 1889. And it may be that the erection and maintenance of gas works by the city at the public expense, and in competition with the plaintiff, will ultimately impair, if not destroy, the value of the plaintiff's works for the purposes for which they were established. But such considerations cannot control the determination of the legal rights of the parties. As said by this court in Curtis v. Whitney, 13 Wall. 68, 70: 'Nor does every statute which affects the value of a contract impair its obligation. It is one of the contingencies to which parties look now in making a large class of contracts, that they may be affected in many ways by state and national legislation.' If parties wish to guard against contingencies of that kind, they must do so by such clear and explicit language as will take their contracts out of the established rule that public grants, susceptible of two constructions, must receive the one most favorable to the public."

The court, also, citing the language of Turnpike Co. v. State, 3 Wall. 210, says:

"No exclusive privileges had been conferred upon it, either in express terms or by necessary implication; and hence whatever may have been the general injurious effects and consequences to the company, from the construction and operation of the rival road, they are simply misfortunes which may excite our sympathies, but are not the subject of legal redress."

Our conclusion is fortified by the decision of the supreme court of Rhode Island upon the vital questions existing in the present cases. Giving full weight to the arguments presented by the complainants concerning the status of that case, as a controversy, prearranged to secure a decision for ulterior purposes, we are yet of the opinion that the views of the learned court upon the main questions are free from any influence resulting from that aspect of the case, and are sound interpretations of statute law. Though we reach our conclusion by a somewhat different path, and upon our independent judgment, assisted, though not controlled, by that learned court, yet we fully concur in the findings of law which have led them, as ourselves, to find that the defendant has a complete right to proceed to the construction of waterworks; and we find that in so doing it will impair no right nor obligation of contract to the benefit whereof the complainants are entitled. The preliminary injunctions, therefore, will be dissolved.

NOTE. For previous decision in this case, see Westerly Waterworks v. Town of Westerly, 75 Fed. 181.

CENTRAL TRUST CO. OF NEW YORK v. EAST TENNESSEE, V. & G. R. CO. et al.

(Circuit Court of Appeals, Sixth Circuit. May 4, 1897.)

No. 413.

1. RAILROADS—DIVERSION OF INCOME—LIABILITY OF MORTGAGEES TO REFUND.
Junior mortgage creditors of an insolvent railroad company are not liable to make good a diversion of a portion of the income by the receiver to the payment of interest on prior mortgages.

2. SAME.
The doctrine that income wrongfully applied by a receiver to the payment of interest on mortgages, or the improvement of the property of the corporation, must be restored, cannot be applied where it is impossible to ascertain whether these expenditures have been made out of the income, or out of money borrowed.

3. SAME—APPLICATION OF INCOME TO PAYMENT OF PRE-EXISTING DEBTS.
Pre-existing debts of a railroad company for necessary operating expenses will not be a first charge on the income of a receivership, unless contracted within a reasonable period prior to the appointment of the receiver. The determinaton of this period is in the sound discretion of the court having jurisdiction of the accounts; and a limitation of six months, so imposed, will not be disturbed on appeal.

4. SAME—CLAIM FOR ADVERTISING MATTER.
A claim for advertising matter furnished to a railroad company prior to the appointment of a receiver is not entitled to rank as a debt for materials necessary to the operation of the road.

Appeals of W. B. Belknap & Co., E. A. Kinsey & Co., Matthews, Northrup & Co., and Westinghouse Air-Brake Co., Parties by Intervention, from the Circuit Court of the United States for the Eastern District of Tennessee.

This is an appeal, by the several interveners mentioned above, from a decree of the circuit court refusing to allow payment of their several claims out of the corpus of the property of the railroad company in preference to the mortgages foreclosed in the principal case. The East Tennessee, Virginia & Georgia Railroad Company is an insolvent railroad corporation, whose entire property was originally placed in the hands of receivers, June 24, 1892, under a bill filed in the circuit court by Samuel Thomas, who was a large general creditor. Subsequently two foreclosure bills were filed in the same court for the purpose of foreclosing two junior mortgages, subject to the lien of certain other and senior mortgages. The original receivership was extended to these foreclosure suits, and the three causes consolidated under the style of the Central Trust Company of New York against the East Tennessee, Virginia & Georgia Railroad Company et al. Under the final decree of foreclosure the railroad and all of its properties and appurtenances have been sold, subject to certain underlying mortgages, and were purchased by the Southern Railway Company. The income of the several receiverships has been exhausted in the payment of operating expenses, preferential claims, and interest upon underlying mortgages, paid to prevent default and premature maturity of the debts thereby secured. The proceeds of the foreclosure sale were insufficient to pay off the mortgage debts, and have been applied towards the payment of the bonds secured by the foreclosed mortgages; but the purchaser, by the terms of the decree of sale, is obligated to pay, in addition to its bid, all such other amounts as shall be necessary to pay off and discharge such claims against the receivers, or against the railroad company, as shall be determined to be entitled to preference over the foreclosed mortgages. The appellants are creditors of the railroad company, who by intervention have asserted claims for materials and supplies furnished to the railroad company before the appointment of the receivers, but who have been denied preference over the mortgagees in payment. Their

claims to priority are asserted—First, because they say their accounts are for materials and supplies used in the operation of the said railroad, and furnished within a short time prior to the appointment of receivers; second, they assert that the net earnings of the railroad company were not applied to the payment of the income debts, but were diverted to the payment of interest upon mortgage debts, and in the improvement of the mortgaged property. For this reason they insist that they are entitled to be paid out of the corpus of the mortgaged property to the extent of such diversion of income. The circuit court refused priority to the claims preferred by W. B. Belknap & Co., E. A. Kinsey & Co., and the Westinghouse Air-Brake Company, upon the ground that their several claims were not for materials and supplies furnished within the time prescribed by the order appointing the receivers. The claim of Matthews, Northrup & Co. was for advertising matter. This claim was rejected by the court below upon the ground that such advertising matter was not a claim of the class entitled to preference. So far as these claims were asserted upon the ground of a diversion of income to the payment of interest, or in improving the mortgaged property, the report of the special commissioner that there had been no such diversion was concurred in by the court.

W. C. Herron, for appellants.

Henry Hudson, for appellee.

Before TAFT and LURTON, Circuit Judges, and SEVERENS, District Judge.

LURTON, Circuit Judge, after making the foregoing statement of facts, delivered the opinion of the court.

The question as to whether there was a diversion of the current income by the railroad company to the payment of interest on the foreclosed mortgage debts, or in the permanent improvement of the mortgaged property, was principally one of fact, and was referred to a special commissioner, who reported that there had been no such diversion. The exceptions to this finding were considered by the court below, and overruled. We think it was not error to exclude from consideration income applied to the payment of interest on the senior mortgages. The junior mortgagees did not receive the income so paid, even if it was technically a diversion, and cannot be called on to reimburse the fund applicable to the payment of the debts of the income for such diversion. St. Louis, A. & T. H. R. Co. v. Cleveland, C. C. & I. Ry. Co., 125 U. S. 658, 8 Sup. Ct. 1011. This doctrine of a diversion of income, and the liability of mortgagees to restore the income thus diverted, was first formulated in Fosdick v. Schall, 99 U. S. 235. Speaking of the ground upon which the mortgagees may be postponed in favor of creditors who had a right to look to the application of current income in payment of their debts, Chief Justice Waite, at page 254, said:

"Whatever is done, therefore, must be with a view to a restoration by the mortgage creditors of that which they have thus inequitably obtained. It follows, therefore, that, if there has been in reality no diversion, there can be no restoration, and that the amount of the restoration should be made to depend upon the amount of the diversion."

During the period of time covered by the purchase of the materials and supplies embraced in the several claims of appellants, the net earnings were probably insufficient to justify the payment of interest on the foreclosed mortgage debts, and to make certain

improvements shown to have been made during that time. But it is also shown that, during the same period, money was borrowed on open account, more than sufficient to equal the diversion complained of, which went into a common treasury, from which operating expenses, preferential claims, interest, and improvements were paid, without any definite showing as to whether the borrowed money was applied to the payment of interest and improvements, or to current income debts. Under this system of bookkeeping, the addition of borrowed money to the income arising from operation showed a substantial surplus after payment of the great mass of income debts, and all disbursements on account of interest upon the two mortgages foreclosed, as well as upon improvements in the roadway. Prior to the period covered by the maturity of appellants' claims, there was a surplus of gross earnings over all operating expenses; but it cannot be contended that the company was under any obligation to future creditors to accumulate a surplus to meet possible deficiencies in the income to meet future income debts, or that it was improper to apply such surplus in payment of interest. St. Louis, A. & T. H. R. Co. v. Cleveland, C. C. & I. Ry. Co., 125 U. S. 658–675, 8 Sup. Ct. 1011. Whatever diversion there may have been of income to payment of debts or liabilities, not properly debts of the income, seems to have been more than reimbursed by the money borrowed. The burden is upon complainants to show that there has been a misappropriation of earnings to the improvement of the mortgaged property, or to the payment of interest, before the mortgagees can be justly called upon to reimburse the fund applicable to debts of the income in consequence of such diversion. If interest was paid or improvements made out of borrowed money, then there was no diversion; or if made out of gross earnings, and the latter was reimbursed by borrowed money, the diversion was made good. The abstracts showing income from all sources and disbursements upon all accounts are somewhat complicated, in consequence of the mode of bookkeeping adopted. The commissioner and court below concurred in reporting that there was no diversion shown. In the absence of very cogent evidence of mistake of fact, or of some error of law, the finding of fact by the commissioner must be accepted as final. Emil Kiewert Co. v. Juneau, 24 C. C. A. 294, 78 Fed. 708; Kimberly v. Arms, 129 U. S. 512–524, 9 Sup. Ct. 355; Tilghman v. Proctor, 125 U. S. 136, 8 Sup. Ct. 894; Turley v. Turley, 85 Tenn. 256, 1 S. W. 891. But, independently of any diversion of current income, there is a class of debts, incurred in maintaining the operation of a railway, which, under special circumstances, and subject to very positive limitations, has been held to outrank, in priority of payment, contract liens. In Miltenberger v. Railway Co., 106 U. S. 286–311, 1 Sup. Ct. 140, 162, it appeared that the receiver had claimed credit for certain claims paid by him for materials and supplies furnished and purchased before his appointment by the railroad company, upon the ground that "the creditors threatened not to furnish any more supplies on credit unless they were paid the arrears." The payments were allowed, the court saying:

"It cannot be affirmed that no items which accrued before the appointment of a receiver can be allowed in any case. Many circumstances may exist which make it necessary, and indispensable to the business of the road and the preservation of the property, for the receiver to pay pre-existing debts, of certain classes, out of the earnings of the receivership, or even the corpus of the property, under the order of the court, with a priority of lien. Yet the discretion to do so should be exercised with very great care. The payment of such debts stands, prima facie, on a different basis from the payment of claims arising under the receivership, while it may be brought within the principle of the latter by special circumstances. It is easy to see that the payment of unpaid debts for operating expenses, accrued within ninety days, due by a railroad company suddenly deprived of the control of its property, due to operatives in its employ, whose cessation from work simultaneously is to be deprecated, in the interest both of the property and of the public, and the payment of limited amounts due to other and connecting lines of road for materials and repairs, and for unpaid ticket and freight balances, the outcome of indispensable business relations, where a stoppage of the continuance of such business relations would be a probable result in case of nonpayment,—the general consequence involving largely, also, the interests and accommodation of travel and traffic,—may well place such payments in the category of payments to preserve the mortgaged property, in a large sense, by maintaining the good will and integrity of the enterprise, and entitle them to be made a first lien."

In Burnham v. Bowen, 111 U. S. 776–781, 4 Sup. Ct. 675, it appeared that there had been no diversion of income, and that an arrearage of debt for materials and supplies was due to the insufficiency of the income to pay necessary operating expenses. The court allowed the claim out of the income earned by the receivers, upon the ground that it "was incurred to keep the road running, and thus preserve the security of the bond creditors." "Under these circumstances," said the court, "we think the debt was a charge, in equity, on the continuing income,—as well that which came into the hands of the court after the receiver was appointed as that before. When, therefore, the court took the earnings of the receivership, and applied them to the payment of the fixed charges on the railroad structures, thus increasing the security of the bondholders at the expense of the labor and supply creditors, there was such a diversion of what is denominated in Fosdick v. Schall the 'current debt fund' as to make it proper to require the mortgagees to pay back. So far as current expense creditors are concerned, the court should use the income of the receivership in the way the company would have been bound in equity and good conscience to use it if no change in the possession had been made. This rule is in strict accordance with the decision in Fosdick v. Schall, which we see no reason to modify in any particular." The liberality with which this equity was extended by some of the circuit courts in favor of general creditors induced the supreme court, in Kneeland v. Trust Co., 136 U. S. 89–97, 10 Sup. Ct. 950, 953, to call attention to the necessity of preserving the general priority of contract liens over all but a limited class of claims. Through Mr. Justice Brewer, the court said:

"The appointment of a receiver vests in the court no absolute control over the property, and no general authority to displace vested contract liens. Because, in a few specified and limited cases, this court has declared that unsecured claims were entitled to priority over mortgage debts, an idea seems to have obtained that a court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a

court appointing a receiver could rightfully burden the mortgaged property for the payment of any unsecured indebtedness. Indeed, we are advised that some courts have made the appointment of a receiver conditional upon the payment of all unsecured indebtedness in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect of the court respect for his vested and contracted priority as the holder of a mortgage on a farm or lot. So, when a court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which by the rulings of this court have been declared to have an equitable priority. No one is bound to sell to a railroad company, or to work for it; and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility, and not in expectation of subsequently displacing the priority of the mortgage liens. It is the exception, and not the rule, that such priority of liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens. St. Louis, A. & T. H. R. Co. v. Cleveland, C., C. & I. Ry. Co., 125 U. S. 658, 673, 8 Sup. Ct. 1011, 1017."

In the subsequent case of Thomas v. Car Co., 149 U. S. 95–117, 13 Sup. Ct. 824, 831, the observations touching the sacredness of contract obligations which we have quoted from Kneeland v. Trust Co. were reaffirmed, and a claim for rental of cars was disallowed as a preferential debt, the court saying:

"The case of a corporation for the manufacture and sale of cars, dealing with a railroad company whose road is subject to a mortgage securing outstanding bonds, is very different from that of workmen and employés, or of those who furnish, from day to day, supplies necessary for the maintenance of the road. Such a company must be regarded as contracting upon the responsibility of the railroad company, and not in reliance upon the interposition of a court of equity."

From these cases it may be deduced that in respect of railroad mortgages there is an implied agreement that all proper operating expenses of such companies, while under control of the mortgagors, are to be paid out of current receipts, and that any diversion of such income by which current operating expenses are left unpaid is a misappropriation of the income, and upon a proper showing the mortgagees receiving the benefit will be required to reimburse the fund applicable to the payment of these "debts of the income," to the extent of the diversion. It may further be deduced that, independently of any diversion, the necessary operating expenses of a mortgaged railroad, constituting a first charge upon the income while under the control of the mortgagor, will continue to be a charge upon the income under a receivership, and, if necessary, upon the corpus of the property. This latter equity is supposed to arise from the nature of the public duties resting upon such companies, and upon the necessity of such expenditures in preserving the property as a going concern for the ultimate benefit of the mortgage creditors. The debts entitled to displace contract liens must, in the nature of this latter-mentioned equity, be such as were incurred in the necessary operating expenses, and constitute but a limited class, fairly defined by the cases we have cited. Debts of this class must be such as were created shortly before the

receivership, and contracted under circumstances reasonably indicating a reliance upon a proper application of the current income to their payment. In the case of Bound v. Railway Co., 8 U. S. App. 461, 7 C. C. A. 322, and 58 Fed. 473, such a creditor was held to have impliedly waived his right to look to the income earned pending an agreed credit of eight months, with privilege of renewal. The supreme court has not definitely laid down any limit within which such debts must have been created to entitle them to outrank mortgage liens in payment. In the case of Miltenberger v. Railway Co., elsewhere cited, a limit of 90 days was adopted, while in the cases of Trust Co. v. Souther, 107 U. S. 591, 2 Sup. Ct. 295, and United States Trust Co. v. Wabash W. Ry. Co., 150 U. S. 287, 14 Sup. Ct. 86, a limit of 6 months was not disapproved. In other cases, under special circumstances, claims originating more than 6 months prior to the receivership have been allowed priority. Hale v. Frost, 99 U. S. 389; Burnham v. Bowen, 111 U. S. 776, 4 Sup. Ct. 675. It is to be observed that in neither of these latter-mentioned cases was there any general order touching the payment of such claims. The practice upon the circuits has varied in this matter of a time limit upon these preferential claims, and the circuit courts of appeals have shown no unanimity in fixing upon such a limitation. In the Fourth circuit it has been ruled that they must have been incurred within a "reasonable time" before the appointment of a receiver, and a claim was allowed priority under a very peculiar receivership, which was created from 9 to 11 months before. It must be admitted that the rule of "a reasonable time" furnishes no sure guide, and leaves the whole matter open to the discretion of the court. The same court, in Boston Safe-Deposit & Trust Co. v. Richmond & D. R. Co., 8 U. S. App. 547, 10 C. C. A. 323, and 62 Fed. 205, adopted a limitation of 90 days, in an opinion by Chief Justice Fuller. In Railroad Co. v. Lamont, 32 U. S. App. 480, 16 C. C. A. 364, and 69 Fed. 23, the court of appeals for the Eighth circuit held the time limit no bar, and allowed a claim which in part originated some three years before the receivership. In the Seventh circuit, we have the authority of Mr. Justice Harlan for saying that a limitation of six months has been regarded as a proper limitation upon such claims. The precise grounds upon which such a rule rests are so well stated by the learned justice that we quote and adopt his reasoning, as reported in Thomas v. Railroad Co., 36 Fed. 808. The justice, on this subject, said:

"The general rule that has obtained in this circuit for many years, though not fully or expressly formulated in any published decision, has been not to charge the income of mortgaged property accruing during a receivership, or the proceeds of sale of such property, with general debts for labor, supplies, and equipment, back of the six months immediately preceding the appointment of a receiver. While the court has not, perhaps, committed itself against applying a different and more liberal rule when the special circumstances or equities of the case demand such a course, the general rule is as just stated; and I am unwilling, in this case, and at this late day, to depart from it. Besides, I am of opinion that, under the circumstances that usually attend the administration of railroad property by the courts through receivers, the rule stated is a wise and salutary one. It would not do to charge the income of