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to preserve uniformity by the force of example."[61] Thus a decision to reject the state law as the federal rule induces confusion regarding the primary rules of conduct in two ways: first, by posing two laws on the same subject and raising doubts about the viability of other state rules; and second, by injecting imprecision through hurried opinions and conflicting decisions among the circuits.

When, as in *Stadium Apartments*, a court chooses to reject the state law as the federal rule, it should face squarely the impact of that decision on the certainty and clarity of its guides to future conduct, especially in an area such as the law of property where the state law is widely presumed to apply and in fact is applied to govern the relations of the parties. The local rule should be rejected only when a sufficient federal interest warrants intrusion into the traditional ambit of the local guides to conduct and the resulting confusion for those who rely on them to plan their future transactions is justified. In *Stadium Apartments* the consequences to the federal system were not confronted directly nor was there an adequate showing of the requisite federal interest to warrant the result obtained.

KENNETH C. DAY

Federal Jurisdiction—Derivative Jurisdiction Upon Removal

"[P]rompt, economical, and sound administration of justice depends upon definite and finally accepted principles governing important areas of litigation, such as the respective jurisdictions of federal and state courts . . . ."[1] One such principle is derivative jurisdiction in the removal area; title 28, United States Code, section 1441[2] allows removal at de-

[61] Friendly, *supra* note 9, at 405. *See also* Mishkin, *The Federal "Question" in the District Courts*, 53 COLUM. L. REV. 157, 158 (1953).

[1] American Fire and Cas. Co. v. Finn, 341 U.S. 6, 8 (1951). Defendant, who had removed on grounds of diversity, lost on the merits in federal court. On appeal he asked that the case be remanded because of jurisdictional shortcomings, and the Court in an opinion written by Justice Reed granted his request, feeling that the ends of justice would be better served through strict enforcement of jurisdictional requirements.

[2] The text of 28 U.S.C. § 1441 (1964) concerns actions removable generally:

(a) Except as otherwise expressly provided by Act of Congress, any civil action brought in a State court of which the district courts of the United States have original jurisdiction, may be removed by the defendant . . . to the district court of the United States for the district and division embracing the place where such action is pending.

(b) Any civil action of which the district courts have original jurisdiction founded on a claim or right arising under the Constitution, treaties or laws

fendant's urging of any case from state court into federal court, provided that the federal court had original jurisdiction.[3] However, the federal court also inquires into the jurisdiction of the court from which the case is removed. When jurisdiction is concurrent, Congress may have designated certain types of state courts as the only appropriate state forums, and thus the federal court's inquiry will focus on this conformity.[4] When jurisdiction is exclusively federal, the court must look to the subject matter of the action to determine whether it is within the realm of the exclusive jurisdiction, in which event no state court would be a proper forum. In any case, the jurisdiction of the federal court upon removal is derivative in nature.[5]

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of the United States shall be removable without regard to the citizenship or residence of the parties. Any other such action shall be removable only if none of the parties in interest properly joined and served as defendants is a citizen of the State in which such action is brought.

(c) Whenever a separate and independent claim or cause of action, which would be removable if sued upon alone, is joined with one or more otherwise non-removable claims or causes of action, the entire case may be removed and the district court may determine all issues therein, or, in its discretion, may remand all matters not otherwise within its original jurisdiction.

[3] Jurisdiction normally breaks down into two areas, jurisdiction over person and jurisdiction over subject matter. Of the two, jurisdiction over subject matter is the more important and is the topic of the text. Jurisdiction over person may be waived either explicitly or implicitly by the parties, but jurisdiction over subject matter cannot be. The federal courts strive not to let technical imperfections in service of process interfere with hearing the case on the merits. See FED. R. CIV. P. 4(h). On the other hand a federal court will take cognizance of a lack of subject matter jurisdiction on its own motion and will dismiss the case. Louisville & N.R.R. v. Mottley, 211 U.S. 149, 152 (1908).

[4] *E.g.*, Beckman v. Graves, 360 F.2d 148 (10th Cir. 1966). A farmer commenced action in a Kansas county court to review the wheat marketing quota imposed on him by his local committee pursuant to the Agricultural Adjustment Act of 1938. Defendant agricultural agent removed to federal district court where the action was dismissed for lack of jurisdiction. Such action would have been properly brought if filed in any state court having *general jurisdiction*, but in Kansas the state district courts are courts of general jurisdiction while the county courts are courts of limited jurisdiction. Since the action was instituted in the improper state court, the circuit court affirmed the dismissal.

[5] Lambert Run Coal Co. v. Baltimore & O.R.R., 258 U.S. 377 (1922); *accord*, Freeman v. Bee Machine Co., 319 U.S. 448 (1943). The theory of derivative jurisdiction is not limited solely to the federal removal area. It has been applied in state systems of justice, which rely on a dual judiciary. For instance, formerly in North Carolina, justice of the peace courts had concurrent jurisdiction with superior court on claims of less than $200. Appeal from the justice's court was to the superior court and invoked a trial de novo. Even though the superior court had original jurisdiction, the appeal would be dismissed if the justice of the peace court had no jurisdiction since jurisdiction was entirely derivative. Hopkins v. Barnhardt, 223 N.C. 617, 27 S.E.2d 732 (1943). The recent reorganization of the courts, resulting in a unitary system, should eradicate the doctrine in North Carolina. N.C. GEN. STAT. § 7A-4 (1969).

Leesona Corp. v. Concordia Manufacturing Co.[6] is a recent federal district court case illustrative of this doctrine. Leesona owned patents which it licensed to certain manufacturers. One of the licensees, Kayser-Roth Corporation, became concerned about the validity of the patents and defaulted on a royalty payment. Prior experience had revealed to Leesona that when one licensee defaulted on payments the remaining licensees discontinued payments also, pending settlement of the initial dispute. Accordingly Leesona waged simultaneous suits in the Rhode Island courts with Kayser-Roth to recover damages for contract violation, and with some sixty other licensees to determine the rights of the parties in order to prevent default on payments. Leesona took a voluntary dismissal as to the contracts action and then added Kayser-Roth as a defendant to the second suit for construction of the contracts and declaration as to the validity of the patents. The defendants removed to federal district court in Rhode Island, and there offered five grounds for dismissal, one of which was lack of subject matter jurisdiction. The defendants argued that since suits concerning patent validity are to be tried exclusively in the federal courts,[7] the state court did not have original jurisdiction over the suit; thus the federal court acquired none on removal. The court ruled that indeed this was a suit designed primarily to test patent validity, not one merely construing licensing agreements, and granted the motions to dismiss.[8]

Leesona sharply outlines the paradox inherent in the derivative jurisdiction doctrine. When jurisdiction over a particular suit is *exclusively* vested in the federal courts,[9] and the suit is filed in a state court and then removed, the federal court will not entertain the cause of action for lack of jurisdiction. Since dismissal is without prejudice, the plaintiff may return the next day and file his suit in the court that had previously dismissed it.[10] The aim of this note is to explore the origin and development of the doctrine and to assess the utility of its application in this context.

The earliest indication of the doctrine's existence appears in a rarely

[6] 312 F. Supp. 392 (D.R.I. 1970).
[7] 28 U.S.C. § 1338 (1964).
[8] 312 F. Supp. at 397.
[9] Some of the areas of exclusive jurisdiction are the following: admiralty and maritime jurisdiction; bankruptcy proceedings; copyright cases; and special areas such as litigation of ICC orders, federal antitrust actions, and federal tort claims. See C. WRIGHT, LAW OF FEDERAL COURTS § 10 (2d ed. 1970).
[10] For possible statute of limitations problems which plaintiff might encounter see pp. 372-73 and notes 26-29 *infra*.

cited dictum of *Martin v. Hunter's Lessee*[11] stating that the power of removal is not strictly an exercise of original jurisdiction, but presupposes that original jurisdiction has attached in the state court.[12] Aside from this rather dubious beginning there are two other recognizable sources of the doctrine. One is in a technical reading of the removal statute—more specifically the interpretation of the word "suit,"[13] which appeared in place of the term "civil action"[14] in earlier versions of the statute. Simply put, a controversy is not a suit unless it is instituted in a court of competent jurisdiciton. Hence a controversy being litigated in a state court having improper jurisdiction never attains the status of a suit—a status necessary if the requirements of the removal statute are to be met.[15] Another source frames itself in this obvious tautology: Any defense available in the state court is available in the federal court after removal; the rights of the parties are not changed by removal.[16] In logical pursuit of this concept, any claim of improper jurisdiction of the state court may be revived after removal.

The Supreme Court in two 1922 opinions carefully defined the derivative jurisdiction of the federal courts upon removal.[17] Preceding

[11] 14 U.S. (1 Wheat.) 304 (1816).

[12] This power of removal is not to be found in express terms in any part of the constitution; if it be given, it is only given by implication, as a power necessary and proper to carry into effect some express power. The power of removal is certainly not, in strictness of language [an exercise of original jurisdiction]; it presupposes an exercise of original jurisdiction to have attached elsewhere.

Id. at 349 (the bracketed portion does not appear in the United States Reports but does appear in 4 L. Ed. 97, 108 (1816)).

[13] *E.g.*, the Judiciary Act of March 3, 1887, ch. 373, § 2, 24 Stat. 553:

any *suit* of a civil nature . . . of which the circuit courts of the United States are given original jurisdiction, which now may be pending, or which may hereafter be brought, in any State court, may be removed by the defendant . . . to the circuit court of the United States for the proper district. (emphasis added)

[14] 28 U.S.C. § 1441 (1964), the text of which appears in note 2 *supra*.

[15] Upshur County v. Rich, 135 U.S. 467 (1890); Fidelity Trust Co. v. Gill Car Co., 25 F. 737 (C.C.S.D. Ohio 1885).

[16] *Compare* Davis v. Gray, 83 U.S. (16 Wall.) 203 (1872) *with* Wabash W. Ry. v. Brow, 164 U.S. 271 (1896) *and* Cain v. Commercial Publishing Co., 232 U.S. 124 (1914). Possibly the earliest indication of availability of all state defenses was in Gier v. Gregg, 10 F. Cas. 339 (No. 5406) (C.C.D. Ill. 1847): "The case, when removed from the state court to the circuit court of the United States, stands in the latter court as it stood in the former, before the removal." *Id.*

[17] The doctrine was already established in the lower courts. R.J. Darnell, Inc. v. Illinois Cent. R.R., 190 F. 656 (C.C.W.D. Tenn. 1911). *See* Sheldon v. Wabash R.R., 105 F. 785 (C.C.N.D. Ill. 1900); Auracher v. Omaha & St. L.R.R., 102 F. 1 (C.C.S.D. Iowa 1900); Swift v. Philadelphia & R.R.R., 58 F. 858 (C.C.N.D. Ill. 1893).

decisions had indicated the way,[18] but *Lambert Run Coal Co. v. Baltimore & Ohio Railroad*[19] and *General Investment Co. v. Lake Shore & Michigan Southern Railway*[20] firmly established the doctrine. In *Lambert* the plaintiff coal company filed suit in the state court to enjoin the railroad from following certain rules of railroad car distribution prescribed by the Interstate Commerce Commission. The defendant removed to federal district court which granted the injunction. The Supreme Court affirmed the circuit court's reversal of this decision and noted that the suit should have been dismissed for want of jurisdiction, since review of ICC orders is to occur exclusively in the federal courts.[21] The plaintiff in *General Investment* sought to enjoin the merger of defendant railroads on the grounds that such merger violated the Sherman and Clayton Antitrust Acts. The defendants removed from the state court into federal district court and asked for dismissal for lack of jurisdiction. The Supreme Court ruled that the suit was properly dismissed.[22] Again Congress had provided exclusive jurisdiction for federal courts over private suits filed under these antitrust acts.[23]

In both *Lambert* and *General Investment* the federal court could have properly entertained the actions if they had originally been brought there. Since they had arrived via removal they were treated to the peculiar twist exerted by the derivative jurisdiction doctrine—dismissal. The stance of the Supreme Court has remained unchanged on this problem,[24] and the unswerving dedication of the lower federal courts[25] to the precedent established in *Lambert* and *General Investment* indicates their reluctance to depart judicially from the doctrine.

The primary justification for retention of the doctrine in its strictest application is that it is a definite and accepted principle helping to define the important area of subject matter jurisdiction. Thus it gives incentive

[18] American Well Works Co. v. Layne & Bowler Co., 241 U.S. 257 (1916); DeLima v. Bidwell, 182 U.S. 1 (1901).

[19] 258 U.S. 377 (1922).

[20] 260 U.S. 261 (1922).

[21] Act of Oct. 22, 1913, ch. 32, 38 Stat. 219, currently embodied in 28 U.S.C. § 2321 (1964).

[22] 260 U.S. at 288: "When a cause is removed from a state court into a federal court the latter takes it as it stood in the former. A want of jurisdiction in the state court is not cured by the removal, but may be asserted after it is consummated."

[23] *See* Clayton Act, Act of Oct. 15, 1914, ch. 323, § 4, 38 Stat. 731, currently embodied in 15 U.S.C. § 15 (1964).

[24] *See* Freeman v. Bee Machine Co., 319 U.S. 448 (1943); Minnesota v. United States, 305 U.S. 382 (1939).

[25] Martinez v. Seaton, 285 F.2d 587 (10th Cir. 1961); Keay v. Eastern Air Lines, Inc., 267 F. Supp. 77 (D. Mass. 1967).

to plaintiffs' lawyers to file their complaints in the proper forum initially. Yet in the early stages of a suit the issues may not be in sharp focus, and it is often difficult for the lawyer to select the proper court. In *Leesona* the plaintiff wanted its large number of licensees to continue to abide by the contracts, which in turn depended on the validity of the patents. In order to file suit in the proper forum, Leesona's lawyer had to decide whether the action sounded in contract or in patent law. Since he was mistaken in his choice, the case was dismissed despite its subsequent removal into the correct forum. There are harsher blows than dismissal without prejudice, but such a ruling is nonetheless costly to the plaintiff whose lawyer has expended considerable time and effort in futile argument.

If the plaintiff wishes to reinstitute proceedings in federal court, he immediately encounters a possible statute of limitations problem. Although 28 U.S.C. § 1446(e) (1964) provides that after removal the state court "shall proceed no further unless and until the case is remanded" and thus presumably[26] tolls any statute of limitations where the state courts are concerned,[27] it does not follow that this has effect where jurisdiction is exclusively federal. In this case the federal cause of action is governed by a federal statute of limitations, either specified by Congress or incorporated into federal law from state law as a matter of policy.[28] Since a dismissal for lack of subject matter jurisdiction would seemingly designate all proceedings thus far a nullity, then the appropriate statute of limitations would not have been tolled,[29] and if the time limit has run before the

[26] This presumption arises because plaintiff is prevented from renewing his efforts in the state court, notwithstanding that he intends to proceed in a correct manner, until the federal court remands or dismisses. Thus, in State Hwy & Pub. Works Comm'n v. Diamond S.S. Transp. Corp., 226 N.C. 371, 378-79, 38 S.E.2d 214, 219 (1946), where plaintiff was enjoined by federal court from proceeding except in that jurisdiction and later had his suit dismissed for lack of subject matter jurisdiction, he was not barred by the statute of limitations from now proceeding in state court. A federal statute enjoining proceedings in the state court would seem to have equal if not greater weight than a court order.

[27] Thus in the fact situation of Beckman v. Graves, 360 F.2d 148 (10th Cir. 1966), plaintiff could return to a state court of general jurisdiction in Kansas, confident that in the interval between removal and eventual dismissal in federal court the statute was tolled.

[28] See 2 J. MOORE, FEDERAL PRACTICE ¶ 3.07[2] (1970).

[29] Black v. City Nat'l Bank & Trust Co., 321 S.W.2d 477, 479 (Mo.), *cert. denied*, 360 U.S. 920 (1959). This would not necessarily be true if the appropriate statute of limitations has a "saving" clause whcih extends the time period in the event that plaintiff's complaint is dismissed or nonsuited before receiving a hearing on the merits. Factor v. Carson, Pirie Scott & Co., 393 F.2d 141 (7th Cir. 1968); Lowry v. International Bhd. of Boilermakers, 220 F.2d 546 (5th Cir. 1955); Johnson v. United States, 68 F.2d 588 (9th Cir. 1934). A recent decision has held a statute of

plaintiff refiles, his cause of action could very easily have been cut off by the statute.

Assuming that the statute of limitations has not run, then a new complaint must be drawn and filed with the accompanying lost office time and recurring annoyances such as filing fees[30] and service of process. In *Leesona*, though an extreme example, there were some sixty defendants who would have to be reached through methods of process available in Rhode Island, entailing several hundred dollars in cost. The defendants, while victorious in the tactical maneuvering, have won only a Pyrrhic victory if the statute has not run and the plaintiff refiles since they face corresponding expenses.

After refiling, the suit most likely will be placed towards the rear of the court calendar. This delay when coupled with the loss of time caused by removal, the dismissal arguments, and any wait plaintiff might have taken before refiling means that a substantial period of time will have passed before the merits of the controversy are reached. As a consequence, evidence may be lost and witnesses may leave the jurisdiction or even die. Furthermore it is axiomatic that an extended lapse of time decreases the trustworthiness of oral testimony. The real danger is that the case will become so stale that the true merits are never discovered adding credence to Gladstone's maxim that "justice delayed is justice denied."[31]

The federal court system also has an interest in the refiling of a suit after dismissal; the courts are over-burdened with litigation, and court time is at a premium. A significant contribution to efficiency in the federal district courts was made by the implementation of the Federal Rules of Civil Procedure. Promulgated by the Supreme Court, the rules are to be construed "to secure the just, speedy, and inexpensive determination of every action."[32] In view of this objective a contradiction bordering on the absurd exists in a federal system of justice which so rigidly adheres to the doctrine of derivative jurisdiction. For a plaintiff who pursues his claim, the likelihood is that the final determination will have been anything but just, speedy, and inexpensive.

Conflict has occurred at least once between the policies underlying the

limitations tolled where federal court had jurisdiction but dismissed on grounds of improper venue. Burnett v. New York Cent. R.R., 380 U.S. 424 (1965).

[30] The filing fee for civil actions in the federal district courts in North Carolina is fifteen dollars.

[31] As quoted in France, *Judicial Reorganization—A Solution to Congestion*, 68 DICK. L. REV. 143 (1964).

[32] FED. R. CIV. P. 1.

new rules and those behind derivative jurisdiction. In *Freeman v. Bee Machine Co.*[33] the defendant removed a breach of contract action into federal district court. The plaintiff promptly moved to amend in order to add a Clayton Act claim for treble damages over which the federal courts have exclusive jurisdiction. Based on the theory of derivative jurisdiction, district courts had not previously allowed such joinder,[34] and the plaintiff's motion was accordingly denied. The circuit court reversed, and the Supreme Court affirmed on the ground that Congress had provided that a properly removed suit should be treated as though it had been originally commenced in district court.[35] Thus the federal rules controlled, notwithstanding that such amendment would not have been allowed in the state court.[36] This approach is an effective circumvention of the principle of derivative jurisdiction in the interests of judicial economy—the policy underpinning the liberal joinder of claims.

Freeman marks the limits of progress made by the courts in undercutting the derivative jurisdiction doctrine. In view of this judicial reluctance, the American Law Institute has proposed the abolition of the doctrine through act of Congress.[37] Under the ALI provisions, a suit within the exclusive jurisdiction of the federal courts, mistakenly commenced in the state courts, will not be dismissed upon removal for want of jurisdiction but will be retained as having been properly removed.[38] Presumably, under these proposals speculation on the impact of a federal statute of limitations would become moot since the plaintiff is spared the unnecessary act of refiling.

In a dual judicial system, uncertainty in the area of original and concurrent jurisdiction will persist. Yet when the plaintiff in good faith selects a state court and the defendant removes, for the federal court to dismiss on the ground that it is the court of original jurisdiction is to exalt form over substance. Among commentators who have addressed themselves to the problem, Professors Moore[39] and Wright[40] have expressed distaste for this peculiar application of the doctrine. A correction certainly

[33] 319 U.S. 448 (1943).
[34] Carroll v. Warner Bros. Pictures, Inc., 20 F. Supp. 405, 408 (S.D.N.Y. 1937).
[35] Act of Mar. 3, 1911, ch. 231, § 38, 36 Stat. 1098.
[36] 319 U.S. at 452.
[37] ALI STUDY OF THE DIVISION OF JURISDICTION BETWEEN STATE AND FEDERAL COURTS §§ 1312(d), 1317(b), & 1382(e) (1969).
[38] *Id.* Commentary to § 1312(d), at 206-207.
[39] 1A J. MOORE, FEDERAL PRACTICE ¶ 0.157(3), at 86 (1965).
[40] WRIGHT, note 8 *supra*, at § 38.

is in order, whether it be through judicial reconstruction of the removal statute with an eye toward policy considerations prominent in this day, or through act of Congress.

JOHN WOODWARD DEES

Income Taxation—Nondeductibility of Appraisal Litigation Expenses

In two recent decisions, the United States Supreme Court ruled that litigation expenses incurred by either individual stockholders[1] or a corporation[2] in a statutory appraisal proceeding to value shares of dissenting shareholders were not deductible as nonbusiness[3] or business[4] expenses. The holdings in *Woodward v. Commissioner*[5] and *United States v. Hilton Hotels Corp.*[6] resolved conflicting results reached earlier by the eighth[7] and seventh[8] circuits in essentially similar fact situations. The disallowance of the claimed deductions in these cases may have significant impact upon future corporate decisions regarding proposed alterations of their corporate structures when there is a substantial likelihood of appraisal proceedings being instituted. Moreover, the character of the appraisal remedy itself as a protective device for the interests of dissenting shareholders may be affected by the decisions.

In *Woodward*, taxpayers owning a majority of stock in a publishing firm voted to extend the corporation's finite charter. The minority stockholder voted against the extension and, pursuant to Iowa law,[9] majority taxpayers negotiated to purchase the minority's stock interest. Following

[1] Woodward v. Commissioner, 397 U.S. 572 (1970).

[2] United States v. Hilton Hotels Corp., 397 U.S. 580 (1970).

[3] INT. REV. CODE of 1954, § 212 [hereinafter cited as § 212] provides in general: In the case of an individual, there shall be allowed as a deduction all the ordinary and necessary expenses . . . (1) for the production or collection of income; (2) for the management, conservation, or maintenance of property held for the production of income; or (3) in connection with the determination, collection, or refund of any tax.

[4] INT. REV. CODE of 1954, § 162(a) [hereinafter cited as § 162] permits the deduction of all ordinary and necessary trade or business expenses.

[5] 397 U.S. 572 (1970).

[6] 397 U.S. 580 (1970).

[7] Woodward v. Commissioner, 410 F.2d 313 (8th Cir. 1969).

[8] Hilton Hotels Corp. v. United States, 410 F.2d 194 (7th Cir. 1969).

[9] IOWA CODE ANN. § 491.25 (1949), provides that the majority shareholders voting for renewal "shall have three years from the date such action for renewal was taken in which to purchase and pay for the stock voting against such renewal." Although the Iowa statute would characterize the action taken by the majority stockholders as a "renewal," in essence the action involved the creation of a perpetual corporation from a finite one.