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Notes and Comments

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NOTES AND COMMENTS

Agency—Attorney and Client—Attorney's Liability to Third Parties On Contracts Made in Behalf of Client

Within the realm of agency it is recognized that where an agent for a disclosed principal deals with a third party, in a manner which would usually accompany or would be incidental or necessary to the accomplishment of the main authorized purpose of the agency, the principal becomes directly liable to the third party for the agent's acts.[1] But the application of this seemingly inviolate principle has been questioned in a few cases involving the liability of an attorney for contracts entered into on behalf of his client. This is somewhat surprising in light of the fact that the courts have been almost unanimous in holding that the nature of the attorney-client relationship recognizes the attorney's authority to bind his client and his duty to protect and promote his client's interest. They extend the scope of this implied authority and duty beyond the mere prosecution of the suit to all things necessary and incidental to this end.[2] Of course, there are limits beyond which this relationship will not extend but it has been the predominant practice for the courts to hold that "where the relationship of attorney and client exists, the law of principal and agent is generally applied, and the client is bound, according to the ordinary rule of agency, by the acts of the attorney within the scope of his authority."[3] The courts in recognizing the attorney-client relationship as basically controlled by the law of agency[4] have well defined standards by which to measure the actions of an attorney in the management of his client's cause.

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[1] See Runkle v. Burnham, 153 U.S. 216 (1894); Edgewood Knoll Apartments, Inc. v. Braswell, 239 N.C. 560, 80 S.E.2d 653 (1954); Stephens v. John L. Roper Lumber Co., 160 N.C. 107, 75 S.E. 933 (1912); RESTATEMENT (SECOND), AGENCY § 161 (1958). It is recognized that an agent even though acting within his actual or apparent authority may substitute his liability for that of his principal if he expressly assumes liability, as was the case in Betz v. Bank of Miami Beach, 95 So. 2d 891 (Fla. 1957), or fails to disclose his principal, as illustrated in Senor v. Bangor Mills, 211 F.2d 685 (3rd Cir. 1954).

[2] Bank of Glade Spring v. McEwen, 160 N.C. 414, 76 S.E. 222 (1912).

[3] *Id.* at 421, 76 S.E. at 225; *accord,* Jacobsen v. Overseas Tankship Corp., 11 F.R.D. 97 (E.D.N.Y. 1950); Middleton v. Stavely, 124 Colo. 28, 235 P.2d 596 (1951); State v. Barley, 240 N.C. 253, 81 S.E.2d 772 (1954).

[4] Generally, a stricter standard of care is imposed upon the attorney

In a recent Massachusetts case the plaintiffs, a partnership of court reporters, were engaged by the defendant, an attorney-at-law, to take shorthand notes of a hearing in which defendant's client was a litigant. There was no explicit agreement between the parties as to whom plaintiffs would look for the costs of their services. Three bills were submitted by plaintiffs to defendant. The first two during the course of the hearing, for work done to date, and the third, at its conclusion, for the final installment. The earlier bills, having been sent to defendant, were at defendant's request redirected to his client and were paid by check drawn on the client under cover-letter of the defendant. It is the last bill for the final installment that represents the principal sum on which plaintiffs sued both the attorney and his client. This suit resulted in a finding for the plaintiffs solely against the attorney and this result was affirmed on appeal by the Supreme Court of Massachusetts in *Burt v. Gahan.*[5]

There is not a wealth of modern case law involving this situation in relation to attorney-client and third party dealings,[6] but a few recent cases are available[7] and from them it becomes apparent that the current treatment by the courts of situations similar to *Burt*

than is normally applied to the general agent. This standard of care is recognized in Hodges v. Carter, 239 N.C. 517, 8 S.E.2d 144 (1954).

[5] — Mass. —, 220 N.E.2d 817 (1966).

[6] The import of this case on the practicing attorney is significant and should not be confined to the narrow fact situation presented in this case, that of an attorney contracting for stenographic services, but should be applied to all situations in which an attorney finds it beneficial or necessary to his client's cause to obtain the services of a third person. A few of the more common examples being the fees or costs of printers, stenographers, appraisers, accountants, investigators, witnesses, arbitrators, officers, etc.

[7] In one such case, the court held that where a stenographer knew the attorney was acting in behalf of a client the attorney was not liable even though the attorney did not specifically describe himself as an attorney. Zengerle v. Weiss, 48 Misc. 2d 271, 264 N.Y.S.2d 747 (1965); *accord,* Rayvid v. Burgh, 37 Misc. 2d 963, 234 N.Y.S.2d 868 (1962); Sanders v. Riddick, 127 Tenn. 701, 156 S.W. 464 (1913). Another court found the attorney not liable for the printing of briefs and abstracts where the attorney's representative capacity was disclosed to the printer on the printed material, even though the attorney was personally billed. Petrando v. Barry, 4 Ill. App. 2d 319, 124 N.E.2d 85 (1955); *accord,* Loder Appeal Press, Inc. v. Peerless Sugar Co., 277 App. Div. 737, 102 N.Y.S.2d 820 (1951). Where an attorney appointed an appraiser for an estate without arrangements being made regarding payment of fees to the appraiser, the court held the attorney not liable because he was an agent for a known principal. Epstein v. Sichel, 107 N.Y.S.2d 248 (Sup. Ct. 1951).

has been to apply the standards established by the law of agency.[8] It is equally apparent that the court in *Burt* chose to depart from this standard in its treatment of the principal case. In doing so the Massachusetts court recognized that where an attorney contracts in behalf of his client with a third party, the law of agency is generally applicable, but then rejected this as the controlling principle in the following passage:

> While in a broad sense counsel may be an agent and his client a principal, there is much more involved than mere agency. The relationship of attorney and client is paramount, and is subject to established professional standards. In short, the attorney, and not his client, is in charge of litigation, and is so recognized by the court.[9]

The *Burt* case supported this departure from the normally applicable rule of agency by their reliance on *Judd & Detweiler, Inc. v. Gittings*[10] which summarized its holding by stating that "in the absence of express notice to the contrary, court officials and persons connected . . . may safely regard themselves as dealing with the attorney, instead of with his client."[11]

The import of the opinion in the *Burt* case, and its supporting authority, seems to be that the attorney has such absolute and complete control over the client's cause that the status of the attorney is actually elevated to the level of a principal and his client is either placed on a parity or subordinated to a lesser role. This concept is subject to attack in that it fails to recognize that the attorney is bound by a more rigid standard of care than is the ordinary agent[12] and that this more stringent duty coupled with the narrow single-purposeness of the scope of his authority actually limits the attorney's authority[13] to enter into contracts as compared to the broad authority usually conferred upon the average business agent.

The *Burt* case's reliance on *Judd* also seems to be somewhat

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[8] The scope of this comment does not include the legal treatment of the taxible costs of litigation.

[9] — Mass. at —, 220 N.E.2d at 818.

[10] 43 App. D.C. 304 (1915). The principal case cited the following cases as to similar effect: Monick v. Melnicoff, 144 A.2d 381 (D.C. Mun. App. 1958); Trimmier v. Thomson, 41 S.C. 125, 19 S.E. 291 (1894); Heath v. Bates, 49 Conn. 342, 44 Am. Rep. 234 (1881); Cocks v. Searl, 21 L.T.R. (n.s.) 62 (K.B. 1905).

[11] 43 App. D.C. at 310-11.

[12] See note 4 *supra* and accompanying text.

[13] See notes 2-3 *supra* and accompanying text.

misplaced in that the *Judd* court was faced with a situation not presented to the court in the principal case. The *Judd* case showed the presence of local custom and also a course of dealing extending over a long period of time between an officer of the law and the attorney which the court expressly recognized as a controlling factor in that case. The court in *Judd* found that where a course of conduct is present the "law may imply a promise on the part of a lawyer to pay fees for the services of client's writs; as where the officer had been in the constant practice of charging his fees for such services to the lawyer, who from time to time had settled such charges without questioning their legality."[14]

It should also be noted that the decision in the *Burt* case relied on the early Massachusetts case of *Tarbell v. Dickinson*[15] where an attorney was held liable to a sheriff for his fees in serving a writ at the attorney's request. Thus, both the decisions relied upon by the Massachusetts court were cases involving a public officer rather than a private contracting individual. The propriety of applying such cases to a fact situation involving a private business man in his dealings with an attorney should not be left unquestioned. The nature of a public ministerial officer is in itself uniquely different from that of a private contractor. The most important difference is that the public ministerial officer has a duty to perform the services requested and the duty is one which has been imposed by law with the general manner of its performance specifically designated. There is usually little or no discretion or bargaining power allowed the officer.[16] Consequently, the courts have generally recognized that the legally imposed duties and responsibilities upon public ministerial officers have demanded protection for the officer in order to encourage him to perform his duties without fear of personal loss.[17] This trend to protect the public ministerial officer in his obligatory contracts makes these cases[18] less persuasive in their application to similar situations where the parties to the contract are private

[14] 43 App. D.C. at 309.

[15] 57 Mass. (3 Cush.) 345 (1849).

[16] See Mississippi v. Johnson, 71 U.S. (4 Wall) 475 (1866); MECHEM, THE LAW OF PUBLIC OFFICES AND OFFICERS §§ 657-8 (2d ed. 1890).

[17] See Erskine v. Hohnbach, 81 U.S. (14 Wall) 613 (1871); State v Lutz, 65 N.C. 503 (1871); Gore v. Mastin, 66 N.C. 371 (1871).

[18] See Murphy v. Shinberg, 304 Mass. 1, 22 N.E.2d 597 (1939); McCloskey v. Bril, 286 App. Div. 143, 142 N.Y.S.2d 5 (1955); Annot., 100 A.L.R. 533 (1936).

individuals who are completely free to contract on any terms and conditions that they desire.

The North Carolina court has held that where the attorney-client relationship exists the law of agency applies.[19] It also recognized that the scope of the attorney's authority to act for and bind his client extends to all things necessary and incidental to the proper management of the client's cause.[20] The North Carolina court has not expressly given public ministerial officers a remedy against attorneys acting in behalf of their clients or imposed a duty on the attorney to expressly disclaim his liability for such fees in this situation. Quite the contrary, the court has stated that the fees of a sheriff "are paid or tendered by the creditor, for whose benefit the services are to be rendered."[21] Similarly, the court has said that the right of a witness to recover his compensation is against the party for whom he is summoned.[22] These pronouncements would seem to indicate that the North Carolina courts would apply the law of agency to the situation presented in *Burt*.[23]

An opinion which questions the application of agency principles to attorney-client and third party contracts in North Carolina is found in *Ethics Opinion No. 445*[24] of the North Carolina State Bar Council which states:

> It is perfectly proper for an attorney to agree with a physician as to how much he shall be paid to testify in a court action, it being understood that this agreement reached between the attorney and physician is by the attorney in his representative capacity for his client and that the amount is to be paid by the client and the client agreeing to the fee charged by the expert witness.[25]

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[19] See note 3 *supra* and accompanying text.

[20] See notes 1-2 *supra* and accompanying text.

[21] Taylor & Duncan v. Rhyne, 65 N.C. 530, 531 (1871); *accord*, Farmers' Bank, Inc. v. Merchants' & Farmers' Bank, Inc., 204 N.C. 378, 168 S.E. 221 (1933); Dunn v. Clerk's Office, 176 N.C. 50, 96 S.E. 738 (1918); Vannoy v. Haymore, 71 N.C. 128 (1874)

[22] See McClure v. Fulbright, 196 N.C. 450, 146 S.E. 74 (1929); Bailey v. Brown, 105 N.C. 127, 10 S.E. 1054 (1890); State v. Massey, 104 N.C. 877, 10 S.E. 608 (1890).

[23] There is nothing expressly in the opinions to indicate that the attorney procured these services for his client but it is unlikely that the contracts arose otherwise.

[24] N.C. State Bar Council, Ethics Opinion No. 445, 11 N.C. BAR 15 (1964).

[25] *Ibid.*

This opinion recognizes the attorney's authority to contract as an agent for a disclosed principal but seems to go further and require that the attorney and the third party reach an understanding that the client has expressly agreed to the expenses to be charged. This interpretation supports the presumption raised in the principal case that an agent acting for a disclosed principal within the scope of his authority is presumed to act for himself unless he expressly disclaims his own liability. Another possible interpretation in conformity with the application of the law of agency to the attorney's dealings with a third party is that it is proper, within the scope of an attorney's general authority, for an attorney to hire an expert witness in behalf of his client's cause; the result, then, is a presumption that the attorney was acting as an agent for his client, that the client is liable on the contract as a principal, and that the client has agreed to the terms of the contract. Whatever the proper interpretation of *Ethics Opinion No. 445* or its standing in a court of law, it raises serious doubts as to the accuracy of any prediction as to the possible outcome of litigation similar to the *Burt* case in North Carolina.

Since the *Burt* case requires the attorney to expressly disclaim personal liability and destroys the old presumption that an agent for a disclosed principal is presumed to be dealing in behalf of his principal when nothing is said to the contrary, the case establishes a pitfall in the path of the unwary attorney. He may no longer contract as an agent for a disclosed principal with the normal resulting consequences for there is now an added presumption that he intends to contract for himself and an added burden of expressly disclaiming his personal liability for his normal actions in behalf of his client. This decision may also establish an inherent conflict between the attorney's duty to freely operate within the scope of his authority to provide all that is necessary and incidental to the best management of his client's cause and his personal interest in his own economic and personal freedom from liability.[26] In North Carolina, the attorney should be wary in his reliance on the agency principle in this area for the *Burt* case illustrates there is room for variance. A voluntary assumption of the burden of specifically dis-

[26] Quaere: Will this conflict create any reluctance on the part of an attorney to represent a client of little means?

claiming personal liability and seeking the clients express authority in this situation may be the stitch in time that saved nine.

ALGERNON L. BUTLER, JR.

Bankruptcy—Exemptions—Life Insurance Policies With Reserved Right to Change Beneficiary

The issue in *In Matter of Wolfe*[1] was whether cash surrender values of insurance policies on the life of the bankrupt were exempt from the claims of a trustee in bankruptcy. Both policies named the wife as beneficiary, but reserved to the bankrupt husband the absolute right to change the beneficiary. In claiming that the cash surrender values of the policies were exempt, the bankrupt relied on both statutory[2] and constitutional[3] provisions. The court held that the statute was a void attempt to extend the insurance exemption fixed in the constitution and that "the cash surrender values of . . . [the] policies are not exempt property under the Constitution . . . of North Carolina . . . ."[4]

As of the date of the filing of a bankruptcy petition, the trustee acquires title to all propery of the bankrupt[5] except that which is held to be exempt.[6] An insurance policy is property that would

[1] 249 F. Supp. 784 (M.D.N.C. 1966).

[2] The relevant portion of the statutory provision reads as follows:

> If a policy of insurance is effected by any person on his own life . . . in favor of a person other than himself . . . the lawful beneficiary . . . thereof, other than the insured or the executor or administrator of such insured . . . shall be entitled to its proceeds and avails against creditors and representatives of the insured . . . whether or not the right to change the beneficiary is reserved or permitted . . . .

N.C. GEN. STAT. § 58-206 (1965).

[3] The relevant portion of the constitution provides as follows:

> The husband may insure his own life for the sole use and benefit of his wife . . . and in case of the death of the husband the amount thus insured shall be paid over to the wife . . . for her . . . own use, free from all the claims of the representatives of her husband, or any of his creditors. And the policy shall not be subject to claims of creditors of the insured during the life of the insured, if the insurance issued is for the sole use and benefit of the wife . . . .

N.C. CONST. art. X, § 7.

[4] 249 F. Supp. at 786.

[5] Bankruptcy Act § 70(a), 52 Stat. 879(a) (1938), 11 U.S.C. § 110(a) (1964).

[6] "This title shall not affect the allowance to bankrupts of the exemptions which are prescribed . . . by the State laws . . . ." Bankruptcy Act § 6, 52 Stat. 847 (1938), 11 U.S.C. § 24 (1964).

pass to the trustee absent some exempting provisions.[7] When the insured reserves the right to change the beneficiary at will and could name his estate or representative as beneficiary, there is property that vests in the trustee.[8] However, if the policy or any rights or proceeds under it are exempt from the claims of creditors, the policy is exempt from the claims of the bankruptcy trustee.[9] Thus even though the right to change the beneficiary is reserved, the policy is not subject to the claims of the trustee if such a policy is exempt under state law.[10]

Prior to 1932 the North Carolina constitutional provision exempting insurance provided that on the death of the husband, the amount of insurance on his life payable to his wife should be paid to her free from the claims of the husband's creditors.[11] The constitution did not contain the provision that a policy issued for the benefit of a wife should be exempt from the claims of the husband's creditors during his life. However, the legislature had enacted a statute providing that when a policy was made payable to a married woman, it inured to her separate use and benefit.[12] In 1925 the

[7] Burlingham v. Crouse, 228 U.S. 459 (1913). See generally, Annots., 68 A.L.R. 1215 (1930), 103 A.L.R. 239 (1936), and 169 A.L.R. 1380 (1947).

The bankrupt may keep the policy alive and free from the claims of creditors by paying to the trustee an amount equal to the cash surrender value of the policy. The saving clause provides as follows:

> That when any bankrupt, who is a natural person, shall have any insurance policy which has a cash surrender value payable to himself, his estate, or personal representatives, he may . . . pay or secure to the trustee the sum . . . stated, and continue to hold, own, and carry such policy free from the claims of the creditors participating in the distribution of his estate under the bankruptcy proceedings, otherwise the policy shall pass to the trustee as assets . . . .

Bankruptcy Act § 70(a) (5), 52 Stat. 879(a) (5) (1938), 11 U.S.C. § 110 (a)(5) (1964). See Hiscock v. Mertens, 205 U.S. 202 (1907) (defining cash surrender value for purposes of this section).

[8] Cohen v. Samuels, 245 U.S. 50 (1917). The Bankruptcy Act gives the trustee title to powers which the bankrupt could exercise for his own benefit. Bankruptcy Act § 70(a)(3), 52 Stat. 879(a)(3) (1938), 11 U.S.C. § 110(a)(3) (1964).

[9] Holden v. Stratton, 198 U.S. 202 (1905). The bankrupt may commit acts that affect the insurance exemption. See Comment, 1961 DUKE L.J. 569.

[10] *In re* Messinger, 29 F.2d 158 (2d Cir. 1928).

[11] N.C. CONST. art. X, § 7 (1868). For a historical analysis of the North Carolina insurance exemption provisions and the cases thereunder, see Faris, *Exemption of Insurance and Other Property in the Virginias and Carolinas,* 17 WASH. & LEE L. REV. 19, 32-36 (1960) [hereinafter cited as Faris].

[12] N.C. GEN. STAT. § 58-205 (1965).

United States Court of Appeals for the Fourth Circuit in *Whiting v. Squires*[13] considered whether these provisions exempted from the claims of the trustee the cash surrender value of an insurance policy naming the bankrupt's wife as beneficiary, but reserving to the husband the absolute right to change the beneficiary. The court in *Squires* felt that such a construction of the statute[14] would confer an exemption beyond that allowed by the North Carolina constitutional provision. Thus the court held:

> The limit of the constitutional exemption . . . is that the wife or the wife and children take the benefits of a policy payable to her or them as beneficiaries at the death of the insured. The exemption may cover a policy payable to the wife and children with no power of the insured to change the beneficiaries, because in such a policy the wife or the wife and children have a vested interest, and the policy, if paid at all, must be paid to them at the death of the husband. But the exemption does not embrace the surrender value, the property of the husband, of a policy in which he can change the beneficiary at will.[15]

Subsequent to *Squires,* the constitutional provision was amended by adding a provision exempting the policy from the claims of the husband's creditors during his life if the policy was issued for the sole benefit and use of the wife.[16] At the same time the legislature added a statutory provision exempting the proceeds and avails of insurance policies, regardless of whether the right to change the beneficiary was reserved.[17]

It seems that the subsequent amendment and statute were intended to overcome the result in *Squires.*[18] Thus the basic issue before the court in the *Wolfe* case was whether this outcome was achieved. In the absence of a conflict with the constitutional provision, the statute would exempt the policy from the claims of the

[13] 6 F.2d 100 (4th Cir. 1925), *cert. denied,* 269 U.S. 587 (1925).

[14] Statutes similar to the one in question have been construed to exempt the cash surrender value even though the right to change the beneficiary is reserved. *E.g., In re* Reiter, 58 F.2d 631 (2d Cir. 1932); Magnuson v. Wagner, 1 F.2d 99 (8th Cir. 1924); *In re* La Tourette, 23 F. Supp. 631 (E.D. Mo. 1938); Brown v. Home Life Ins. Co., 3 F.2d 661 (E.D. Okla. 1925); Slurszberg v. Prudential Ins. Co., 192 Atl. 451 (N.J. 1936).

[15] Whiting v. Squires, 6 F.2d 100, 01-02 (4th Cir. 1925), *cert. denied,* 269 U.S. 487 (1925).

[16] N.C. CONST. art. X, § 7. See note 3 *supra.*

[17] N.C. Sess. Laws 1931, ch. 179, § 1, N.C. GEN. STAT. § 58-206 (1965). See note 2 *supra.*

[18] Faris at 36. See note 21 *infra.*

trustee.[19] However, the statutory provision must be considered in light of the North Carolina view that the legislature cannot by statute add to an exemption specified in the constitution.[20] The trustee's claim is ultimately resolved by determining whether the present constitutional provision allows exemption during the husband's life when the right to change the beneficiary is reserved. In reaching its result, the court in *Wolfe* concluded that the constitutional amendment did not overrule *Squires*.[21] It held that the wives and children are protected from the claims of the husband's creditors during his life only when the policies are for their *sole* benefit and that the provision does not exempt the policies when the bankrupt has the power to change beneficiaries.[22]

It seems the court felt that insurance is not for the sole benefit of the wife when the husband has the right to change the beneficiary.[23] In reaching the result in the *Wolfe* case, the court apparently assumed that this was the basis of the *Squires* decision. The true basis of the *Squires* decision, however, is that the exemption was granted only for the amounts to be paid over to the wife in the case of the husband's death.[24] The constitutional provision interpreted provided that *on the death of the husband,* "the amount thus insured shall be paid over to the wife . . . free from all claims of . . . creditors."[25] It appears that the cases relied on[26] by the

[19] *E.g., In re* Messinger, 29 F.2d 158 (2d Cir. 1928); *In re* Beckman, 50 F. Supp. 339 (N.D. Ala. 1943).

[20] Wharton v. Taylor, 88 N.C. 230 (1883). The case involved the validity of an attempt by the legislature to expand the homestead exemption beyond the limits specified in the state constitution. See Aycock, *Homestead Exemption In North Carolina,* 29 N.C.L. REV. 143, 144 (1951).

[21] 249 F. Supp. at 786.

> By reading the 1931 statutory amendment and the constitutional amendment together, there is reason to believe that the legislature did intend to limit the effect of the *Squires* case. So far as the constitutional amendment alone is concerned, however, the wording clearly falls short of overruling *Squires.* At the same time the statutory amendment seems to be just another unconstitutional attempt . . . at expanding the insurance exemption.

Faris at 36.

[22] 249 F. Supp. at 786.

[23] In determining the extent of the exemption granted by the amended constitutional provision, "the principal problem will be in determining what policies are for their *sole* benefit." Faris at 36.

[24] See text accompanying note 16 *supra.*

[25] N.C. CONST. art. X, § 7 (1868).

[26] Morgan v. McCaffrey, 286 F. 922 (5th Cir. 1923) (whenever any person shall die); *In re* Morgan, 282 F. 650 (S.D. Fla. 1922) (when person dies); *In re* Long, 282 F. 383 (S.D. Fla. 1918) (whenever any person dies).

Squires court involve construction of the scope of provisions purporting to exempt proceeds payable *at the death of the insured,* rather than a determination that insurance is not for the sole benefit and use of the beneficiary merely because the right to change is reserved.

It is submitted that the 1932 amendment does overrule the *Squires* decision. This is because the amendment purports to grant exemption during the life of the insured husband and, in addition, applies to the *policy* rather than the proceeds payable at death. Exemption of the policy itself should exempt the cash surrender value from the claims of the bankruptcy trustee.[27] Thus the result in *Wolfe* seems to be founded on the idea that the policy is not issued for the sole benefit of the wife if the husband retains the right to change the beneficiary. Such a restrictive construction, coupled with the modern practice of reserving the right to change beneficiaries,[28] would make the constitutional provision a virtual nullity. The insurance is for the benefit of the wife if, at the time of the bankruptcy, she is named as beneficiary and the power to change has not been exercised,[29] and reservation of the power to change the beneficiary should not deprive the policy of the characteristic of

[27] See *In re* La Tourette, 23 F. Supp. 631 (E.D. Mo. 1938). And where the provision purports to exempt the "proceeds and avails," the courts hold the cash surrender value is exempt. *E.g.,* Pearl v. Goldberg, 300 F.2d 610 (2d Cir. 1962); *In re* Messinger, 29 F.2d 158 (2d Cir. 1928); *In re* Beckman, 50 F. Supp. 339 (N.D. Ala. 1943).

[28] In refusing to hold that exemption is precluded by reservation of the right to change the beneficiary, courts have specifically referred to the prevalent tendency to include such reservations in modern insurance policies. See, *In re* Reiter, 58 F.2d 631 (2d Cir. 1932), Slurszberg v. Prudential Ins. Co., 192 Atl. 451 (N.J. 1936).

Very few of the policies now issued would qualify for exemption under the rule established in the instant case.

> [A]ll . . . policies as now issued contain provisions which, in effect, state that unless otherwise provided by endorsement to the policy, the insured is the *owner* of the policy. The *owner* of the policy possesses the right to change the beneficiary without the consent or approval of the beneficiary. . . . [I]t is believed that the *overwhelming majority* . . . of the policies issued in which the husband is the insured and the wife is named beneficiary, are those in which the insured—husband is the owner (rather than the beneficiary—wife). . . .

Letter From Robert H. Koonts to David S. Orcutt, March 13, 1967. (Mr. Koonts is Associate General Counsel for Jefferson Standard Life Insurance Company, Greensboro, N.C.)

[29] See *In re* Pittman, 275 Fed. 686 (E.D.N.C. 1921). Although Judge Connor was mistaken as to the power of the trustee to require the bankrupt to exercise a change of beneficiary, his test for determining if insurance is for the benefit of the wife seems to be the proper one.

being for the benefit of the wife.[30] Construction of the exemption provision should be such that it accomplishes its paramount purpose, the protection of the wife.[31] The decision of the district court in *Wolfe* defeats that purpose and is contrary to repeated holdings of bankruptcy referees in the state since the constitutional amendment and statute were added.[32] It has been suggested that the constitutional amendment only assures that policies of insurance on the life of the husband are exempt during his life if there is no reservation of the right to change the beneficiary.[33] Such a restrictive interpretation of the effect of the constitutional amendment credits the legislature with drafting and submitting to the people a constitutional amendment, and simultaneously enacting a statute in violation of that amendment.

While a decision of the North Carolina Supreme Court[34] could definitely establish the scope of the constitutional exemption, it is unpredictable when the court would be called upon to decide that question. A more immediate and effective way to overcome the unfortunate decision in *Wolfe* would be to amend the constitutional provision, making the insurance exemptions available in North Carolina similar to the exemptions allowed in other jurisdictions.[35] This could easily be accomplished by replacing the present language of the constitutional provision with the wording of North Carolina General Statute § 58-206.[36]

DAVID S. ORCUTT

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[30] *E.g., In re* Reiter, 58 F.2d 631 (2d Cir. 1932); *In re* La Tourette, 23 F. Supp. 631 (E.D. Mo. 1938); Brown v. Home Life Ins. Co., 3 F.2d 661 (E.D. Okla. 1925); Slurszberg v. Prudential Ins. Co., 192 Atl. 451 (N.J. 1936).

[31] *E.g., In re* Reiter, 58 F.2d 631 (2d Cir. 1932); Slurszberg v. Prudential Ins. Co., 193 Atl. 451 (N.J. 1936).

[32] See the order of Referee Rufus W. Reynolds in the principal case. In his conclusions of law, the referee stated:

> The undersigned Referee for over nineteen years has been consistently and regularly recognizing the cash surrender of life insurance policies on the bankrupt to be exempt where the beneficiary is the wife or children of the bankrupt even though there is a reservation for a change of beneficiary.

Order of Rufus W. Reynolds, Referee in Bankruptcy, In Matter of Wolfe, Nos. B-35-65 & B-36-65 (M.D.N.C. 1965).

[33] Brief for Appellant, p. 4, In Matter of Wolfe, 249 F. Supp. 784 (M.D.N.C. 1966).

[34] The North Carolina court apparently has not considered the effect of the constitution and the statute in a situation where the creditor is seeking to attack the policy during the life of the insured husband.

[35] See Riesenfeld, *Life Insurance and Creditors' Remedies in the United States*, 4 U.C.L.A. L. REV. 583 (1957).

[36] (1965).

Civil Procedure—The Indispensable Party Doctrine and Federal Rule 19

The troublesome application of the indispensable party doctrine at common law and under old rule 19 of the Federal Rules has in recent years been the subject of intensive scholarly examination and criticism[1] which led directly to a complete clarification and rewriting of rule 19.[2] Both the validity and effectiveness of the revised rule, however, have already been seriously questioned by the third circuit in *Provident Tradesmens Bank & Trust Co. v. Lumbermens Mut. Cas. Co.*[3] A combination of the court's poorly articulated objections to rule 19 and its overall confusion in analysis indicates that the revision has not only created new difficulties but failed to resolve completely the old, at least as far as the third circuit is concerned.

The modern indispensable party practice owes its origin primarily to *Shields v. Barrow*,[4] which defined three groups of parties: "proper" or "formal"—parties who *can* be joined if desired; "necessary"—parties interested in the action who *should* be joined if at all possible in order to do complete justice and minimize litigation; and "indispensable"—parties who *must* be joined or the suit dismissed if their interests are not "separable" from the interests of those already joined. Basically the determination of indispensability is a question of weighing the interests of the courts in completing all common litigation efficiently in one suit, the interests of the defendant in protection from multiple vexation, and the interest of the absent party in not being adversely affected by the outcome.[5] Many courts analyzed the problem in that way. Other courts, however, apparently mislead by the emphasis in *Shields* on the undefined concept of "separability" and the ideal of doing "complete justice," lost sight of the basic interests outlined above. Some mechanically

[1] See generally, Fink, *Indispensable Parties and the Proposed Amendment to Federal Rule 19*, 74 YALE L.J. 403 (1965) [hereinafter cited as Fink]; Hazard, *Indispensable Party: The Historical Origin of a Procedural Phantom*, 61 COLUM. L. REV. 1254 (1961) [hereinafter cited as Hazard]; Reed, *Compulsory Joinder of Parties in Civil Actions*, 55 MICH. L. REV. 327 (1957) [hereinafter cited as Reed].

[2] Order, 39 F.R.D. 213, 218 (1966). It became effective July 1, 1966.

[3] 365 F.2d 802 (3d Cir. 1966).

[4] 58 U.S. (17 How.) 130 (1855); see also, Washington v. United States, 87 F.2d 421 (9th Cir. 1936).

[5] Reed at 330-40, 356.

applied technical and abstract classifications such as "joint interest," "united in interest" or "separability," when a closer examination would have revealed, for instance, that the absent party could in no way have been affected by the outcome of the suit.[6] Others felt they had to dismiss if all possible claims arising out of the same transaction could not be litigated in the one action before them.[7] Still others made the mistake of thinking that a judgment would bind the absent party to his detriment and thus held there was no "jurisdiction" over parties already joined,[8] in spite of the fact that no judgment can *legally* affect anyone not a party to the action.[9] Because of the hardship of dismissal often occasioned by rulings of indispensability, some states enacted remedial statutes making "joint" obligations joint and severable so that a court could proceed without an absent party who could not be served with process.[10] Although old rule 19 was intended to elicit an examination and a balancing as the common law doctrine often did,[11] the rule's confusing language helped perpetuate many of the errors[12] and some courts refused to apply it at all in the indispensable party situation.[13]

[6] *Id.* at 355-56. See also FED. R. CIV. P. 19, Comment, 39 F.R.D. 89, 91 (1966).

[7] See Fouke v. Schenewerk, 197 F.2d 234 (5th Cir. 1952), criticized in Hazard at 1288-89.

[8] See Samuel Goldwyn, Inc. v. United Artists Corp., 113 F.2d 703, 707 (3d Cir. 1940); *cf.* Calcote v. Texas Pac. Coal & Oil Co., 157 F.2d 216 (5th Cir.), *cert. denied,* 329 U.S. 782 (1946); see also Reed at 332-34, 343.

[9] Reed at 343. It is, of course, possible for a party to be *factually* injured by a judgment in his absence if, for example, a fund to which he has a claim is exhausted so that his claim, though legally unimpaired, is worth nothing as a practical matter. It is this kind of factual injury that provoked the issue of indispensability in *Provident Tradesmens.* See Reed at 336.

[10] See 2 WILLISTON, CONTRACTS § 336 (3d ed. 1959) (collecting statutes). The effect of calling a party indispensable in federal court is often dismissal, either because that party cannot be served with process or his joinder would destroy diversity. It is probable, however, that a state court will term the same party indispensable as well, and if he is out of the state court's jurisdiction, the plaintiff will have no forum in which to prosecute his suit.

[11] See Fink at 430-31.

[12] See FED. R. CIV. P. 19, Comment, 39 F.R.D. 89, 90-91 (1966). The rule arguably equated "indispensable" with the phrase "having a joint interest" and as a result, many courts continued to look to the technical catchwords as automatic indications that certain parties were indispensable. In addition, the use of the word "jurisdiction" in 19(b) was misleading, for while it was intended to refer to the subject matter of the action, some courts interpreted it to mean that the absence of an indispensable party itself deprived the court of jurisdiction over the parties already joined.

[13] Calcote v. Texas Pac. Coal & Oil Co., 157 F.2d 216, 219 (5th Cir.), *cert. denied,* 329 U.S. 782 (1946); *cf.* Chidester v. City of Newark, 162

The recent scholarly literature exploded many of the misconceptions that grew around the old rule, and the revision that followed reflects the impact of Professor Reed's analysis. While the court in *Provident Tradesmens* discussed only the old rule,[14] its treatment of the case would probably have been the same had it applied the new.[15]

The litigation leading up to *Provident Tradesmens* arose out of a two vehicle accident in which all but one of the parties were killed, including the responsible driver who was operating a borrowed car. Provident, as administrator of the estate of Lynch, a passenger, sued the driver's estate in federal court and obtained a default judgment. Lumbermens, the car owner's insurer, had refused to defend, claiming the driver was not within the scope of the owner's permission at the time of the accident and thus not covered by the policy. Provident then brought the present declaratory judgment action which involved the issue of permission and Lumbermens' liability. The driver's estate was joined as a defendant, and the two other claimants, whose state court actions against the owner were still pending, were joined as plaintiffs; the owner was not joined. The issue of Lumbermens' liability was determined in Provident's favor by the court which directed verdicts for two plaintiffs and by a jury which found for the third.[16]

F.2d 598 (3d Cir. 1947); United States v. Washington Institute of Technology, Inc., 138 F.2d 25 (3d Cir. 1943) (in both cases the third circuit ruled that indispensable parties under rule 19 were those who were indispensable *prior* to the rule; in determining their existence, then, the court did not look to the rule for standards).

Old rule 19 contained a negative implication which lent itself to that interpretation and allowed the court in *Provident Tradesmens* to say that "Rule 19, in terms, relates only to 'necessary parties' and specifically excludes from its sweep 'indispensable parties.'" 365 F.2d at 811. The revision contains no such negative implication.

[14] The new Rule 19 became effective July 1, 1966, when the appeal in the present action was pending. Although the Order of the Supreme Court amending the Rules is directed at the district courts and cases there pending, Order, 39 F.R.D. 213 (1966), and probably does not include appeals, the court here raised the question itself and thus arguably should have applied the new Rule.

[15] Although the court indicated its recognition of the revision only once, 365 F.2d at 806, it is quite possible that the entire opinion was directed exclusively at the substance of the new rule. It was already well settled in the third circuit that the standards of old rule 19 did not apply in the indispensable party situation (see note 13 *supra*), and unless the court was implicitly discussing the new rule, most of its lengthy opinion was superfluous.

[16] 218 F. Supp. 802 (E.D. Pa. 1963). Two verdicts were directed for the two estate plaintiffs because the only witness on the scope of permission, the

On appeal, the third circuit after a rehearing en banc, held 5-2 that the owner was an indispensable party, an issue raised sua sponte despite the provision in rule 12(h)(2)[17] of the Federal Rules that the indispensability question is waived after trial on the merits. Judgment was vacated and the cause remanded with directions to dismiss the action. The court reasoned that depending on the outcome of the state court actions against him, the owner might have to share the proceeds of his limited insurance policy with claims against the driver and thus might lose a measure of protection if there were a judgment declaring the insurer liable in this action. The possibility of such an adverse effect on the owner's interest as a result of the declaratory judgment made him an indispensable party under *Shields v. Barrow*,[18] and the lower court should never have proceeded without him. The indispensable party doctrine, the court emphasized, is a rule of substantive law which rule 19 cannot alter or affect without violating the Enabling Act.[19] In the dissenting opinion, Judge Freedman argued that the court should try to preserve the jury verdict. The owner's interest could be protected, he suggested, simply by shaping a decree that would stay execution on the insurance policy until the state court actions against the owner were concluded. At that time the owner, if found liable, could assert his claim of superiority to the insurance fund and relitigate the issue of permission.

There are three possible interpretations of the majority opinion, ranging from complete rejection of the substance of new rule 19 to almost complete acceptance, with important reservations as to its outer limits. There is much at first glance to support an interpretation that the court is rejecting outright the substance of the new rule; the majority opinion is confusing and inconsistent, however,

owner, was ruled incompetent to testify under the Pennsylvania Dead Man's Act, PA. STAT. ANN. tit. 28 § 322 (1958) and there was thus no evidence to rebut the Pennsylvania presumption that a dead man operates a borrowed car within the scope of his permissive use. The lower court ruled the owner incompetent to testify on the ground that his interest was adverse to that of the two estates because he stood to lose a measure of his insurance protection in this suit. The owner could, of course, testify as to the other plaintiff who was not killed in the accident. The third circuit based its finding of possible adverse affect on the owner's interest entirely on the district court's determination of adverse interest for purposes of the Dead Man's Act. 365 F.2d at 805.

[17] FED. R. CIV. P. 12(h)(1) before the revision.

[18] 58 U.S. (17 How.) 130 (1855).

[19] 28 U.S.C. § 2072 (1964), which provides in part that "such rules shall not abridge, enlarge, or modify any substantive right . . ."

both in what it says and the authority it cites, and there is equal support to counter this view. Quoting dictum from a recent case in the first circuit,[20] the majority states that "what are indispensable parties is a matter of substance, not of procedure"[21] and later makes the assertion that rule 19 cannot modify "the standards by which the existence of an indispensable party may be determined."[22] In yet another passage the majority contends that there is nothing in an early Supreme Court decision[23] to merit its citation as a "flexible and imaginative adaptation of remedies in disregard of the indispensable party doctrine."[24] These statements justify an interpretation that the majority is condemning the new rule's standards for determining indispensability by balancing the interests of the defendant, plaintiff, absent party and courts, and taking into account any imaginative decree that might lessen injury to the absent party. Instead, the majority intimates, it will continue to apply the indispensable party doctrine as it existed prior to the adoption of the rules in 1938.[25] In a formalistic, abstract classification of rights typical of that doctrine, the court said that since the "interests of the insurer and insured are identical, their interests are joint;"[26] ergo in an action against the insurer, the insured is indispensable.[27] If, indeed, the absent party could have been protected by the dissent's proposed decree,[28] it is not difficult to interpret the majority

[20] Stevens v. Loomis, 334 F.2d 775, 778 n.7 (1st Cir. 1964). In his opinion, Judge Aldrich discussed the proposed new rule in its preliminary form and the Advisory Committee Comment thereto, *id.* at 777 n.4. The formulation of the rule at that time contained no reference at all to the words "indispensable parties," and Judge Aldrich made the not illogical assumption that the Rule was intended only to clarify existing rules for necessary parties, leaving indispensable parties out of its scope entirely. See also Fink at 424-26.

[21] 365 F.2d at 806. (All italicized in original.)

[22] *Id.* at 812. The authority quoted was *dictum* in Stumpf v. Fidelity Gas Co., 294 F.2d 886, 890 (9th Cir. 1961), a case which is ironically cited with approval by the Advisory Committee, FED. R. CIV. P. 19, Comment, 39 F.R.D. 88, 92 (1966).

[23] Payne v. Hook, 74 U.S. (7 Wall.) 425 (1869).

[24] 365 F.2d at 810.

[25] See notes 13 & 15 *supra.*

[26] 365 F.2d at 809.

[27] This is an example of some of the court's inconsistent reasoning which indicates that much of its language cannot be meant seriously. The characterization here of the insurer and the owner as having a joint interest is totally irrelevant to the indispensability question actually raised by the court—the "joint" claims of the owner and *driver.*

[28] 365 F.2d at 811, 816 n.16.

to say implicitly that on its face new rule 19 violates the Enabling Act.

There are three indications, however, that this interpretation is unsatisfactory. In the first place, the court relied in part on *Roos v. Texas Co.*,[29] a case which demonstrates the kind of flexible analysis[30] the Rules' Advisory Committee has recommended for the new rule.[31] The reasoning is as follows: the absent party will be factually injured by a judgment here if he is not joined; joinder will defeat diversity; true, it is possible to frame a decree that will protect the absent party; that decree, however, would defer the plaintiff's recovery to the indefinite future and thus be a virtual denial of relief; therefore, the case must be sent back to the state court where all parties can be joined and the funds paid out at once. The court's reliance on *Roos,* then, is certainly inconsistent with the first interpretation that the court is applying rigid, technical classifications and disregarding the practical consequences. In the second place, the court on three separate occasions asserts that the indispensable party doctrine accords a "substantive right to a person to be joined as a party to an action when his interests may be affected by its outcome."[32] This is somewhat different from the contention that rule 19 cannot affect the standards by which the *existence* of an indispensable party is determined, for those mechanical and formalistic standards often foreclose any examination of the facts to determine exactly what an absent party's interest is. Finally, the majority opinion emphasizes that a declaratory judgment action is procedural, not equitable, in nature.[33] In pointing this out, the court is merely asserting that a tribunal in such a proceeding has *less* leeway to continue in the absence of interested parties than it would if it were sitting in equity. But the very recognition of the distinction, however unreal that difference is,[34] belies the notion

[29] 23 F.2d 171 (2d Cir. 1927), *cert. denied,* 277 U.S. 587 (1928).

[30] 365 F.2d at 811, 816 n.16.

[31] FED. R. CIV. P. 19, Comment, 39 F.R.D. 89, 93 (1966).

[32] 365 F.2d at 805, 809, 812. The court at one point speaks of a party's substantive right to be joined when his rights *will* be affected, in contrast to *may* be affected. The court here was faced with the latter situation, for the owner might not be found liable in the state courts, either on the question of the driver's negligence or the issue of permission.

[33] 365 F.2d at 809-10.

[34] The Court seems to be overlooking the fact that while a declaratory judgment action is procedural, it is also discretionary: "The flexibility inherent in the declaratory procedure indicates that there may be times when the court will be able to proceed without prejudicing the rights of absentees,

that the court intends blindly to apply such catchwords as "joint interest" in ruling on indispensability in all cases. These inconsistencies, then, somewhat discredit the first interpretation and indicate that the court meant something other than a complete rejection of rule 19.

A second interpretation can be made that the court was accepting one possible view of the new Rule and rejecting another—that it actually did go beyond a mechanical approach to balance the underlying factors, but that it dismissed because it would not accept what might be considered a fundamental change in the old rule and the common law doctrine in its best application. It has been recognized that the new rule is subject to two readings.[35] The first is that the revision is merely intended to clarify and strengthen the old rule in light of cases that misconstrued it or failed to apply it at all; this much is certainly clear from the Advisory Committee Comment.[36] The second reading is that Professor Reed's proposed formulation[37] and the new rule 19 could be taken to mean that having weighed the four factors enumerated in rule 19(b), a court "is then free to proceed without an absent person *who would be affected by the decree, no matter how it was shaped,* if the court decides on balance that it would be more convenient and fairer to go on without the absent party than to dismiss."[38] The Advisory Committee Comment supports this reading of the rule as well.[39] In addition, the Comment points out that the idea of proceeding even though a decree would not fully protect the absent party was "well understood in the older equity practice"[40] of the 17th and 18th centuries. There is, however, an intervening line of authority begin-

although the same result would be more difficult to reach under stricter procedures." Caldwell Mfg. Co. v. Unique Balance Co., 18 F.R.D. 258, 260 n.2 (S.D.N.Y. 1955). See also Reed at 354-55 n.94: "[T]he declaratory judgment may be shaped, *as an equitable decree,* to accomplish the possible." (Emphasis added.)

[35] Fink at 415.

[36] See note 14 *supra.*

[37] Reed at 336.

[38] Fink at 415. (Emphasis added.)

[39] "It is true that an adjudication between the parties before the court may on occasion adversely affect the absent person as a practical matter, or leave a party exposed to a later inconsistent recovery by the absent person. These are factors which should be considered in deciding whether the action should proceed, or should rather be dismissed; but they do not themselves negate the court's power to adjudicate as between the parties who have been joined. FED. R. CIV. P. 19, Comment, 39 F.R.D. 88, 89 (1966).

[40] *Id.* at 90. See Hazard for a history of that practice.

ing roughly with *Shields v. Barrow*[41] in the 19th century which has apparently ruled out this particular proposition. Even the cases cited by the Advisory Committee as examples of a "shaping of relief" by which prejudice may be averted or *"lessened"* seem to indicate on the contrary that the relief shaped must be without *any* substantial prejudice to the absent party.[42] The second reading of the new rule, then, may be disregarding this authority and may be the source of the Third Circuit's objections to the revision.

The second interpretation that the majority opinion is merely rejecting the latter reading of the new rule is supported by those same considerations analyzed above as countering the first interpretation: the court's reliance on *Roos v. Texas Co.,* its assertion of a party's substantive right to be joined, and its emphasis on the nonequitable nature of declaratory judgment. As pointed out above, the court, in basing its decision in part on *Roos,* accepts an approach that requires a court to weigh the underlying factors before coming to a final decision on indispensability. It is just intimating by its otherwise sweeping language that it will not balance away any injury to an absent party no matter how strongly other considerations call for proceeding without him. It is perhaps this hesitancy to sanction any irrevocable injury to an absent party that the court was referring to when it asserted so often that a person has a *substantive* right to be joined to an action when his interests may be affected by its outcome. Finally, we have seen that the court's emphasis on the non-equitable nature of the present action is a recognition that a court *can* balance, though how far it can go may vary with the kind of action brought. That emphasis may also be an attempt to underscore the court's rejection of the second reading of rule 19 insofar as the revision purports to incorporate the old equity practice of proceeding with an action despite injury to an absent party. If, in this situation, the dissent's suggested decree could be completely effective, the majority's concern over some injury to the owner is then somewhat off the mark. But if the owner's interest could not adequately be protected by any decree, the majority may

[41] 58 U.S. (17 How.) 130 (1855).

[42] See, *e.g.,* Stumpf v. Fidelity Gas Co., 294 F.2d 886 (9th Cir. 1961); Ward v. Deavers, 203 F.2d 72 (D.C. Cir. 1953); Roos v. Texas Co., 23 F.2d 171 (2d Cir. 1927), *cert. denied,* 277 U.S. 587 (1928); Miller & Lux, Inc. v. Nickel, 141 F. Supp. 41 (N.D. Cal. 1956). See also cases cited in Provident Tradesmens Bank & Trust Co. v. Lumbermans Mut. Cas. Co., 365 F.2d 802, 810 (1966); Fink at 433.

be making the objection that rule 19's command to proceed could amount to an unconstitutional denial of due process.[43]

There is an obvious difficulty with the above interpretation. While the court insists that the owner has a substantive right to be joined, it is clear that his joinder in the declaratory action would accomplish nothing[44] except to force dismissal for lack of diversity.[45] Thus the court must have had something else in mind in its ruling on indispensability, and the possibility of dismissal as an end in itself suggests a third interpretation which may be the most proper one to make. The Court may simply have decided, without stating the reasons, that all of the litigation arising out of the accident should have been confined to the same state court. The considerations leading to such a decision could have prompted dismissal even under the new rule 19. The conditional decree deferring a possibly decreased recovery for an indefinite period, for instance, would come close to denying any relief at all to the plaintiff. The inadequacy of relief is the third of the four factors to be weighed under the new rule,[46] and was the basis for the dismissal in *Roos v. Texas Co.*[47]

Furthermore, the shaping of relief itself would have entailed considerably more difficulties than the dissent, perhaps, anticipated.

[43] See Note, 80 HARV. L. REV. 678, 682 (1967); see also Reed at 336. *Cf.* Western Union Tel. Co. v. Pennsylvania, 368 U.S. 71 (1961), which may cast constitutional doubt on the analogous problem of subjecting a party presently in the action to double liability to other plaintiffs not parties to the suit, and thus not bound by it. See JAMES, CIVIL PROCEDURE § 9.17 (1965).

[44] Since the state court actions would still be pending, the owner would have no basis for claiming a share in the insurance fund, and the court would still have to resort to a decree to protect him. Thus, the owner would be only a formal party to the action and could do no more than he has already done—testify. In fact, the owner would probably prefer *not* to be a party, for then he would be entitled to the benefit of a judgment in this action were it in favor of the insurer, see Hinchey v. Sellers, 7 N.Y.2d 287, 165 N.E.2d 156, 197 N.Y.S.2d 129 (1959); but he would not have been bound had it gone the other way, Makariw v. Rinard, 336 F.2d 333 (3d Cir. 1964).

[45] Joinder would put Pennsylvanians on both sides of the suit.

[46] FED. R. CIV. P. 19(b) provides in part:

> The factors to be considered by the court include: first, to what extent a judgment rendered in the person's absence might be prejudicial to him or to those already parties; second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided; third, whether a judgment rendered in the person's absence will be adequate; fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder.

[47] 23 F.2d 171 (2d Cir. 1927), *cert. denied*, 277 U.S. 587 (1928).

Lynch, for instance, would presumably be entitled to interest on the judgment until paid,[48] and the insurer would argue that it should not have to pay it since the court is responsible for the delayed recovery. Absolving the insurer of liability for some of the interest during the stay of execution, however, would require considerable administrative red tape.[49] Further, the insurer might have to pay interest on Lynch's *entire* judgment against the driver, even if that judgment exceeded the policy limits or the decreased insurance coverage allotted to Lynch upon assertion of claims by the owner under the terms of the proposed decree.[50] In addition, there may be far greater problems relating to the legality of giving the owner a claim of superiority, or even of apportioning the funds on a pro-rata basis; these difficulties involve the second factor under rule 19(b), and will be examined more fully below.

Finally, it is clear that the plaintiff will have an adequate remedy in state court—the fourth factor to be considered under the new rule 19. It is not much of an answer to say that since the plaintiff has waited eight years, it is unfair to make him start all over again;[51] the decree itself would defer his recovery anyway. In fact, the court might have had positive reasons for thinking that this litigation should have been in state court from the start[52] and that a Federal court is really an improper forum. A state court, for instance, could better deal with the problem of distributing the funds if all suits were consolidated; the possibility of any unreasonable disparity in recovery by different plaintiffs would be lessened; and difficulties with interest payments and settlement[53] would be less likely to arise. The

[48] This would include, in addition to interest on the judgment against the insurer, interest on the judgment against the driver, for which many policies provide even though the insurer is not legally bound until there is a judgment against it. See Alford v. Textile Ins. Co., 248 N.C. 224, 103 S.E.2d 8 (1958); 7 AM. JUR. 2d *Automobile Insurance* § 197 (1963).

[49] See Commercial Union Ins. Co. v. Adams, 231 F. Supp. 860 (S.D. Ind. 1964), where the court stipulated that sizeable funds interplead by the insurers would be invested by the court to offset costs.

[50] See Annot., 76 A.L.R.2d 979 (1961). In some jurisdictions, the interest owed by the insurer is computed on the basis of the policy limits alone. See, *e.g.*, Alford v. Textile Ins. Co., 248 N.C. 224, 103 S.E.2d 8 (1958).

[51] 365 F.2d at 820 (dissenting opinion). Plaintiff would have to seek a declaratory judgment in a state court under PA. STAT. ANN. tit. 12, § 831 (1953).

[52] Had Lynch sued both the driver and the owner as the other plaintiffs did, he would not have had diversity and would have had to start in state court.

[53] See note 58 *infra*.

inappropriateness of a Federal court as a forum seems to have been a weighty factor in many rulings on indispensability that resulted in dismissal;[54] courts have even sent cases down to the state courts under the cloak of indispensability where actually the absent party would in no way have been injured, legally or factually, by a federal court judgment.[55]

Thus, a combination of incomplete relief, possible impracticality of the shaped decree, and the availability and perhaps desirability of another forum might well call for dismissal here even under a liberal application of the new rule. The nub of the dissenting opinion is that the jury determination of permission ought to be preserved if at all possible; but these factors could even outweigh that consideration when it is remembered that the owner is probably going to relitigate the same issue again himself. Even under this interpretation, of course, the court is still issuing a definite caveat: the court will not proceed to judgment in a future case in the absence of a party who would be injured thereby, no matter how strongly other considerations call for preserving the action. Such a warning would explain much of the court's categorical, sweeping language; it was merely pointing out, in a strong way, that there is a very long line of precedent that the new rule 19 may be disregarding.

The foregoing analysis of the court's decision, of course, is based on its rather inadequate view of the protective decree and the owner's need for protection. Any evaluation of the result that should

[54] Roos v. Texas Co., 23 F.2d 171 (2d Cir. 1927), *cert. denied*, 277 U.S. 587 (1928) ("There is no apparent injustice in the result. . . . why the suit should be brought here it is difficult to see." *Id.* at 173); Fitzgerald v. Haynes, 241 F.2d 417 (3d Cir. 1957) ("[I]f the joining of these principal parties in interest should reveal that the controversy is essentially a local one among Pennsylvanians, and thus *not a diversity case,* the result would be no more than the relegation of the suit to the forum in which it belonged from the beginning." *Id.* at 420). (Emphasis added.)

[55] *E.g.,* Fouke v. Schenewerk, 197 F.2d 234 (5th Cir. 1952); American Ins. Co. v. Bradley Mining Co., 57 F. Supp. 545 (N.D. Cal. 1944). The court may well have had other unstated reservations against allowing Lynch to prosecute his claim alone in Federal court. It may have been concerned that a jury in a similar situation might be more generous than if actively faced with having to award damages for three plaintiffs against limited insurance coverage. It may have been concerned that the insurer's refusal to defend in Federal court which lead to a default judgment may have prejudiced the other plaintiffs and the owner to the extent that a defense could have meant less damages and less of an inroad on the insurance fund. Finally, the insurer was prepared to challenge the application of the statutory presumption which resulted in two directed verdicts against it; the court may have preferred not to deal with that question, leaving it to the state court.

have been reached, however, requires an unassuming examination of the feasibility of the proposed decree, and, more fundamentally, of the precise injury to which the owner allegedly was subject. Superficially, at least, the correctness of the court's decision could logically be seen to turn on the decree's feasibility. Thus, if the dissent's proposal can fully protect the owner with a minimum of red tape, it would seem that the court was wrong in ruling the owner indispensable under the reasoning of the first two interpretations, and possibly under the third. On the other hand, it would seem to follow as well that if the decree cannot protect the owner, then the court was correct—the owner had to be a party to the action that would now be brought at the state level where, all claims being joined, the court could more easily distribute the funds. It is precisely here, however, that Judge Freedman's otherwise well documented dissent fails for want of authority.[56] In fact, it is not clear at all that a court could properly order a pro-rata distribution of the funds; it is even less clear that it could grant superiority to the owner.

While there appears to be no direct authority on this question, *claimants* involved in separate actions generally take on a "first in time, first in right" basis; in other words, priority to the insurance fund is accorded on the basis of priority of judgment.[57] Much of the rational underlying this rule would apply equally in this situation where there are conflicting claims between insureds.[58]

[56] See note 57 *infra.*

[57] *E.g.,* Ligouri v. Allstate Ins. Co., 76 N.J. Super. 204, 184 A.2d 12 (Ch. 1962); David v. Bauman, 24 Misc. 2d 67, 196 N.Y.S.2d 746 (Sup. Ct. 1960); see generally, Comment, *Pro-Rating Automobile Liability Insurance to Multiple Claimants,* 32 U. CHI. L. REV. 337 (1965); Annot., 70 A.L.R.2d 416 (1960). The only authority apparently cited by the dissent for giving the owner proration or superiority consisted of two early Supreme Court cases decided in 1859 and 1909 which naturally do not deal with automobile liability insurance, 365 F.2d at 819 n.9.

[58] The insurer should not have to determine the value of all potential claims in order to settle with each on a pro-rata basis (this is particularly true here since the owner may win in the state court); the dockets would be overburdened if no one claim could be settled until all actions had come to completion; ratable distribution would interfere with the insurer's contractual right to settle, Comment, 32 U. CHI. L. REV. 337, 339, 340 & n.14 (1965). A particularly acute settlement problem could arise in the case. If a decree were granted staying execution, Lynch might prefer to settle in order to get his funds now. But the insurer might settle too high, opening himself to liability if the court were later to order proration for the owner's benefit. Conversely, the insurer might be able to drive a very hard bargain with Lynch by a threat that the latter would receive very little if the owner were to get a claim for superiority. If the owner were

On the other hand, pro-rata distribution has been allowed where all suits have been joined in one action, or the insurance company has used the device of interpleader after all claims have been reduced to final judgment.[59] Because of these exceptions, it is possible here, for instance, that following a stay of execution, the insurer might interplead to allow proration. It may even be possible in the future to interplead in federal court where, as in *Provident Tradesmens,* there are claims still outstanding; the Ninth Circuit recently rejected interpleader where all claims had not come to judgment,[60] but the Supreme Court has granted certiorari.[61] Futhermore, it might be possible to order an equitable apportionment at the request of the owner by analogy to surety law, where the surety can ask the court to direct application of the debtor's involuntary payments ratably between the latter's secured and unsecured obligations.[62] Aside from these rather unlikely possibilities, however, it is quite possible that a federal court would have no authority to direct proration here. The fact that apportionment can be had if all claims are joined in one suit may be one more reason why the court reversed, or why it should have. If all these claims had been joined in state court at the start, much of the difficulty would not have arisen. It would thus seem that since the legality of a protective decree is doubtful, the owner would be adversely affected by a judgment in his absence, and the court was correct in ruling him indispensable to the action and therefore dismissing it.

Unfortunately, a closer examination of the apportionment problem leads inevitably to exactly the opposite conclusion. The court's

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then found *not* liable, the insurer would have escaped the entire accident with very little liability.

[59] *E.g.,* Burchfield v. Bevans, 242 F.2d 239 (10th Cir. 1957); Century Indem. Co. v. Kofsky, 115 Conn. 193, 161 Atl. 101 (1932). Proration has even been allowed in one state court where the insurer interplead *before* all claims had been adjudicated, Underwriters for Lloyds v. Jones, 261 S.W.2d 686 (Ky. 1953); *but see,* Burchfield v. Bevans, 242 F.2d 239, 243 (10th Cir. 1957).

[60] Tashire v. State Farm Fire & Cas. Co., 363 F.2d 7 (9th Cir. 1966).

[61] State Farm Fire & Cas. Co. v. Tashire, 35 U.S.L. WEEK 3110 (U.S. Oct. 11, 1966).

[62] *Cf.,* F. D. Cline Paving Co. v. Southland Speedways, Inc., 250 N.C. 358, 108 S.E.2d 641 (1959). It is, of course, a stretched analogy to call the driver a debtor, the plaintiffs creditors, and the owner a surety who is seeking to have the debtor's agent, the insurer, apply funds ratably between debts on which the owner is also liable and debts on which the driver is liable alone, particularly where there is not one creditor but three. Normally, where there is a voluntary payment, the debtor or creditor may apply the proceeds as desired.

dismissal was quite improper precisely because the owner's interest cannot be protected by any court at this stage of the litigation. What the above analysis overlooks is the fundamental fact that the question of indispensability was raised, not at the original suit against the driver, but at the declaratory judgment proceeding against the insurer. If the issue had been raised at Lynch's original action in federal court before he obtained his judgment against the driver, Lynch would then have been sent back to the state court for lack of diversity and presumably he would have been forced to get a judgment along with the other plaintiffs. In that situation, the insurance fund could have been apportioned. But raising the problem at this stage is futile, because Lynch has already won the race to judgment and is already entitled to priority in the fund over the state court plaintiffs who have yet to get a judgment against the owner. The state court plaintiffs have thus *lost* their rights to share equally in the fund, and likewise, the owner has lost his right to equal protection from it. It is probable, then, that both a federal *and* a state court would be legally required to *refrain* from "protecting" the owner and the plaintiff suing him. Thus, clearly a ruling at this late stage that the owner is indispensable because of a potential loss of protection is patently erroneous—legally, he *cannot* be protected in any court.

The same conclusion can be reached by a far simpler and more obvious route, however, if the question initially raised is not *how* to protect the owner, but whether he *needs* protection in the first place. The only argument for giving the owner priority in the funds of his own policy is that he has paid the premiums and thus ought to have first claim on their proceeds. But the entire insurance fund will ultimately be paid out on his behalf, no matter how it is distributed to each claimant. The owner will have the full benefit of the policy, for he is liable in any event for injury caused by the driver and his premiums give him protection against that liability. Thus, if the Court were to reduce Lynch's share of the fund by one-half, it is true that the owner would have that much more to apply to claims against him arising out of the state court actions. But it is also clear that Lynch would now pursue the owner for the other half of his original judgment, and the owner would have gained nothing in the end. In other words, any proceeds paid out now from the policy will eventually go to reduce the owner's ultimate

liability. The only situation where the owner could gain from a proration would be if the driver were solvent and could himself pay that portion of Lynch's judgment not collectible from the insurance fund.[63] In this case, the entrance of a default judgment against the driver's estate would seem to indicate that it is insolvent; even if it were not, however, the legal roadblocks to proration discussed above still face the court. The problem, then, of finding a way to protect the absent owner is largely irrelevant, for he probably is not subject to injury to start with. And if he cannot be adversely affected by a judgment, quite obviously he is not indispensable.

While many of these difficulties may never have occurred to either the majority or the dissent, there can be no question that rule 19, old or new, calls for their recognition. The irony of *Provident Tradesmens* is that the revised rule's emphasis on shaping imaginative relief to protect absent parties led both the majority and the dissent away from ever inquiring whether the owner needed protection in the first place—the very error the old rule was primarily revised to correct.

Because of the court's sweeping, contradictory language and the potential disparity between those consequences considered and those overlooked, it is difficult to state precisely the effect of *Provident Tradesmens*. Because of the uncertain need for, or legality of, any protective decree that might have been shaped for the absent party, it is equally hard to judge what should have been the proper decision, were the new rule definitely applicable. Perhaps the fairest conclusion is that the court did balance some competing factors which were based on an inadequate view of the facts, deciding a state court was the more proper forum to deal with many of the difficulties of relief that in actuality were probably more illusory than real. It is just as fair to say, however, that the court indicates in no uncertain terms its unwillingness to sanction any injury to an absent party no matter how strongly other considerations call for proceeding with the action. Unfortunately, the case did not provide the best factual context for testing the second reading of the rule because the owner probably does not need any protection and thus, necessarily, could not be adversely affected by the declaratory

[63] If the driver had unlimited personal funds, of course, there would be absolutely no possibility at all of adversely affecting the owner's interest no matter how the insurance funds are paid out, for he would then be able to satisfy his right of indemnity against the driver.

judgment. Indeed, the litigation was too far advanced to warrant any constructive interference, either to find some injury that required protection or to send the case back to the state courts where it, perhaps, belonged from the start. The court should have considered the indispensability question waived as the Federal Rules clearly provide.[64]

C. B. GRAY

Conflicts—Forum Non Conveniens in North Carolina

The plaintiff with a transitory cause of action[1] has available a wide selection of forums for suit, limited only by considerations of obtaining service of process.[2] Hence, a defendant often finds himself fortuitously subjected to suit in a forum highly inappropriate for the conduct of his defense and without legitimate counter-balancing advantage to the plaintiff. To combat this unnecessary and oppressive burden in particular cases, courts and legislatures have devised various means by which the plaintiff is precluded from prosecuting his suit within certain inconvenient forums.[3] The doc-

[64] The Supreme Court has granted certiorari, 35 U.S.L. WEEK 3303 (U.S. Feb. 28, 1967) (no. 806).

[1] "Actions are transitory when the transactions on which they are based might take place anywhere, and are local when they could not occur except in some particular place." Brady v. Brady, 161 N.C. 325, 326, 77 S.E. 235, 236 (1913); Bunting v. Henderson, 220 N.C. 194, 16 S.E.2d 836 (1941). "[B]ecause of the history and forms of the common law, there are certain actions which are safely brought only in a particular locality. These are called local actions, and all others are transitory." Currie, *The Constitution and the Transitory Cause of Action,* 73 HARV. L. REV. 36, 66 (1959).

[2] In transitory actions the defendant may be sued in any jurisdiction where he may be found. McDonald v. MacArthur Bros. Co., 154 N.C. 122, 69 S.E. 832 (1910). Common law venue rules were designed to obtain jurisdiction over evasive defendants. See generally Foster, *Place of Trial in Civil Actions,* 43 HARV. L. REV. 1217 (1930). Note recent expansion of jurisdiction over defendants. *E.g.,* International Shoe Co. v. Washington, 326 U.S. 310 (1945); Gray v. American Radiator & Standard Sanitary Corp., 22 Ill. 2d 432, 176 N.E.2d 761 (1961).

[3] Congress has enacted a statute, 28 U.S.C. § 1404(a) (1964), which provides: "For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought." See generally Comment, 8 STAN. L. REV. 388 (1956), for a discussion of the statute's effect and scope, as well as references to numerous other periodical comments. As to actions in sister states to enjoin the plaintiff from proceeding in the inappropriate forum, see generally Messner, *The Jurisdiction of a Court of Equity Over Persons to Compel the Doing of Acts Outside the Territorial*

trine of *forum non conveniens* has been one of the most successful methods of affording this relief for defendants.[4]

The doctrine of *forum non conveniens* appears to have been first enunciated in the Scottish courts,[5] and was practiced occasionally in American courts during the 19th century.[6] The doctrine allows the trial court discretionary power to decline the hearing of a transitory cause of action if the forum is inappropriate for the trial.[7] However, it is not applicable unless there are at least two forums available to the plaintiff, the doctrine then providing the criterion for the choice between them.[8]

General application of *forum non conveniens* in state courts has not taken place until recent years.[9] Slow development of the doctrine

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Limits of the State, 14 MINN. L. REV. 494, 495-506 (1930); Comment, 29 U. CHI. L. REV. 740 (1962); Note, 27 IOWA L. REV. 76 (1941). The commerce clause of the U.S. Constitution has been used to restrain the plaintiff's choice of forum. See, *e.g.*, Denver & R.G.W.R.R. v. Terte, 284 U.S. 284 (1932); Davis v. Farmers' Co-op. Co., 262 U.S. 312 (1923). See generally Dainow, *The Inappropriate Forum*, 29 ILL. L. REV. 867 (1935) [hereinafter cited as Dainow]; Comment, 46 COLUM. L. REV. 643 (1946).

[4] See generally GOODRICH, CONFLICT OF LAWS 15 (4th ed. 1964); Barrett, *The Doctrine of Forum Non Conveniens*, 35 CALIF. L. REV. 380 (1947) [hereinafter cited as Barrett]; Blair, *The Doctrine of Forum Non Conveniens in Anglo-American Law*, 29 COLUM. L. REV. 1 (1929); Braucher, *The Inconvenient Federal Forum*, 60 HARV. L. REV. 908 (1947); Comment, 42 CALIF. L. REV. 690 (1954); Comment, 29 U. CHI. L. REV. 740 (1962); Comment, 1964 U. ILL. L.F. 646.

[5] See, *e.g.*, La Société du Gaz de Paris v. La Société Anonyme de Navigation "Les Armateurs français," [1925] SESS. CAS. 332 (Scot. 2d Div.), *aff'd*, [1926] Ses. Cas. 13 (H.L.), where the lower court discusses fully the development of *forum non conveniens* in Scotland; Brown v. Cartwright, 20 Scot. L.R. 818 (1883).

[6] See, *e.g.*, Pierce v. Equitable Life Assur. Soc'y, 145 Mass. 56, 12 N.E. 858 (1887); Gardner v. Thomas, 14 Johns. 134, 7 Am. Dec. 445 (N.Y. 1817); Morris v. Missouri Pac. Ry., 78 Tex. 17, 14 S.W. 228 (1890).

[7] Application of the doctrine has been more narrowly restricted in contract actions than tort due in part to the more consistent rules of damages in contract actions among jurisdictions. See Rhodes v. Barnett, 117 F. Supp. 312, 316 (S.D.N.Y. 1953); Anderson v. Delaware, L. & W.R.R., 18 N.J. Misc. 153, 11 A.2d 607 (Cir. Ct. 1940). In admiralty the doctrine is of long standing. See Swift & Co. Packers v. Compania Colombiana Del Caribe, S.A., 339 U.S. 684 (1950). Where problems of service of process or the statute of limitations will be confronted by plaintiff in the foreign forum, state courts often condition the dismissal on defendants acceptance of service of process or waiver of the statute of limitations bar. See Wendel v. Hoffman, 259 App. Div. 732, 18 N.Y.S.2d 96 (1940). "While the plaintiff ordinarily controls choice of the forum, a court does not exercise jurisdiction if it is a seriously inappropriate forum for the trial of the action so long as an appropriate forum is available to the plaintiff." RESTATEMENT (SECOND), CONFLICT OF LAWS § 117(e) (Tent. Draft No. 4, 1957).

[8] Gulf Oil Corp. v. Gilbert, 330 U.S. 501, 506-07 (1947).

[9] In 1947, Barrett was able to state that the doctrine was accepted "in

is in part attributable to an interpretation of the privileges and immunities clause of Article IV of the United States Constitution[10] that would prohibit states from declining jurisdiction over cases where nonresidents are parties.[11] The Supreme Court has never spoken directly on point,[12] but recent widespread acceptance of the

barely half a dozen states." Barrett 389. Whereas, Trautman in 1960 stated that the Washington Supreme Court by recently rejecting the doctrine had placed itself in the minority. Trautman, *Forum Non Conveniens in Washington—A Dead Issue?*, 35 WASH. L. REV. 88, 93 (1960) [hereinafter cited as Trautman].

States accepting *forum non conveniens* or having indicated approval of the doctrine are: *Arkansas,* Running v. Southwest Freight Lines, 227 Ark. 839, 303 S.W.2d 578 (1957); *California,* Price v. Atchison, T. & S.F. Ry., 42 Cal. 2d 577, 268 P.2d 457 (1954); *Delaware,* Dietrich v. Texas Nat'l Petroleum Co., 193 A.2d 579 (Del. Super. Ct. 1963); *District of Columbia,* Byrd v. Southern Ry., 203 A.2d 37 (D.C. Ct. App. 1964); *Florida,* Atlantic Coast Line R.R. v. Cameron, 190 So. 2d 34 (Fla. Dist. Ct. App. 1966); *Illinois,* People *ex rel.* Chesapeake & O. Ry. v. Donovan, 30 Ill. 2d 178, 195 N.E.2d 634 (1964); *Indiana,* Hartunion v. Wolflick, 125 Ind. App. 98, 122 N.E.2d 622 (1954); *Iowa,* Bradbury v. Chicago, R.I. & P. Ry., 149 Iowa 51, 128 N.W. 1 (1910); *Kansas,* Gonzales v. Atchison, T. & S.F. Ry., 189 Kan. 689, 371 P.2d 193 (1962); *Louisiana,* Union City Transfer v. Fields, 199 So. 206 (La. Ct. App. 1940); *Maine,* Foss v. Richards, 126 Me. 419, 139 Atl. 313 (1927); *Maryland,* Texaco, Inc., v. Vanden Bosche, 242 Md. 334, 219 A.2d 80 (1966); *Massachusetts,* Universal Adjustment Corp. v. Midland Bank, Ltd., 281 Mass. 303, 184 N.E. 152 (1933); *Minnesota,* Johnson v. Chicago, B. & Q.R.R., 243 Minn. 58, 66 N.W.2d 763 (1954); *Mississippi,* Strickland v. Humble Oil & Ref. Co., 194 Miss. 194, 11 So. 2d 820 (1943); *Missouri,* Loftus v. Lee, 308 S.W.2d 654 (Mo. 1958); *New Hampshire,* Jackson & Sons v. Lumbermen's Mut. Cas. Co., 86 N.H. 341, 168 Atl. 895 (1933); *New Jersey,* Wangler v. Harvey, 41 N.J. 277, 196 A.2d 513 (1963); *New York,* De La Bouillerie v. DeVienne, 300 N.Y. 60, 89 N.E.2d 15 (1949); *Oklahoma,* St. Louis-San Francisco Ry. v. Superior Court, 290 P.2d 118 (Okla. 1953); *Oregon,* Horner v. Pleasant Creek Mining Corp., 165 Ore. 683, 107 P.2d 989 (1940); *Pennsylvania,* Plum v. Tampax, Inc., 399 Pa. 553, 160 A.2d 549 (1960); *Texas,* Flaiz v. Moore, 359 S.W.2d 872 (Tex. Sup. Ct. 1962); *Utah,* Mooney v. Denver & R.G.W.R.R., 118 Utah 307, 221 P.2d 628 (1950); *Vermont,* Wellman v. Mead, 93 Vt. 322, 107 Atl. 396 (1919); *Wisconsin,* Lau v. Chicago & N.W. Ry., 14 Wis. 2d 329, 111 N.W.2d 158 (1961).

[10] U.S. CONST. art. IV, § 2, cl. 1. "The citizens of each State shall be entitled to all privileges and immunities of citizens in the several States."

[11] This interpretation seems to have originated from the early case of Corfield v. Coryell, 6 Fed. Cas. 546 (No. 3230) (C.C.E.D. Pa. 1823), where Justice Washington by dictum concluded that access to a state court is a fundamental right protected by the clause. Succeeding cases seem to have approved the dictum. See, *e.g.,* Miles v. Illinois Cent. R.R., 315 U.S. 698, 704 (1942); Chambers v. Baltimore & O.R.R., 207 U.S. 142, 148 (1907).

[12] In applying *forum non conveniens,* several courts have taken the position that any such discrimination is based on residence not citizenship, thus not violating the constitutional clause. Robinson v. Oceanic Steam Nav. Co., 112 N.Y. 315, 19 N.E. 625 (1889); Loftus v. Pennsylvania Rd. Co., 107 Ohio St. 352, 140 N.E. 94 (1923); Central R.R. v. Georgia Co., 32 S.C.

doctrine in state forums indicates a present belief by the judiciary that the constitutional provision is not violated so long as there is no arbitrary denial of forum access to noncitizens.

The application of *forum non conveniens* in the federal courts was conclusively sanctioned in 1947 by the Supreme Court in *Gulf Oil Corp. v. Gilbert.*[13] The Court affirmed the dismissal by the District Court for the Southern District of New York of suit brought by a Virginia resident for damages against a Pennsylvania corporation for a tortious act committed in Virginia. The Court spelled out certain factors, not exclusive, to be considered in the denial or grant of this relief. They included factors of public interest such as administrative difficulties and burdens of jury duty, as well as the private interests of the litigant involved, such as access to sources of proof and availability of witnesses.[14] The Court noted: "The principle of *forum non conveniens* is simply that a court may resist imposition upon its jurisdiction even when jurisdiction is authorized by the letter of a general venue statute."[15]

Following the decision in *Gulf Oil Corporation,* Congress enacted a statute authorizing federal courts to transfer a civil action to any other district where it might have been brought for the "convenience of parties and witnesses, in the interest of justice."[16] This statute has substantially reduced the need for the doctrine of *forum non conveniens* in federal courts.[17]

Decisions in North Carolina either referring to or applying the principle of *forum non conveniens* are few. Various pronouncements of the court have confirmed the right of non-citizens to sue in North Carolina courts, citing the privilege and immunity clause of the Constitution.[18] These cases have been judicially interpreted else-

319, 11 S.E. 192 (1890). This reasoning appears to have been accepted by the Supreme Court in Douglas v. New York, N.H. & H.R.R., 279 U.S. 377 (1929).

[13] 330 U.S. 501 (1947).

[14] For a thorough discussion of various factors considered by courts see Annot., 90 A.L.R.2d 1109, 1112 (1963); Annot., 48 A.L.R.2d 800, 814 (1956).

[15] 330 U.S. at 507.

[16] 28 U.S.C. § 1404(a) (1964). See note 3 *supra.* In Norwood v. Kirkpatrick, 349 U.S. 29 (1955), the Court noted that since under the statute transfer, not dismissal, resulted, a lesser showing of inappropriateness was necessary than that required by *forum non conveniens.*

[17] The doctrine may still be applicable where international parties are involved. Mobil Tankers Co., S.A. v. Mene Grand Oil Co., 236 F. Supp. 362 (D. Del. 1964).

[18] *E.g.,* Howle v. Twin State Express, Inc., 237 N.C. 667, 75 S.E.2d 732

where as placing North Carolina in a group of jurisdictions rejecting *forum non conveniens*.[19] This interpretation is questionable in that the court in these decisions faced solely the issue of a non-citizen's access to North Carolina courts.

Also inconsistent with rejection of *forum non conveniens* was North Carolina's general application of the corporation internal affairs rule.[20] Under this rule the court refused to interfere with the internal management of business matters of foreign corporations, thereby referring the plaintiff to the foreign forum.[21] However, the North Carolina legislature passed a statute in 1955 prohibiting state courts from dismissing actions solely because they involve the internal affairs of a foreign corporation.[22] The legislature recognized the courts' discretion to dismiss the action but directed that other factors such as convenience of the parties and ability to grant adequate relief be considered by the court. The authors of the statute commented:

> While the doctrine of nonintervention in the internal affairs of a foreign corporation is still frequently asserted, the courts have increasingly taken jurisdiction in cases which that doctrine would seem to deny. At this date it is believed that a test more nearly approaching 'forum non-conveniens' should govern the court's

(1953); McDonald v. MacArthur Bros. Co., 154 N.C. 122, 69 S.E. 832 (1910).

[19] Barrett 388 n.40; Currie & Lieberman, *Purchase-Money Mortgages and State Lines: A Study in Conflict-of-Laws Method,* 1960 DUKE L.J. 1, 9 n.28; Trautman 94 n.22.

[20] See Reid v. Norfolk Southern R.R., 162 N.C. 355, 78 S.E. 306 (1913); Brenizer v. Royal Arcanum, 141 N.C. 409, 53 S.E. 835 (1906); Howard v. The Mutual Reserve Fund Life Ass'n, 125 N.C. 49, 34 S.E. 199 (1899); *cf.* Belk v. Belk's Dep't Store, Inc., 250 N.C. 99, 108 S.E.2d 131 (1959).

[21] The internal affairs rule has now been essentially absorbed into the doctrine of *forum non conveniens* in most jurisdictions. See Koster v. Lumbermen's Mut. Cas. Co., 330 U.S. 518 (1947); see generally Note, *Forum Non Conveniens as a Substitute for the Internal Affairs Rule,* 58 COLUM. L. REV. 234 (1958).

[22] N.C. GEN. STAT. § 55-133(a) (1965), which provides:

> No action in the courts of this State shall be dismissed solely on the ground that it involves the internal affairs of a foreign corporation but the court may in its discretion dismiss such an action if it appears that *more adequate relief can be granted* or that the *convenience of the parties would be better served* by an action brought in the jurisdiction of its incorporation or in the jurisdiction where the corporation has its executive or managerial headquarters or, because of the circumstances, in some other jurisdiction.

(Emphasis added.)

decision and that a statute making that apparent would represent a sound innovation.[23]

In 1949, the legislature enacted a statute specifically granting North Carolina courts discretion to dismiss any civil action over which such court has jurisdiction for the convenience of parties and witnesses and in the interest of justice, provided that the cause of action arose out of the state and both the plaintiff and defendant are nonresidents.[24] The question remains open as to whether the statute will preclude the dismissal of actions where one or both of the parties are residents, or the cause of action arose within the state. When faced with the issue our court may well interpret the statute as limiting rather than enabling, thereby holding that lower courts are prohibited from dismissing cases because of inconvenient forum unless the prerequisites specified in the statute are met. This would be an unfortunate though quite legitimate interpretation.

"For the convenience of parties and witnesses and in the interest of justice,"[25] trial courts should retain the discretion to dismiss actions brought before the inappropriate forum. To view N.C. GEN. STAT. § 1-87.1 (1953), as an enabling statute embodying the principle of *forum non conveniens* for use in the more obviously appropriate circumstances would be consistent with efficient administration of justice and the general purpose of the statute.

The North Carolina Supreme Court has recognized the right of lower courts to dismiss actions over which they have jurisdiction in numerous instances by application of the internal affairs rule.[26] Many of these cases involved residents as parties.[27] Likewise, the legislature has recognized this same discretion of lower courts by

[23] Belk v. Belk's Dep't Store, Inc., 250 N.C. 99, 105, 108 S.E.2d 131, 136 (1959).

[24] N.C. GEN. STAT. § 1-87.1 (1953), which provides:

For the convenience of parties and witnesses and in the interest of justice, any judge of any court in this State may dismiss without prejudice any civil action over which such court has jurisdiction if the court shall find that:

(1) The cause of action arose out of the State, and

(2) The defendant is a nonresident of this State, and

(3) The plaintiff is a nonresident of this State or the deceased person in behalf of whose estate the action has been instituted was at the time of his death a nonresident of this State.

[25] *Ibid.*

[26] See note 20 *supra* and accompanying text.

[27] Reid v. Norfolk Southern R.R., 162 N.C. 355, 78 S.E. 306 (1913); Brenizer v. Royal Arcanum, 141 N.C. 409, 53 S.E. 835 (1906); Howard v. The Mutual Reserve Fund Life Ass'n, 125 N.C. 49, 34 S.E. 199 (1899).

its enactment of N.C. GEN. STAT. § 55-133 (1965), which acknowledged the courts' practice in corporate affairs cases, directing only that other factors be taken into consideration in its application. Note that N.C. GEN. STAT. § 55-133 (1965) was enacted *later* in time than N.C. GEN. STAT. § 1-87.1 (1953), arguably signifying that the legislature did not intend to limit the court's right to dismiss an action over which it has jurisdiction. Therefore, to recognize this same discretion to dismiss an action not prescribed in N.C. GEN. STAT. § 1-87.1 (1953), on the basis of inconvenient forum would have ample precedent by the courts' application of the internal affairs rule.

To limit the doctrine of *forum non conveniens* to the prerequisites of N.C. GEN. STAT. § 1-87.1 (1953) may be unfavorably discriminatory to residents. Suppose, for example, a Florida resident brings an action in North Carolina against a North Carolina corporation doing substantial business in Florida for a tortious act committed in Florida. Assume that due to difficulties of evidence the corporation can present a successful defense only in the Florida forum. Under a literal interpretation of N.C. GEN. STAT. § 1-87.1 (1953), the corporation will be forced to defend in the North Carolina court.[28] However, if the defendant were a Virginia corporation the court could dismiss the action, thereby encouraging a hearing in the more convenient forum.

Jurisdictions that will dismiss actions wherein a resident is a party, by application of the doctrine of *forum non conveniens,* are few indeed.[29] Without question these factors weigh heavily in favor of retaining the action within the forum. The North Carolina statute reflects an enlightened policy in its adoption of the principles of *forum non conveniens* for actions meeting the prescribed conditions. Nevertheless, North Carolina can only enhance its reputation for efficient administration of justice by allowing its lower courts

[28] This assumes that North Carolina will consider the act of incorporation in the particular case within the state as constituting legal residence. Where a domestic corporation is doing nation-wide business, it would not be uncommon for its legal residence to be a particularly unattractive forum for various suits.

[29] Excluding instances where the internal affairs rule was applicable, research revealed only four jurisdictions within the United States having ruled on point. Winsor v. United Air Lines, Inc., 154 A.2d 561 (Del. Super. Ct. 1958); Giseburt v. Chicago, B. & Q.R.R., 45 Ill. App. 2d 262, 195 N.E.2d 746 (1964); Gonzales v. Atchison, T. & S.F. Ry., 189 Kan. 689, 371 P.2d 193 (1962); Gore v. United States Steel Corp., 15 N.J. 301, 104 A.2d 670, *cert. denied,* 348 U.S. 861 (1954).

to exercise discretion beyond that specified by statute in the disposition of actions brought before an inappropriate forum. The court should be free to relieve a harassed defendant and to encourage litigation in a forum better suited to a just result.

GERALD M. MAYO

Constitutional Law—First Amendment Protection of the Right to Demonstrate—the "New" Limitations

Petitioners in *Adderley v. Florida*[1] were among a group of students engaged in integration efforts in Leon County, Florida. On the day following the arrest of some of their fellows, approximately two hundred students including the thirty-two petitioners marched to the Leon County jail. There they stood and sat upon the jail premises, dancing, singing and clapping. In so doing they partially obstructed a jail entrance and a jail driveway used by the sheriff and his officers to transport prisoners, and by tradesmen servicing the jail but not generally by the public. The sheriff, after notifying the demonstrators that he was the legal custodian of the jail, ordered them to leave or be arrested for trespass. Many left, but 107 remained and were arrested. This included petitioners, who were convicted of a violation of a Florida trespass statute.[2] After the Florida appellate court denied rehearing,[3] the Supreme Court granted certiorari.[4] Upon hearing, a five justice majority determined that the convictions should be affirmed. The opinion, written by Justice Black, made it clear that otherwise valid state trespass convictions under properly worded statutes, nondiscriminatorily applied, will not be invalidated because the purpose of the trespass was the assertion of civil rights, and that in the case of trespass on public lands, the court will test the propriety of regulation, not by the purpose[5] of the trespass, but by the *use* to which the property is dedicated.

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[1] 385 U.S. 39 (1966).

[2] FLA. STAT. ANN. § 821.18 (1965). "Every trespass upon the property of another, committed with a malicious and mischievous intent, the punishment of which is not specifically provided for, shall be punished by imprisonment not exceeding three months, or by fine not exceeding one hundred dollars."

[3] Adderley v. State, 175 So. 2d 249 (Fla. 1965) (per curiam).

[4] Adderley v. Florida, 382 U.S. 1023 (1966).

[5] *I.e.* "To petition . . . for redress of grievances," U.S. CONST. amend. I.

The affirmance of this conviction no doubt came as a surprise to many, as it is the first Supreme Court decision upholding such a conviction in the short but turbulent history of sit-in cases.[6] This absence of affirmances seems to have given rise to a largely unarticulated belief[7] that essentially all demonstrations against governmental policy on state property are protected against state prosecution by the first amendment as made applicable to states by the due process clause of the fourteenth amendment.[8] A similar belief has arisen that in cases involving demonstrations against racial segregation, any prosecution is invalid as state action enforcing unequal treatment of the races,[9] and therefore a violation of the equal protection clause of the fourteenth amendment.[10] But no holding by the Court fully supported either of these beliefs or squarely refuted them. Indeed these questions had seldom been reached. In no case prior to *Adderley* had the majority of the Court found that the record made out an otherwise valid conviction under an otherwise constitutional statute properly applied, as may be seen by a brief review of the leading sit-in cases.

In *Garner v. Louisiana*,[11] the first sit-in case to reach the Supreme Court, petitioners, peaceful participants in sit-ins at the "white" lunch counters of privately owned businesses, were charged with a breach of the peace. Petitioners presented to the court, among other contentions, the equal protection argument, based on the aid of the criminal law in the maintenance of segregation.[12] The Chief

[6] While in Drews v. Maryland, 381 U.S. 421 (1965), the Court did not overturn the disorderly conduct convictions of four sit-in demonstrators tried before passage of the Public Accommodations Law, 78 Stat. 243, 42 U.S.C.A. §§ 2000(a)-2000(a)(6) (1964), but who appealed after its passage, the Court refused review in a memorandum which gave neither indication of its grounds nor holding as to the validity of such convictions.

[7] This belief is evidenced by the contention of petitioners in the principal case, "that they had a constitutional right to stay on the property over the jail custodian's objections," 385 U.S. at 47; and by the premise of Justice Douglas's dissenting opinion that the jailhouse, as "one of the seats of government . . . is an obvious center of protest." *Id.* at 49 (dissenting opinion of Douglas, J.).

[8] Edwards v. South Carolina, 372 U.S. 229 (1963); Whitney v. California, 274 U.S. 357 (1927); Gitlow v. New York, 268 U.S. 652 (1925).

[9] See, Bell v. Maryland, 378 U.S. 226, 242-60, 286-318 (1964) (concurring opinions of Douglas, J., and Goldberg, J.). While this question was not squarely before the Court in the principal case, its relevance to the decision will be discussed below.

[10] See, Civil Rights Cases, 109 U.S. 3 (1883).

[11] 368 U.S. 157 (1961).

[12] *Id.* at 163.

Justice, for the majority, found it "unnecessary to reach the broader constitutional questions presented,"[13] and reversed the case on the ground that the record did not disclose "any evidence which would support a finding that the petitioners' acts caused a disturbance of the peace."[14] Therefore, the Court held the convictions were without due process of law.[15]

A 1963 case, *Edwards v. South Carolina*,[16] presented an appropriate fact situation for testing the applicability of first amendment protection to demonstrations. These defendants were arrested for breach of the peace while holding a non-violent demonstration on the state capitol grounds as an expression of their grievances regarding state policies. Here the Court came closer to reaching the broad issues. It found that the first amendment rights to peacefully assemble and petition government were indeed infringed, but made it clear that: "We do not review in this case criminal convictions resulting from the evenhanded application of a precise and narrowly drawn regulatory statute evincing a legislative judgment that a certain specific conduct will be limited or proscribed."[17] The Court reversed four other 1963 convictions on a finding of forbidden state action without reading the broader issues.[18]

In early 1964 five more sit-in cases were decided by the Court, and in four of them the Court found clear grounds for voiding the judgments without reaching the broad issues.[19] In the other case,

[13] *Id.* at 163.

[14] *Id.* at 163-64.

[15] Thompson v. Louisville, 362 U.S. 199 (1960). The following year, in Taylor v. Louisiana, 370 U.S. 154 (1962), the Court reversed a breach-of-peace conviction arising out of a bus station sit-in by following *Garner*.

[16] 372 U.S. 229 (1963).

[17] *Id.* at 236.

[18] In Avent v. North Carolina, 373 U.S. 375 (1963); Gober v. City of Birmingham, 373 U.S. 374 (1963); and Peterson v. City of Greenville, 373 U.S. 244 (1963), the convictions were in cities having segregation ordinances. In Lombard v. Louisiana, 373 U.S. 267 (1963), an announcement by city officials that sit-ins would not be permitted was held to be sufficient state action to invalidate the conviction, even though the city had no segregation ordinance.

[19] In Bouie v. City of Columbia, 378 U.S. 347 (1964), the Court found a violation of due process in that the statute under which petitioners were convicted did not give them fair warning of the prohibition of their acts. In Robinson v. Florida, 378 U.S. 153 (1964), the Court reversed a conviction arising out of a sit-in in a segregated restaurant on a finding of state action in that a health regulation required separate toilet and lavoratory facilities for the races. In Barr v. City of Columbia, 378 U.S. 146 (1964), violation of due process was found on grounds of a want of evidence to support the charge. The conviction in Griffin v. Maryland, 378 U.S. 130

Bell v. Maryland,[20] a majority of the Court (six justices) actually reached the broad equal protection issue, but divided evenly with three holding that enforcement of a state trespass statute against demonstrators who were ordered to leave because of their race was a discriminatory state action[21] and three that it was not.[22] The other justices favored reversal on other grounds.[23]

Ten days after the decision in *Bell v. Maryland,* the relative importance of the broad unconstitutional state action theory for voiding sit-in convictions lost much of its importance when the Public Accommodations Act[24] became law. The segregation of most potential sit-in sites became illegal, so that police protection of the right to segregate property became largely irrelevant.[25] Therefore, most of the controversy after the enactment of the statute is primarily concerned with the first amendment doctrine that was to become the principal issue in *Adderley.*

This issue was raised twice more in important decisions before *Adderley.* In the *Cox v. Louisiana*[26] decisions, as had been the case in *Edwards,* the facts were ideal for testing the extent to which the first amendment protects the activities of demonstrators. These cases arose out of street demonstrations protesting segregation and the arrest of other demonstrators then held in a jail located in a courthouse across the street from the site of the demonstrations. The leader of these demonstrations was convicted under state statutes prohibiting disturbance of the peace,[27] obstructing public passage-

(1964), was reversed on grounds of unconstitutional state action in that the order excluding Negroes came from a uniformed deputy sheriff.

[20] 378 U.S. 226 (1964).

[21] *Id.* at 242 (opinion of Douglas, J.); *Id.* at 286 (opinion of Goldberg, J.).

[22] *Id.* at 318 (dissenting opinion of Black, J.).

[23] The Maryland legislature had enacted a public accommodations statute, MD. ANN. CODE art. 49B § 11 (Supp. 1963), after the conviction of petitioner but before the decision of the Supreme Court. It was the sense of the three justices that the Court should remand for reconsideration in light of the change in state law.

[24] 78 Stat. 243, 42 U.S.C.A. §§ 2000(a)-(a)(6) (1964), held constitutional in Heart of Atlanta Motel, Inc. v. United States, 379 U.S. 241 (1964) and Katzenbach v. McClung, 379 U.S. 294 (1964).

[25] This is true even as to sit-ins occurring prior to passage of the act, since the Court held on the same day the act was declared constitutional that it brought abatement. Hamm v. City of Rock Hill, 379 U.S. 306 (1964) (5- to -4 decision).

[26] 379 U.S. 536 (1964); 379 U.S. 559 (1965).

[27] LA. REV. STAT. § 14:103.1 (Supp. 1962).

ways[28] and picketing in or near a courthouse.[29] In the first of the *Cox* decisions, the Court reversed the first two of these convictions. But, as in *Edwards,* the basis of reversal was narrow enough to leave questions as to the view of the majority regarding the broad proposition. The Court did hold that by the breach-of-peace conviction Louisiana "infringed appellant's rights of free assembly by convicting him under this statute."[30] In so doing, the Court indicated that the elements of demonstration, including singing, cheering, foot-stamping, and clapping, are protected forms of expression, but tied this determination to a holding that the conviction could not be sustained because:

> The statute . . . as authoritatively interpreted by the Louisiana Supreme Court, is unconstitutionally vague in its overly broad scope . . . [as one element of the crime was] . . . congregating . . . with intent to provoke a breach of the peace, or under circumstances such that a brecah of the peace may be occasioned.[31]

As the Louisiana court in applying this element defined "breach of the peace" as including agitation or arousal from a state of repose, the Supreme Court held that a person might be punished for the peaceful expression of unpopular views, so that his first amendment rights would be infringed.[32] This finding of unconstitutionality for overbreadth prevented the opinion from being of much probative value in seeking a test for the propriety of governmental regulation of demonstrations.

The Court's treatment of the other two charges gave little aid in defining the scope of first amendment coverage of demonstrations. In reversing the conviction for obstructing passageways, the Court stated:

> We emphatically reject the notion urged by appellant that the First and Fourteenth Amendments afford the same kind of freedom to those who would communicate ideas by conduct such as patrolling, marching, and picketing on streets and highways, as these amendments afford to those who would communicate ideas by pure speech.[33]

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[28] LA. REV. STAT. § 14:100.1 (Supp. 1962).
[29] LA. REV. STAT. § 14:401 (Supp. 1962).
[30] Cox v. Louisiana, 379 U.S. 536, 545 (1965).
[31] *Id.* at 551, quoting State v. Cox, 244 La. 1087, 1105, 156 So. 2d 448, 455 (1963).
[32] *Cf.* Terminiello v. Chicago, 337 U.S. 1, 4-5 (1949).
[33] Cox v. Louisiana, 379 U.S. 545, 555 (1965).

But as the application of the statute by city officials was held to be discriminatory, the Court did not reach the broad question. Then, in reversing the conviction for picketing near a courthouse in the second of the *Cox* opinions,[34] the Court made clearer the import of the first opinion that the same standards will not apply in testing the propriety of regulating picketing as in the case of ordinary speech.[35] The Court found that the Louisiana statute was constitutional on its face.[36] However, it found that the application of the statute was a violation of due process, but on grounds so narrow that they have little precedential value beyond the particular facts of the case.[37]

The last of the cases requiring close examination before *Adderley* was *Brown v. Louisiana*,[38] another case presenting an appropriate situation for examination of the application of the first amendment through the fourteenth, and the case in which the prevailing opinion[39] reached the issue most broadly. Petitioners had entered a public library, which some of the evidence indicated practiced segregation. One of them handed the librarian a card bearing the name of a book. The librarian had searched for the book and finding it not to be on her shelves told petitioners that she would order it for them. At this point, the librarian testified, she expected them to leave. Instead, one of petitioners sat down in the only chair in the room, and the others stood around him. After they had refused to leave at the request of the librarian and her superior, the two ladies called the sheriff. He repeated the request, and when petitioners still did not leave arrested them under another clause

[34] Cox v. Louisiana, 379 U.S. 545, 559 (1965).

[35] The Court held that "the fact that free speech is intermingled with . . . conduct does not bring with it constitutional protection," and that the "clear and present danger" test is not necessarily applicable when speech is not in its "pristine form." *Id.* at 564, 566.

[36] The state legislation described by Justice Goldberg as "a valid law, dealing with conduct subject to regulation so as to vindicate important interests of society," *id.* at 564, was modeled on a federal statute, 18 U.S.C. § 1507 (1964), drafted by members of the Supreme Court.

[37] The reversal turned on an entrapment theory based on an "administrative determination" of the meaning of the word "near" by police officials present at the demonstration.

[38] 383 U.S. 131 (1966).

[39] There was no true majority opinion as the five justices supporting reversal spoke in three separate opinions in a 3-1-1 split. The decision of the Court was announced in the opinion of Mr. Justice Fortas joined by the Chief Justice and Justice Douglas. It is to this opinion that the term "prevailing opinion" is applied herein.

of the same breach of the peace statute tested in the first *Cox* opinion. After noting that the conviction was reversible on the same basis of statutory construction as in *Cox,* the opinion went on to express more explicitly than in any other case the view that the first amendment offers a broad protection of expression by physical presence:

> We are dealing here with an aspect of a basic constitutional right—the right under the First and Fourteenth Amendments guaranteeing freedom of speech and of assembly, and freedom to petition the Government for a redress of grievances . . . [T]hese rights are not confined to verbal expression. They embrace appropriate types of action which certainly include the right in a peaceable and orderly manner to protest by silent and reproachful presence . . . the unconstitutional segregation of public facilities.[40]

Thus the prevailing opinion indicated that the first amendment guarantees the right to use the property of others, or at least that of the government, as a platform for the expression by physical demonstration of dissident opinions. This holding, taken in the light of similar but narrower holdings in the *Edwards* and *Cox* decisions, presented the best evidence of the law as to first amendment protection of the right to demonstrate. Protection was to be complete, so long as the demonstrators met two tests: the presence must be for the purpose of expression; and the demonstration must be orderly.

Nine months later came *Adderley v. Florida.* The Court rendered its surprising opinion applying Black's new use test. However, the opinion in *Adderley,* despite the growing definiteness of statement and breadth of protection from *Edwards* to *Cox* to *Brown,* was not actually novel and need not have been surprising, for a line of separate opinions at least two years long had foreshadowed the shape of constitutional doctrines to come. As the pronouncements of the Court became stronger, as the protection of demonstration proved broader, the number of adherents became correspondingly smaller. The clear indications that the Court would one day greatly restrict the constitutional protection of expression by trespass began with the dissenting opinion in *Bell v. Maryland,*[41] over two years before *Adderley.*

[40] Brown v. Louisiana, 383 U.S. 131, 141-42 (1966).

[41] The contention that petitioners had a constitutional right to enter

It is true that the major issue in *Bell* was the applicability of the equal protection clause of the fourteenth amendment to use of state criminal laws in cases of sit-ins in segregated establishments. But it is equally true that petitioners raised the due process-First amendment aspect of the fourteenth, and that the dissent dealt specifically with the issue. Justice Black, speaking for himself and Justices White and Harlan, described the argument as coming down to this:

> That since petitioners did not shout, obstruct Hooper's business . . . , make speeches, or display picket signs, handbills, or other means of communication, they had a perfect constitutional right to assemble and remain . . . over the owner's continuing objections, for the purpose of expressing themselves by language and demonstrations. . . .[42]

Significantly Justice Black's rewording of petitioners' argument bears striking resemblance to the test prescribed in *Brown,* and significantly he resoundingly rejected it.[43] Though this case is not directly parallel to *Adderley* since the demonstration in *Bell* occurred on private property, this dissent is a clear rejection of the liberal protection doctrine over two years before the *Adderley* decision.

Then in *Cox,* four justices rejected the broad first amendment view. Justice Black, while concurring in the reversal of the breach-of-peace and obstructing-public-passageways convictions, did so solely on the basis of constitutional impropriety of the particular statutes in the case. He felt that the first statute[44] was violative of due process as it was broad, vague and not so narrowly drawn as to assure nondiscriminatory application, and so was constitutionally invalid under the holding in *Edwards.* Black made it clear, though, that this narrow basis was his only ground for concurring, and that his joining in the opinion in *Edwards* had never indicated that he accepted the broad view of first amendment protection of demonstrations, as he wrote:

> or to stay on Hooper's premises against his will because, if there, they would have had a constitutional right to express their desire . . . is a bootstrap argument. The right to freedom of expression is a right to express views—not a right to force other people to supply a platform or a pulpit.

Bell v. Maryland, 378 U.S. 226, 345 (1964) (dissenting opinion of Black, J.).

[42] *Id.* at 344.

[43] *Id.* at 345.

[44] LA. REV. STAT. § 14:103.1 (Supp. 1962).

> *Edwards* . . . as I understand it, did not hold that either private property owners or the States are constitutionally required to supply a place for people to exercise freedom of speech or assembly. . . . What *Edwards* as I read it did hold, and correctly I think, was not that the Federal Constitution prohibited South Carolina from making it unlawful for people to congregate, picket, and parade on or near that State's capitol grounds, but rather that in the absence of a clear, narrowly drawn, nondiscriminatory statute prohibiting such gatherings and picketing, South Carolina could not punish people for assembling at the capitol to petition for redress of grievances.[45]

Also, while Black concurred in reversing the conviction under the obstructing-public-passageways statute,[46] he did so on grounds that the statute, because of exclusions therein, was discriminatory,[47] and he made it clear that this did not indicate any weakening of his views as to the broad proposition.[48]

The other two dissenters from *Bell,* White and Harlan, reiterated their belief that conduct is not so protected by the first amendment as is speech. In a joint opinion written by White, they concurred in reversal of the breach-of-peace conviction, but did so saying: "I do not agree with everything the Court says concerning the . . . conviction, particularly its statement concerning the unqualified protection to be extended to Cox's exhortations to engage in sit-ins. . . ."[49] These two justices dissented in the reversal of the obstructing-passageways conviction, agreeing with Black that a properly drawn statute can be used to regulate picketing and marching, and finding that the Louisiana statute was not discriminatory or improperly drawn.

In addition to the reiteration of position by the dissenters from *Bell, Cox* brought an increase in their number as Justice Clark,[50]

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[45] Cox v. Louisiana, 379 U.S. 536, 578-79 (1965) (separate opinion of Black, J.).

[46] LA. REV. STAT. 14:100.1 (Supp. 1962).

[47] *Cf.,* New Negro Alliance v. Sanitary Grocery Co., 303 U.S. 552, 561 (1938).

[48] "I have no doubt about the general power of Louisiana to bar all picketing on its streets and highways. Standing, patrolling, or marching back and forth is conduct, not speech, and as conduct can be regulated and prohibited." Cox v. Louisiana, 379 U.S. 536, 581 (1965) (separate opinion of Black, J.).

[49] *Id.* at 591. (Separate opinion of White, J.)

[50] Clark had earlier indicated his inclination as he was the lone dissenter in Edwards v. South Carolina, 372 U.S. 229, 238 (1963) (dissenting opinion of Clark, J.).

one of the three not reaching broad issues in *Bell,* filed his separate opinion. He concurred in reversal of the breach-of-peace and obstructing-passageways convictions, but, like Black, did so on narrow grounds, as he stated his agreement with Black on the broader first amendment question.[51]

Finally, in the *Brown* case, the coming of *Adderley* was shown to be not only probable but reasonably certain. Black, in a dissenting opinion for four justices,[52] laid down the interpretation of the first amendment's scope that was to prevail in *Adderley:*

> The First Amendment . . . protects speech, writings, and expression of views in any manner in which they can be legitimately and validly communicated. But I have never believed that it gives any person or group of persons the constitutional right to go wherever they want, whenever they please, without regard to the rights of public or private property or to state law.[53]

After repudiating the broad view of the first amendment, Black set out the "use" test that he would later apply for the majority in *Adderley,* as he distinguished *Brown* from *Cox* on the basis of the sites of the two demonstrations.[54]

While it is true that this foreshadowing of the *Adderley* opinion is still the voice of a four-justice minority, these are not exactly the same four justices who had expressed similar views previously. Justice Stewart, who had not reached the issue in *Bell* and had been with the majority in *Cox,* joined in Black's dissent in *Brown,* placing himself on the side of those who find demonstrations to be outside the scope of general application of the First Amendment. Justice White, who had sided with Black in the earlier decisions, voted with the majority favoring reversal of the *Brown* conviction, but did so in a separate opinion, on narrow factual grounds, making

[51] "I . . . agree with him [Black] that the statute prohibiting obstruction of public passageways is invalid under the Equal Protection Clause. And . . . I arrive at the same conclusion for the same reason on the question regarding the breach of the peace statute." Cox v. Louisiana, 379 U.S. 536, 589 (1965) (separate opinion of Clark, J.).

[52] Brown v. Louisiana, 383 U.S. 131, 151 (1966) (dissenting opinion of Black, J.).

[53] *Id.* at 166.

[54] "Public buildings such as libraries, schoolhouses, fire departments, courthouses, and executive mansions are maintained to perform certain specific and vital functions. Order and tranquility of a sort entirely unknown to the public streets are essential to the normal operation." *Id.* at 157 (dissenting opinion of Black, J.).

clear that he had not changed his view as to the broad proposition.[55]

If Justice White had considered the statute in this case to be properly drawn, and its application properly made, the opinion of Justice Black would have been not the dissent but by the majority. So in *Brown,* nine months before *Adderley,* it became clear that if a case came before the Supreme Court involving conviction of demonstrators under a statute that was clear, narrowly drawn, and nondiscriminatory, a majority of the court[56] was not going to find a violation of the first amendment simply because expression by demonstration was limited. The conviction in *Adderley* was made under such a statute,[57] and the Court reached not a surprising conclusion but the exact result foreshadowed in *Brown.* The five-justice majority voted to uphold the conviction.

Black, now writing for a majority, rejected with great clarity the view that the first amendment offers full protection to expression by physical entry:

> [P]etitioners' argument that they had a constitutional right to stay on the property, over the jail custodian's objections . . . has as its major unarticulated premise the assumption that people who want to propagandize protests or views have a constitutional right to do so whenever and however and wherever they please. That concept of constitutional law [is] vigorously and forthrightly rejected. . . .[58]

Black then announced with equal force the view adopted by the majority. So long as the regulation of the use of state owned property is evenhanded and not directed at the particular views being expressed,[59] the power of the state to bar citizens from its property or restrict them from protest activities while thereon does not con-

[55] Were it clear . . . that lingering in a public library for 10 minutes . . . contravened some explicit statute, ordinance, or library regulation of general application, or even if it were reasonably clear that a 10-minute interlude . . . exceeded what is generally contemplated as a normal use of a public library, I would have difficulty joining in a reversal of this case . . . Nor would I deem the First Amendment to forbid a municipal regulation limiting loafing in library reading rooms. *Id.* at 150 (separate opinion of White, J.).

[56] Justices Black, White, Clark, Stewart, and Harlan.

[57] FLA. STAT. ANN. § 821.18 (1965).

[58] Adderley v. Florida, 385 U.S. 39, 47-48 (1966).

[59] There is not a shred of evidence that this power [of the sheriff to exclude from the jail premises] was exercised . . . because the sheriff objected to what was being sung or said by the demonstrators or because he disagreed with the objectives of their protests. . . . There is no evidence that on any other occasion had similarly large groups

flict with the first amendment, so long as such regulation is consistent with the nature of the property.[60]

The wisdom of Black's opinion may perhaps be best assessed by subjecting it to the examination of dissent, *i.e.* the dissent of Justice Douglas for himself and three other justices.[61] The dissenters insist that the conviction of petitioners infringes their right "to assemble, and to petition the government for a redress of grievances."[62] To support this proposition, Douglas makes much of the fact that the purpose of petitioners' presence was one of expression, asserting that this fact brings it within the scope of first amendment protection.[63] The dissent also deems it important that the sheriff, "well understood the purpose of the rally,"[64] and that the testimony as to the purpose "was not contradicted or even questioned."[65] Yet such language in the dissent does nothing to weaken Black's thesis, nor, in real sense, to even criticize it. Black well knew that the purpose of the trespassers was to express their views. His whole opinion makes that clear, but he and the majority simply found this purpose to be irrelevant. A crime had been committed. A conviction had been obtained that the majority found to be constitutional.[66] That the guiding principles which led the trespassers to violate the statute were believed by them to be of greater virtue than the principles of those who governed the state did not, in the eyes of the majority, take the act out of the scope of the criminal statute or bring it within the scope of the first amendment. Black was even able to cite authority concurred in by three of the dissenters

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. . . been permitted to gather on this portion of the jail grounds for any purpose.

Id. at 47.

[60] Black stated for the majority: "The State, no less than a private owner of property, has the power to preserve the property under its control for the use to which it is lawfully dedicated." *Id.* at 47. "The United States Constitution does not forbid a State to control the use of its own property for its own lawful nondiscriminatory purpose." *Id.* at 48.

[61] *Id.* at 48 (dissenting opinion of Douglas, J., with whom the Chief Justice and Brennan and Fortas, Jj., concur).

[62] U.S. CONST. amend. I.

[63] "There is no question that petitioners had as their purpose a protest against the arrest of Florida A. & M. students for trying to integrate public theatres . . . and state and local policies of segregation. . . ." 385 U.S. at 51 (dissenting opinion of Douglas, J.).

[64] *Id.* at 51 (dissenting opinion of Douglas, J.).

[65] *Id.* at 51.

[66] Even the dissent did not find the statute invalid in its general application.

supporting this proposition.[67] Thus the dissent and the opinion of the majority do not each criticize the reasoning of the other, rather they present two squarely opposed premises. Of the two, Black's thesis seems preferable. The theory of the dissent implies that no entry can be regulated where the trespasser holds dissident views and the person in charge of the premises knows that the trespasser entered to express those views. Justice Douglas's thesis invites a situation in which nurses would have to pick their way among supine demonstrators to attend their patients; in which teachers would have to peer over the signs of pickets to inspect the decorum of their classes; in which jail administrators would be hampered in the transportation of their prisoners by the presence of singing, dancing, shouting crowds. The view of the dissent would find all these and innumerable equally unpalatable eventualities justified by the simple fact that the demonstrators had first notified the custodian of the premises of an intent to express opinion by their presence. The five justices of the majority seem justified in finding this prospect undesirable.

The dissent goes on to complain, in support of the theory that the conviction is violative of the first amendment, that: "[T]he jail-house grounds were not marked with 'NO TRESPASSING!' signs, nor does respondent claim that the public was generally excluded from the grounds. Only the sheriff's fiat transformed lawful conduct into unlawful trespass."[68] Yet as Black pointed out, "the sheriff, as jail custodian, had power . . . to direct that this large crowd of people get off the grounds,"[69] and petitioners were not arrested until the sheriff had twice ordered them to leave and apprised them of his position as custodian of the jail. What greater strength the erection of "no trespassing" signs could have added to this order can go only to the exclusion of the public generally. While it is true that there is no evidence that the public generally was excluded, it is equally true, as Black pointed out, that there was no evidence that any other part of the public had ever held a mass

[67] "The conduct which is the subject of this statute—picketing and parading—is subject to regulation even though intertwined with expression and association." Cox v. Louisiana, 379 U.S. 559, 563 (1964). This opinion was joined by Douglas, Warren, and Brennan. Fortas was not yet on the Court. See, Giboney v. Empire Storage & Ice Co., 336 U.S. 490, 502 (1949). But *cf.*, Thornhill v. Alabama, 310 U.S. 88 (1940).

[68] 385 U.S. at 52.

[69] *Id.* at 46-47.

meeting on the premises or remained there after an order to leave.

Finally, the dissent admits that Black's "use" test for defining the outer limits of the state's power to exclude demonstrators from its premises has validity.[70] But then Douglas goes on to say, "[T]his is quite different from saying that all public places are off limits to people with grievances."[71] Indeed it is quite different, but Douglas has set us a straw man. Black at no point suggests that all public places are or should be off limits. In fact, in distinguishing the principal case from *Edwards,* Black makes clear that this is not his position as he points out that, "Traditionally, state capitol grounds are open to the public. Jails, built for security purposes, are not."[72]

In further attacking the majority opinion, the dissent suggests that the Court's holding would place in the discretion of the custodian of public property the power to determine when the property shall be used to express ideas. This power, Douglas argues, would give the custodian, "the awesome power to decide whose ideas may be expressed, and who shall be denied a place to air their claims and petition their government."[73] However, the power which the majority recognizes as being vested in the custodian is not an unbridled one, nor is it awesome. A custodian may not decide who may express views and who may not. The custodian may only perform his function of administering the property evenhandedly according to its dedicated use.

In short, the majority in the principal case is not announcing a novel doctrine granting a new and frightful power to state employees. Instead, it is rendering a predictable opinion recognizing that the administration of property is impossible if its use by the public is not confined to purposes at least akin to its normal function.

An examination of Black's opinion is not completed by a contrast of constitutional theories. It must be noted that other considerations were in the minds of the majority. These considerations are more fully reflected in Black's dissent in *Brown*[74] than in

[70] "There may be some public places which are so clearly committed to other purposes that their use for the airing of grievances is anomalous. There may be some instances in which assemblies and petition for redress of grievances are not consistent with other necessary purposes of public property." *Id.* at 54.

[71] *Id.* at 54.

[72] *Id.* at 41.

[73] *Id.* at 54.

[74] Brown v. Louisiana, 383 U.S. 131, 151 (1966) (dissenting opinion of Black, J.).

his opinion in *Adderley*. Black and those who joined with him were concerned that a failure to enforce laws against demonstrators was part of a dangerous trend. Their concern is displayed in two statements of the *Brown* dissent. First:

> It is high time to challenge the assumption in which too many people have too long acquiesced, that groups that think they have been mistreated or that have actually been mistreated have a constitutional right to use the public's streets, buildings, and property to protest whatever, wherever, whenever they want, without regard to whom such conduct may disturb.[75]

And the closing statement of the dissent:

> But I say once more that the crowd moved by noble ideals today can become the mob ruled by hate and passion and greed and violence tomorrow. If we ever doubted that, we know it now. The peaceful songs of love can become as stirring and provocative as the Marseillaise did in the days when a noble revolution gave way to rule by successive mobs until chaos set in. The holding in this case today makes it more necessary than ever that we stop and look more closely at where we are going.[76]

The weight of this concern in the formation of the views expressed in this dissent and in the principal case is subject to deep inquiry. Black, the great exponent of first amendment liberties,[77] is apparently reading history and finding the forerunner of the protest demonstration, not in pamphleteering of Thomas Payne or the dissident speaking of Edmond Burke, but in the violent revolutionaries of nineteenth century France. He who long has advocated the first amendment protection of ideas,[78] now fears that this departure from traditional Anglo-American forms of protest will end in mobs unwilling to rest on the merits of their ideas, but bent upon prevailing through the physical strength of their adherents. While the degree to which these fears influenced Black's decision is not subject to exact measurement, they must necessarily be considered by all who would study this opinion and reflect on future decisions.

The effect of this case will certainly be great. Protest demonstra-

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[75] *Id.* at 162.

[76] *Id.* at 168.

[77] See Cahn, *Justice Black and First Amendment "Absolutes": A Public Interview*, 37 N.Y.U.L. REV. 549 (1962).

[78] See, *e.g.*, Feldman v. United States, 322 U.S. 487, 501 (1944) (dissenting opinion of Black, J.).

tion is certainly not dead. But state governments may now be assured that so long as their regulations are clear and narrowly drawn, and so long as their administration is nondiscriminatory, they may protect public property from invasion by demonstrators unless the nature of such property is such that its use for mass assembly is appropriate.[79] Conversely, those who would demonstrate should be warned that in planning their protests they should incline toward the selection of sites in which public assemblies are normal or have previously or traditionally occurred, and where they will not unduly interrupt some administrative or judicial function of government.

It is unclear what effect this opinion will have on cases arising out of civil rights demonstrations in the segregated accommodations of private persons. As indicated above, the view that the first amendment prevented prosecution of demonstrators generally has been held in conjunction with a view that the equal protection clause of the fourteenth protected from prosecution for trespass those who were ordered from the property of others because of their race. This question was not, of course, before the Court in *Adderley*.[80] However, the opinion may be of some aid in predicting the probable result when the question does arise.[81] Since three of the six justices who reached the equal protection issue in *Bell v. Maryland*[82] rejected the demonstrators' arguments, and since these same three, joined by two others, have now found that demonstrators, even on public property, are not insulated from convictions for trespass by the motives behind their entry, it seems likely that future protestors holding sit-ins in establishments not covered by the Public Accommodations Act would certainly not be protected by the first amendment and probably not by the equal protection clause of the

[79] Various parts of Black's opinion suggest that capital grounds, public parks, and to a limited extent the streets are among those places appropriate for demonstration.

[80] Petitioners did raise this issue by claiming that they were entitled to abatement under the doctrine of Hamm v. City of Rock Hill, 379 U.S. 229 (1964), as their protests had been directed toward segregated facilities. The Court found this contention untenable.

[81] There is a greater likelihood of the issue's arising than might at first appear. True, the Public Accommodations Act, 78 Stat. 743, 42 U.S.C.A. §§ 2000(a)-(a)(6) (1964), made segregation of most establishments unlawful. But the act did leave certain exceptions. (*E.g.* sellers of food for off-premises consumption, providers of lodging for transients with accommodations for fewer than six in the residence of the proprietor, possibly operators of participant sports centers).

[82] 378 U.S. 226, 318 (1964) (dissenting opinion of Black, J.).

fourteenth. Therefore those who would urge integration of the remaining lawfully segregated establishments would be well advised to do so by boycott, lawful picketing, or other means not involving the invasion of the segregated property. Otherwise, they run the risk of sustained convictions under clear, narrowly-drawn statutes.

DAVID B. SENTELLE

Constitutional Law—State Cannot Award Damages for Invasion of Privacy Without Proof of Actual Malice

The United States Supreme Court, in *New York Times Co. v. Sullivan*,[1] held that a state court could not constitutionally award damages in a libel suit by a public official against a critic of his official conduct without a showing of actual malice—that defendant knew the statement was false or that there was a reckless disregard for its truth. The malice requirement has since been extended to a prosecution under a state criminal libel statute.[2] In the recent case of *Time, Inc. v. Hill*,[3] the Court extended the malice requirement to a civil action for damages brought under a state invasion of privacy statute.[4]

In September of 1952 plaintiff Hill and his family were held hostage for nineteen hours in their home outside Philadelphia. The captors—three escaped convicts—then released the family unharmed. The following spring, a novel[5] was published describing "the experience of a family of four held hostage by three escaped convicts in the family's suburban home."[6] The family in the novel suffered violence and verbal abuse at the hands of the convicts, while the Hill family had not. When a play made from the book opened for

[1] 376 U.S. 254 (1964).

[2] Garrison v. Louisiana, 379 U.S. 64 (1964). *New York Times* and *Garrison* involved respectively a city commissioner and state criminal court judges—all clearly "public officials." In Rosenblatt v. Baer, 383 U.S. 75 (1966) the public official concept was extended to include a commissioner of a county ski recreation area.

[3] 385 U.S. 374 (1967).

[4] N.Y. CIVIL RIGHTS LAW §§ 50-51. Section 50 makes the use "for advertising purposes, or for the purposes of trade, the name, portrait or picture of any living person" without that person's consent, a misdemeanor. Section 51 gives any person whose name is so used, remedies in the form of actions for an injunction and for damages.

[5] HAYES, THE DESPERATE HOURS (1953).

[6] 385 U.S. at 378.

tryouts in Philadelphia, Life Magazine published a story captioned "True Crime Inspires Tense Play."[7] The text stated that the book and play had been "inspired by the [Hill] family's experience."[8] Plaintiff Hill brought an action for damages under the New York statute and, after two trials, an award of $30,000 compensatory damages[9] was affirmed by the New York Court of Appeals.[10] That court construed the statute as allowing a cause of action only for the fictionalized, or false, use of one's name for trade purposes.[11]

While refusing to condemn the statute as unconstitutional on its face, the Court, in an opinion by Mr. Justice Brennan, held that the first amendment protections of free speech and press prohibited application of the statute without proof of actual malice. Since under the trial court's instructions the jury could have found liability without finding that the false statements were made knowingly or recklessly, the case was remanded for a possible new trial.

Inception of the right of privacy is cited as the classic illustration of the forceful impact of scholarly comment upon the law.[12] Despite its relatively recent development,[13] the right is now said to have been recognized in thirty-four states and the District of Columbia.[14] It is distinguishable from defamation principally because

[7] Life, Feb. 28, 1955, p. 75.

[8] *Id.* at 75.

[9] At the initial jury trial plaintiff was awarded $50,000 compensatory and $25,000 punitive damages. A new trial was ordered as to damages only and, after waiver of a jury, plaintiff was awarded $30,000 compensatory damages by the court.

[10] Hill v. Hayes, 15 N.Y.2d 986, 260 N.Y.S.2d 7, 207 N.E.2d 604 (1965).

[11] The statute contains no such limitation on its face. N.Y. CIVIL RIGHTS LAW §§ 50-51. However, in an opinion handed down between the argument of *Hill* in the Supreme Court and the date of decision, the New York Court of Appeals made it clear that "factual reporting of newsworthy persons and events is in the public interest and is protected." Spahn v. Julian Messner, Inc., 18 N.Y.2d 324, 328, 274 N.Y.S.2d 877, 879, 221 N.E.2d 543, 545 (1966).

[12] Prosser, *Privacy*, 48 CALIF. L. REV. 383 (1960).

[13] Its beginnings are generally traced to a law review article published in 1890. Warren and Brandeis, *The Right to Privacy*, 4 HARV. L. REV. 193 (1890). See generally, Kalven, *Privacy in Tort Law—Were Warren and Brandeis Wrong?*, 31 LAW & CONTEMP. PROB. 326 (1966); Prosser, *Privacy*, 48 CALIF. L. REV. 383 (1960); Wade, *Defamation and the Right of Privacy*, 15 VAND. L. REV. 1093 (1962).

[14] Of the thirty-five jurisdictions recognizing the right, thirty-one have done so by case law, while four have statutory provisions. PROSSER, TORTS 831-32 (3d ed. 1964).

Recently, Professor Kalven has questioned the substance of the right. He notes that "the lack of legal profile and the enormity of the counter-privilege [to serve the public interest in news] converge to raise for me the question of whether privacy is really a viable tort remedy. The mountain,

damage results from the infliction of mental distress, while in defamation, harm to reputation is the critical element.[15] Dean Prosser has subdivided the privacy tort into four categories: intrusion, disclosure, false light and appropriation.[16] *Hill* involved the third category, described as placing the plaintiff "in a false light in the public eye."[17]

Generally, though the press is privileged to report matters of "public interest," fictionalization of such matters has been held to nullify the privilege.[18] The Supreme Court in *Hill* establishes the proposition that although there is fictionalization, the "public interest" privilege is not defeated unless there was knowledge of the falsity or reckless disregard for the truth. The privilege formerly existing is not only expanded, but is raised to a constitutional level.

Mr. Justice Brennan, in the opinion of the Court, reasons that because of the vast range of matter published in the press the risk of public exposure has become inherent in our society, one "which places a primary value on freedom of speech and of press."[19] He argues that freedom of discussion must encompass all issues, and cannot be limited to areas of political expression. He points out that erroneous statements are no less likely in the area involved in *Hill* than in the context of official conduct, and that since the *New York Times* rule was fashioned because of the likelihood of error in that context, it should be applied here too. Mr. Justice Brennan insists that the result was not reached through a rote application of the *New York Times* principles, but only upon consideration of the factors that arise in the *Hill* factual setting.[20]

I suggest, has brought forth a pretty small mouse." Kalven, *Privacy in Tort Law—were Warren and Brandeis Wrong?*, 31 LAW & CONTEMP. PROB. 326, 337 (1966). However, for a provocative argument that the privacy action is destined to eventually swallow up defamation actions, see Wade, *Defamation and the Right of Privacy*, 15 VAND. L. REV. 1093 (1962).

A North Carolina case recognized the right where plaintiff's photograph was used in an advertisement under a false name and without her consent. But in the absence of proof of special damages only nominal damages were allowed. Flake v. Greensboro News Co., 212 N.C. 780, 195 S.E. 55 (1938). No subsequent North Carolina cases have been found on the point.

[15] Themo v. New England Newspaper Publishing Co., 306 Mass. 54, 57, 27 N.E.2d 753, 755 (1940).

[16] Intrusion consists of invading the plaintiff's physical solitude, disclosure is publicity of private information about the plaintiff and appropriation is the use of plaintiff's name or likeness for the defendant's benefit. PROSSER, TORTS 833-44 (3d ed. 1964).

[17] *Id.* at 837.

[18] See note 11 *supra* and accompanying text.

[19] 385 U.S. at 388.

[20] We find applicable here the standard of knowing or reckless false-

Whatever factors may have been present in *Hill,* the *political* setting upon which the Court relied in *New York Times* was absent. *New York Times* and two later cases in which the rationale was expanded[21] involved libel actions by governmental officials against critics of their official conduct. In each case the Court relied upon the factual backdrop of the political arena in applying a constitutional buffer protecting unintended falsity.[22] The principal case, in contrast, was a privacy action by a private individual. His conduct was in no way "official" nor was it in any sense political.

Plaintiffs in *New York Times, Garrison* and *Rosenblatt* had an opportunity to rebut the falsity that was not available to Hill because they were all public officials when the falsity was published and had considerable access to news media. Hill's cause of action arose when Life published its fictionalized report of the incident—two years after he had been involuntarily placed in the limelight. At that time, whatever accessibility to the press he might have had by virtue of the event was gone.

Mr. Justice Black, in an opinion in which Mr. Justice Douglas joined, concurred in the remand of the case but disagreed with the Court's constitutional principles.[23] His rationale[24] is by far the

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hood not through blind application of New York Times Co. v. Sullivan, relating solely to libel actions by public officials, but only upon consideration of the factors which arise in the particular context of the application of the New York statute in cases involving private individuals. This is neither a libel action by a private individual nor a statutory action by a public official. Therefore, although the First Amendment principles pronounced in *New York Times* guide our conclusion, we reach that conclusion only by applying these principles in this discrete context.

Id. at 390-91.

[21] New York Times Co. v. Sullivan, 376 U.S. 254 (1964), involved a libel suit by an elected city commissioner against the publisher of an advertisement imputing false misconduct to law enforcement officials who worked under plaintiff's supervision. Garrison v. Louisiana, 379 U.S. 64 (1964), dealt with a criminal libel prosecution against a state district attorney who had criticized the official conduct of certain judges. Rosenblatt v. Baer, 383 U.S. 75 (1966), involved a libel suit by a supervisor of a county recreation area against the publisher of a newspaper column imputing misconduct to a small group of which plaintiff was a member.

[22] In all three the Court stated that it had considered the cases against a background of "profound national commitment to the principle that debate on public issues should be uninhibited, robust, and wide-open, and that it may well include vehement, caustic, and sometimes unpleasantly sharp attacks on government and public officials." 383 U.S. at 85, 379 U.S. at 75, 376 U.S. at 270.

[23] 385 U.S. at 398-401. (Opinion of Black, J., concurring.)

[24] See *e.g.,* Rosenblatt v. Baer, 383 U.S. 75, 94 (1966) (Opinion of Black, J., concurring in part and dissenting in part); New York Times Co.

simplest of those presented in the decision. He begins with the premise, set out in his concurring opinion in *New York Times,* that at the minimum there must be an "unconditional right to say what one pleases about public affairs."[25] He feels the majority is wrong in balancing the competing values of free speech and the right to privacy because this gives to judges the power to choose between conflicting values when, in his view, that choice has already been made by the framers when they adopted the first amendment. Further, he feels that this portends future "balancing" by which other freedoms embodied in the Bill of Rights will be eroded away.

Mr. Justice Black's view appears subject to much of the same criticism as the Court's. However absolute the freedoms of press and speech may be, the political settings in *New York Times* and subsequent cases seem to have presented a much greater need for free speech than did *Hill.* The need for unhampered discussion of public officials' conduct is surely more vital than the need for news coverage of the opening of a play. Yet if one accepts Mr. Justice Black's principle that the first amendment freedoms are absolute, the above criticism is foreclosed. There can be no weighing of the competing values of free speech and the potential harm from speech because the framers of the constitution made that choice—in favor of free speech.

Mr. Justice Douglas, while concurring in Mr. Justice Black's opinion, adds two salient points in a separate opinion.[26] First, since the book and play revived the public interest created by the incident in *Hill,* news stories dealing with them were privileged. Fictionalization of those events—deemed to have given rise to the cause of action—is no more beyond the public interest privilege, in his view, than "a water color of the assassination of a public official"[27] would be. He feels that any right of privacy in this context is irrelevant. Second, the exception created by the majority for knowing or reckless falsity gives, he thinks, too broad a discretion to the jury and will prove to be no bar to a recovery when emotions are high and prejudices present.

Should the privilege to report events of public interest vanish when the reports are fictionalized? Mr. Justice Douglas seems to

v. Sullivan, 376 U.S. 254, 293 (1964) (Opinion of Black, J., concurring).

[25] 376 U.S. at 297.

[26] 385 U.S. at 401-02. (Opinion of Douglas, J., concurring.)

[27] *Id.* at 401.

argue that it should not in any event, in order that the creative process may have full protection of the first amendment. Still, it is also arguable that the privilege should be defeated when the fictionalization causes greater harm than a factual account would have caused.[28] The Hills, however, were depicted as undergoing more suffering and as displaying more courage than they did in fact. This may have created more public sympathy and admiration than otherwise would have been the case, but there is little likelihood—at least in the ordinary sense—that additional harm resulted. Thus, in the factual circumstances of *Hill,* whichever argument is accepted, the result for which Mr. Justice Douglas contends seems sound.

His second contention—that the malice requirement will be a small obstacle to emotional juries—appears equally sound. If a jury's whims are too uncertain to risk the use of a negligence standard, as Mr. Justice Brennan contended for the Court, a malice standard is likely to be just as uncertain. A jury emotionally drawn to one side of a case will in all probability decide in favor of that side whether the finding required is one of negligence or of malice.

Mr. Justice Harlan concurred in the remand of the case but dissented from the Court's application of the *New York Times* standard.[29] He feels that the Court's protection of unintentional falsehood in that case was based on two principles: the inevitability of error in dealing with abstract matters and the undesirability of the censorship that might arise if the elusive concept of "truth" were placed in the hands of juries. However, he argues, these principles do not negative a state's interest in encouraging thorough preparation and checking of material before publication. Further, he contends, because the *New York Times* political setting and the likelihood of competition of ideas on the matter at issue were absent in *Hill,* the state interest is much stronger here. Thus, he feels that a

[28] Thus, cases in which falsification has been held to have exceeded the public interest privilege have generally involved falsehood that, while not defamatory, was at least in some way derogatory. See *e.g.,* Leverton v. Curtis Publishing Co., 192 F.2d 974 (3d Cir. 1951) (Plaintiff was photographed lying injured after a pedestrian accident. The photo was used—twenty months later—in an article to illustrate "pedestrian carelessness" when in fact plaintiff had not been careless); Gill v. Curtis Publishing Co., 38 Cal. 2d 273, 239 P.2d 630 (1952) (A photo of plaintiffs (husband and wife) with arms around each other was used with a story about love. The photo depicted "love at first sight," described in the article as bad and leading to divorce, when in fact plaintiffs were happily married.)

[29] 385 U.S. at 402-411. (Opinion of Harlan, J., concurring in part and dissenting in part.)

more limited protective "breathing space" is required in the *Hill* situation, and that a state should be able to "hold the press to a duty of making a reasonable investigation of the underlying facts. . . ."[30]

In *New York Times,* application of the principles described above by Mr. Justice Harlan was plainly grounded on the peculiarly vital function that free discussion serves in the area of politics and government; and just as plainly, that political background was absent in *Hill.* Hence, there is much logic in Mr. Justice Harlan's argument that the facts in *Hill* call for a more limited immunization of falsity. His proposal that the negligence standard be adopted is also supported by his analogy to other professions upon which such a standard is imposed.[31] That standard is no more objectionable on the ground of uncertainty due to jury prejudice than is the present standard of malice.[32]

Speaking for the dissenters,[33] Mr. Justice Fortas seems to agree with the constitutional principles laid down by Mr. Justice Brennan —that a state may validly subject a party to liability for knowingly or recklessly publishing false matter about a private individual.[34] He feels, however, that the remand was possibly a guise used by the majority to camouflage a more permissive constitutional rule, and with that he disagrees.[35] Further, Mr. Justice Fortas argued that under the jury instructions (covering both punitive and compensatory damages) given by the trial court, knowing or reckless publication was found. In his view, the verdict could not have been rendered under the instruction on punitive damages without having been predicated on a finding of the requisite knowledge or reck-

[30] *Id.* at 409.

[31] Both the medical and the legal professions were cited as examples. *Id.* at 410 & n.7.

[32] A publication must have been made with "knowledge of its falsity or in reckless disregard of the truth" before a state may constitutionally condemn it by damage awards. *Id.* at 387-88.

[33] *Id.* at 411-20. (Opinion of Fortas, J., dissenting, in which Mr. Justice Clark and the Chief Justice join.)

[34] Mr. Justice Fortas also agrees with the Court's refusal to hold the New York statute unconstitutional on its face. *Id.* at 411.

[35] Perhaps the purpose of the decision here is to indicate that this Court will place insuperable obstacles in the way of recovery by persons who are injured by reckless and heedless assaults provided they are in print, and even though they are totally divorced from fact. If so, I should think that the Court would cast its decision in constitutional terms.
Id. at *Ibid.*

lessness.[86] Though the instructions were not letter perfect, he urged that they met the standard set out by the majority.

The members of the Court seem to fit into three basic groups on the constitutional issue in the principal case. Justices Black and Douglas adhere to the absolute view that a state should not be permitted, constitutionally, to award damages for the publication of any matter in the public interest, even including calculated falsity. Mr. Justice Harlan, at the other end of the spectrum, feels that a state should be able, constitutionally, to award damages to a private citizen for publication of false matter in the public interest if the publisher failed to use reasonable care in verifying its truth. The six other members of the Court, including the dissenters, contend that a state may constitutionally impose civil sanctions for *knowing or reckless publication* of false matter in the public interest where private individuals are involved. The majority view thus lies in a middle ground between the two extremes.

The majority has clearly made a policy determination that the right of free speech outweighs a private individual's "right of privacy" where there is no intentional falsity; but they reach Mr. Justice Black's result with Mr. Justice Harlan's rationale. Accordingly, the court's rationale might be more appropriately articulated in terms of the absolute right that free speech is coming to be. In any event, by extending the public interest privilege to a constitutional level, *Hill* seems likely to limit considerably the future usefulness of "privacy" as a tort.

PHILIP L. KELLOGG

[86] The jury at the first trial was instructed that it might award exemplary damages only if they found that defendant

> falsely connected plaintiffs with The Desperate Hours and that this was done knowingly or through failure to make a reasonable investigation. . . . [Y]ou do not need to find that there was any actual ill will or personal malice toward the plaintiffs *if you find a reckless or wanton disregard of the plaintiffs' rights.*

Id. at 416. Although the majority seized upon the portion of the instruction that allowed the jury to make an award upon a finding of "failure to make a reasonable investigation," Mr. Justice Fortas felt that, taken as a whole, it met the *New York Times* standard.

Corporations—Directors and Officers—Standard of Care—Liability for Negligence

In *Selheimer v. Manganese Corp.*,[1] the majority and managing directors of Manganese were sued in a derivative action for negligent, imprudent and careless conduct in the management of the corporation that resulted in loss and ultimate insolvency. The corporation purchased a manganese oxide plant in Paterson, New Jersey from a corporation owned by the majority directors of Manganese. Following this purchase, the defendants caused 200,000 shares of stock to be sold to the public, the sale netting 412,000 dollars for the corporation. The prospectus for this sale stated that the corporation proposed to erect and operate a plant in Pennsylvania where substantial operating activities would be centered and that the corporation had arranged for the purchase of an ideally located plant at Colwyn, Pennsylvania, that would enable the corporation to operate at advantageous freight rates.

In spite of the defendants' knowledge that the Colwyn plant was far superior to the Paterson plant and that the Paterson plant was wholly unsuited for commercial production, they continued to invest money in the Paterson plant. 158,000 dollars was spent on equipment for the plant and, by August 1959, the plant had sustained a loss of 104,000 dollars with total sales of only 2,000 dollars. By August, Manganese's funds had been reduced to only 55,000 dollars out of 412,000 dollars originally available; this amount was not enough to put the Colwyn plant into operation. The Colwyn plant was never used. The assets of Manganese brought only 30,000 dollars upon its going into bankruptcy.[2]

The chancellor found that the managing directors were careless, imprudent, negligent and wasteful in their conduct, that this conduct caused the losses and insolvency, and that they were liable personally for these losses. The reviewing court, sitting en banc, agreed with the chancellor's finding of negligence, but found that defendants were not liable unless they were guilty of fraud, self-dealing or wanton misconduct and dismissed the complaint. The supreme court rejected

[1] 224 A.2d 634 (Pa. 1966).

[2] There were other transactions involved in the case but they tended to show some self-dealing by the defendants. These acts are not related to the issue of negligence but rather to the defendants' lack of good faith.

the decree of the court en banc[3] and held that the defendants' actions were to be measured by Section 408 of the Business Corporation Law of 1933 which provides:

> Officers and directors shall be deemed to stand in a fiduciary relation to the corporation, and shall discharge the duties of their respective positions in good faith and with that diligence, care and skill which ordinarily prudent men exercise under similar circumstances *in their personal business affairs.* (Emphasis added.)

Under this statute the court affirmed the chancellor's finding of negligence, but reversed and remanded as to the measure of damages. The Pennsylvania director's statute, if literally construed, creates a standard of care which is more stringent than that required at common law or by similar statutes in other states.

The early cases which attempted to define the relation of the director to his corporation and the standard of care required of him in performing his duties vary greatly from state to state.[4] The relation of the director to the corporation has been characterized as that of agent,[5] trustee (or quasi trustee),[6] and gratuitous mandatory.[7] Courts in the nineteenth century experienced difficulty in determining what this relation was and generally avoided thorough analysis by trying to characterize the relation in terms of well estab-

[3] The supreme court said that the court en banc misconstrued Smith v. Brown-Borhek Co., 414 Pa. 325, 200 A.2d 398 (1964) which held that stockholders can ratify negligent acts of directors but not fraudulent or wasteful acts.

[4] See Annot., 2 A.L.R. 867 (1919) which discusses representative cases and the various positions taken by American courts. See generally BALLANTINE, CORPORATIONS §§ 62-72 (Rev. ed. 1946) [hereinafter cited as BALLANTINE]; HORNSTEIN, CORPORATION LAW AND PRACTICE, §§ 432-46 (1959) [hereinafter cited as HORNSTEIN].

[5] See, *e.g.*, Briggs v. Spaulding, 141 U.S. 132 (1890); Hun v. Cary, 82 N.Y. 65 (1880). See generally Note, 36 NOTRE DAME LAW. 343 (1961); Bennett, *The Louisiana Business Corporation Act of 1928*, 2 LA. L. REV. 597 (1940) [hereinafter cited as Bennett].

[6] See, *e.g.*, Hun v. Cary, 82 N.Y. 65 (1880) (trustees to bank depositors); Besseliew v. Brown, 177 N.C. 65, 97 S.E. 743, 2 A.L.R. (1919). See generally Bennett 638; Note, 36 NOTRE DAME LAW. 343 (1961).

[7] See, *e.g.*, Swentzel v. Penn Bank, 147 Pa. 140, 23 Atl. 405 (1892); Sperling's Appeal, 71 Pa. 11 (1872). In *Sperling's Appeal* the court said that directors are not technical trustees. "They can only be regarded as mandatories—persons who have gratuitously undertaken to perform certain duties, and who are therefore bound to apply ordinary skill and diligence, but no more." *Id.* at 20-21. See generally Adkins & Janis, *Some Observations on Liabilities of Corporate Directors*, 20 BUS. LAW. 817, 819 (1965) [hereinafter cited as Adkins]; Bennett 638.

lished legal categories. The label "agent" is inappropriate since in reality there is no principal who can control the agent. Trustee is equally inappropriate since the corporation and not the directors have title to the assets.[8] The gratuitous mandatory label is archaic since it assumes that all directors serve gratuitously and devote little time to the corporation, an assumption no longer true in many cases.[9] However, all courts recognized that a director is a fiduciary of some sort with the duty to act in good faith and for the benefit of the shareholders rather than himself. The more modern position is simply that a director stands in a fiduciary relation to his corporation[10] and that this position is sui generis.[11]

Judicial attempts to define the standard of care required of directors and the liability for negligent mismanagement resulted in several distinct positions. The least-stringent is that a director is only liable for fraud or gross negligence amounting to fraud. This view is another way of saying that a director must use only slight care and reveals the reluctance of some courts to review the conduct

[8] Note, 36 NOTRE DAME LAW. 343 (1961).

[9] See, *e.g.*, Sperling's Appeal, 71 Pa. 11 (1872) (Action for negligent mismanagement) (Directors, not being compensated, not held to strict standards of trustee or agent of an estate). For the assertion that "mandatory" is no longer an appropriate label, see Adkins 819.

[10] This is evidenced by the wording of several modern directors statutes. IDAHO CODE ANN. § 30-142 (1947); LA. REV. STAT. § 12-36 (1951); N.C. GEN. STAT. § 55-35 (1965); OKLA. STAT. ANN. tit. 18, § 1.34 (1953); PA. STAT. ANN. tit. 15, § 2852-408 (1958); WASH. REV. CODE ANN. § 23.01.360 (1961). In North Carolina, the fiduciary duty runs to the stockholders as well as the corporation. For a discussion of the effect of this, see Folk, *Revisiting the North Carolina Corporation Law: The Robinson Treatise Reviewed and the Statute Reconsidered,* 43 N.C.L. REV. 768, 796-97 (1965). These statutes are similar or identical to the MODEL BUSINESS CORPORATION ACT § 33, U.L.A. c. 9. However, only a few states adopted this model act; it was withdrawn by the commissioners in 1957. This act should not be confused with the American Bar Association's Model Business Corporation Act which does not contain a similar provision. It has been used as a model by several states. For a general discussion of the state statutes, see Adkins 817.

[11] *In re* E. C. Warner Co., 232 Minn. 207, 45 N.W.2d 388 (1950), 35 MINN. L. REV. 564 (1951). The court, in a proceeding to determine whether directors are entitled to reimbursement for defense of suits against the corporation stated: "Confusion has resulted from a failure to recognize that the position of a director of a corporation, though fiduciary in many respects, is sui generis and is not to be confused with the position of that of trustee, quasi-trustee, or agent." *Id.* at 212, 45 N.W.2d at 392. The court further stated that the law of agency and trusts was developed before corporations became of great social importance. It is not possible to fit corporate management into either status and do justice to the necessities of it. *Id.* at 212, 45 N.W.2d at 392.

and judgment of directors.[12] At the other extreme is the view adopted in the Pennsylvania statute that a director must use the same degree of care and prudence that men prompted by self-interest generally exercise in their own affairs.[13] This standard of care is generally considered too strict since it would discourage honest men from serving as directors.[14] The middle and most widely accepted view is that a director must use the same care, skill, diligence and judgment that an ordinarily prudent man would exercise in similar circumstances in like position.[15] This standard is generally considered the most reasonable and workable one since it is flexible enough to be applied to varying circumstances and is strict enough to insure sound management.

Since the late 1920's, eleven states have adopted statutes defining the relation of the director to the corporation and the standard of care required of the director.[16] These statutes are generally very similar to the MODEL BUSINESS CORPORATION ACT § 33, 9 U.L.A. which provides:

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[12] See, *e.g.*, Sperling's Appeal, 71 Pa. 11 (1872); Commonwealth v. Anchor Bldg. & Loan Ass'n, 20 Pa. Super. 101 (1902). The court in *Sperling's Appeal*, held that directors are liable for fraud, gross negligence, and gross inattention to duties which results in the fraud of agents, "yet they are not liable for mistakes of judgment, even though they may be so gross as to appear as absurd and ridiculous, provided they are honest and provided they are fairly within the scope of the powers and discretion confided to the managing body." 71 Pa. at 24. This case has been criticized as being too lax. See Hun v. Cary, 82 N.Y. 65 (1880); BALLANTINE § 63. See generally HORNSTEIN § 446; ANNOT., 2 A.L.R. 867 (1919); Adkins 818-19; Baynes, *The Fiduciary Duty of Management—Concept of the Courts*, 35 U. DET. L.J. 561 (1958) [hereinafter cited as Baynes].

[13] See, *e.g.*, Hun v. Cary, 82 N.Y. 65 (1880) (Bank directors held liable for purchase of expensive building to create illusion of prosperity to community). The court said, "as he is bound to exercise ordinary skill and judgment, he cannot set up that he did not possess them." *Id.* at 74. To the same effect as *Hun*, see Kavanaugh v. Commonwealth Trust Co., 223 N.Y. 103 (1918) (Action for negligent inattention; defendent never attended meetings).

[14] Swentzel v. Penn Bank, 147 Pa. 140, 23 Atl. 405 (1892); BALLANTINE § 63; Adkins 818-19. See generally ANNOT., 2 A.L.R. 867 (1919).

[15] See, *e.g.*, Briggs v. Spaulding, 141 U.S. 132 (1891); Barnes v. Andrews, 298 Fed. 614 (S.D. N.Y. 1924); Besseliew v. Brown, 177 N.C. 65, 97 S.E. 743, 2 A.L.R. 867 (1919); Hunt v. Aufderheide, 330 Pa. 362, 199 Atl. 345 (1938). See generally BALLANTINE, § 63; Adkins 817; Baynes 561.

[16] 17 IDAHO CODE ANN. § 30-142 (1947); KY. REV. STAT. § 271.365 (1955); LA. REV. STAT. § 12-36 (1951); MICH. STAT. ANN. § 21.47 (1959); MINN. STAT. ANN. § 301.31 (1947); N.Y. Business Corporation Law § 717; N.C. GEN. STAT. § 55-35 (1965); OKLA. STAT. ANN. tit. 18, § 1.34 (1953); PA. STAT. ANN. tit. 15, § 2852-408 (1958); S.C. CODE ANN. tit. 12, § 12-18.13 (Supp. 1966); WASH. REV. CODE ANN. § 23.01.360 (1961).

> Officers and directors shall be deemed to stand in a fiduciary relation to the corporation, and shall discharge the duties of their respective positions in good faith, and with that diligence, care and skill which ordinarily prudent men would exercise under similar circumstances in like positions.

According to the commissioner's note to the model act, the standard provided in the act is designed to clear up the conflict among the cases, is believed to represent the weight of authority and is the most fair and practical standard.[17] The state statutes, as a rule, do not change the common law standard but merely codify the generally accepted rule.[18] Pennsylvania, alone, creates a different standard of care by placing the words "in their personal business affairs" in the place of the words "in like positions" in the model act.[19] This change of wording is interpreted in *Selheimer* as changing the common law standard that existed in Pennsylvania before adoption of Section 408.

The court in *Selheimer,* after rejecting the decision of the court en banc to the effect that directors are only liable for losses resulting from fraud, self-dealing or wanton misconduct,[20] stated:

> This statute mandates a standard of care for directors much more stringent and harsh than the standard enunciated by our courts prior to the passage of the statute. Our case law prior to the statute taught that the directors of a corporation—whether business, banking or otherwise—were held simply to a standard of ordinary care and diligence and that, absent fraud or gross negligence amounting to fraud, such directors would not be personally liable for their actions. The standard prior to Section

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[17] MODEL BUSINESS CORPORATION ACT § 33, at 186.

[18] See, *e.g.,* Detroit Gray Iron & Steel Foundaries, Inc. v. Martin, 362 Mich. 205, 106 N.W.2d 793 (1961); Fulton v. Talbert, 255 N.C. 183, 120 S.E.2d 410 (1961). For examples of applications and constructions of these statutes, see Otis & Co. v. Pennsylvania Ry., 61 F. Supp. 905 (E.D. Pa. 1945) (Applies PA. BUSINESS CORPORATION ACT § 408); McLeod v. Lewis-Clark Hotel Co., 66 Idaho 584, 164 P.2d 195 (1945); Pool v. Pool, 16 So. 2d 132 (La. Ct. App. 1943); Detroit Gray Iron & Steel Foundaries, Inc. v. Martin, 363 Mich. 205, 106 N.W.2d 793 (1961); Scott v. Stanton Heights Corp., 388 Pa. 628, 131 A.2d 133 (1957). For a general discussion of these statutes, see Adkins 817; Bennett 637; Note, 36 NOTRE DAME LAW. 343 (1961).

[19] The statutes in Louisiana, Kentucky, Idaho, North Carolina, Oklahoma, and Washington adopt substantially the wording of the model act. The New York, South Carolina, Michigan and Minnesota statutes employ the model act standard of care but do not state that directors are "deemed to stand in a fiduciary relation." Minnesota, South Carolina and New York merely require the directors to discharge their duties in good faith.

[20] See note 4 *supra.*

> 408 might well be stated as that care, skill and diligence which the ordinary prudent man would exercise under similar circumstances.[21]

In construing Section 408, the court greatly emphasized the legislative background.[22] However, after laying this background, the court, on the facts did not reach a result different from that required by the common law rule. The court stated: "In our view, however, regardless of whether we follow the statutory rule or the rule enunciated in our case law prior to the statute, the same result follows in the case at bar."[23] An affirmative answer to the following question was said to be self-evident:

> In the absence of fraud, self-dealing, or proof of personal profit or wanton acts of omission or commission, are the directors of a business corporation, who have been imprudent, wasteful, careless and negligent, personally liable, under either the common law or Section 408, where such actions have resulted in corporate losses resulting in the insolvency of the corporation?[24]

After reviewing the facts, it was concluded that the defendants' actions in respect to the Colwyn plant were not the result of errors of judgment or calculated business risks.[25] Nor could their actions be classified as mere negligence. "With the knowledge the defendants had of the unsuitability of the Paterson plant for profitable

[21] Selheimer v. Manganese Corp., 224 A.2d 634, 641 (Pa. 1966). At this point the court reviewed the leading Pennsylvania cases which developed the common law standard of care, *e.g.*, Hunt v. Aufderheide, 330 Pa. 362, 199 Atl. 345 (1938) (Directors held to same care, skill and diligence ordinarily prudent man would use in similar circumstances); Swentzel v. Penn Bank, 147 Pa. 140, 23 Atl. 405 (1892) (Liable only for fraud or gross negligence amounting to fraud) (Expressly rejects the "own affairs" standard); Sperling's Appeal, 71 Pa. 11 (1872) (Liable only for gross negligence or gross misconduct).

[22] 224 A.2d at 642-43. The court said that a certain legislative background must be kept in mind: (1) the phrase "in their personal affairs" was not found in the Model Business Corporation Act, (2) prior to the statute, the case law rejected the standard expressly provided in Section 408, (3) the standard in Section 408 does not represent the majority view, (4) Section 408 imposes on a director of a business corporation a much higher degree of care than the law imposes on a director of a banking or building and loan corporation.

[23] *Id.* at 643.

[24] *Id.* at 644.

[25] *Id.* at 646. Previously the court stated the generally accepted rule that directors who exercise their judgment in good faith are not liable for errors of judgment or mistakes. *Id.* at 644. This is usually referred to as the business judgment rule; it takes into account that directors of business corporations are expected to take calculated business risks. See generally BALLANTINE §§ 62-72; HORNSTEIN §§ 432-446.

production," their pouring of assets into the Paterson plant was held to defy explanation.[26] In fact the defendants' whole pattern of conduct was said to border on willful misconduct and self-dealing since they caused the corporation to pay them unauthorized salaries and to purchase equipment from companies in which the defendants owned an interest.[27] Finally, the court agreed with the chancellor that the four majority directors were personally liable for any losses that resulted from their wasteful and negligent actions.[28]

This case, although clearly establishing that Section 408 differs from and is more stringent than the common law standard of care, does little or nothing to illustrate what the difference is. By holding that the defendants' action was violative of the common law standard (which was none too clear in Pennsylvania) as well as the statutory standard, the court avoided the problem of determining exactly the effect of the words "in their personal business affairs." Admittedly, it would have been of little value for the court to attempt to draw an exact line marking the difference between actionable and blameless conduct, yet, it would have been helpful if the court had given some indication of what the effect of the statute is. As the case stands, it is authority only for the general principle that Section 408 requires greater care than other similar statutes and the common law standard.

As the court recognized, the terminology of the statute is very strict[29] and if literally applied might render directorships unattractive.[30] A flexible, comparative standard is needed today because circumstances under which directors act will vary greatly from one corporation to another—some directors taking a very active role in management as in *Selheimer,* and some functioning, for the most part, in a broad policy making and advisory capacity characteristic of larger corporations. Negligence is always a question of fact under the circumstances. The court in *Selheimer* recognizes this statement as a guiding general principle;[31] however, under the

[26] 224 A.2d at 646.

[27] These facts relate to the issue of breach of the duty to act in good faith and not to the issue of failure to use due care. At the suggestion of defendant Selheimer, the board of directors voted to reimburse the corporations for salaries received but they had not been repaid. *Id.* at 638-39. For cases involving breach of fiduciary duty under Section 408, see *id.* at 643.

[28] *Id.* at 646.

[29] *Id.* at 640, 643.

[30] See BALLANTINE § 63; Adkins 819.

[31] 224 A.2d at 644.

Pennsylvania statute, the court, of necessity, will have less latitude in taking the circumstances of each case into account than will other courts that apply the majority rule. Regardless of the size of the corporation, the nature of it, the number of directorships a particular director holds, the compensation received, or the demands of the director's own affairs, a director in Pennsylvania must always use the care a prudent man uses in his own affairs.[32]

Where directors, as is the case in some large and some close corporations, are, in reality, independent, highly paid professional managers, the "own affairs" standard is not completely objectionable; but, this is not the universal situation. In the future should the court find occasion to apply the statute literally and should it reach a result different from the common law, corporations will be forced into employing experienced, professional directors at adequate compensation. Without compensation or a personal interest in the corporation's success, it is unlikely that one would be willing to take on the responsibility of a directorship in a corporation of any complexity.

ALBERT VICTOR WRAY

Corporations—Interested Directors—Fiduciary Duty and the Business Judgment Rule

The business judgment rule is a defense to directors who, in the exercise of their discretionary powers, cause corporate losses through errors in judgment.[1] It is based on the assumption that the directors, elected by the shareholders for this purpose, are in the best position to decide corporate policy and that a court, less familiar with the problems involved, should not substitute its judgment for that of the directors.[2] The shareholders have no right to appeal to the courts

[32] For a criticism of the Pennsylvania statute as too subjective, see Adkins 819. The comments to the NEW YORK BUSINESS CORPORATION LAW § 717 expressly recognizes the need for a flexible, comparative standard of care: "The adoption of the standard prescribed by this section will allow the court to envisage the directors' duty of care as a relative concept, depending on the kind of corporation involved, the particular circumstances and the corporate role of the director."

[1] See Briggs v. Spaulding, 141 U.S. 132 (1891); Otis & Co. v. Pennsylvania R.R., 61 F. Supp. 905 (E.D.Pa. 1945), *aff'd per curiam* 155 F.2d 522 (3d Cir. 1946); Spiegel v. Beacon Participations, Inc., 297 Mass. 398, 8 N.E.2d 895 (1937); Abrams v. Allen, 297 N.Y. 52, 74 N.E.2d 305 (1947).

[2] See Coffman v. Maryland Publishing Co., 167 Md. 275, 173 Atl. 248

for relief from the decisions made by the directors if such decisions are made in good faith,[3] with due care,[4] and in accordance with applicable fiduciary duties owed the corporation and its shareholders.[5]

While the shareholders do assume this risk of errors in judgment, they should not be held to assume the risk of disloyalty. The rule does not protect directors who act in their own personal interest.[6] Directors owe a fiduciary duty to the corporation and its minority shareholders to act in the best interest of the corporation.[7] They cannot use their position of trust to benefit themselves or a particular group of shareholders at the expense of the corporation or its other shareholders.[8] A recent decision by the Delaware Supreme Court illustrates how the business judgment rule will occasionally be expanded into this area of fiduciary duty to uphold an otherwise suspect transaction by interested directors.

In *Warshaw v. Calhoun*[9] the plaintiff was a minority share-

(1934); Helfman v. American Light & Traction Co., 121 N.J. Eq. 1, 187 Atl. 540 (1936); Pollitz v. Wabash R.R., 207 N.Y. 113, 100 N.E. 721 (1912); Marony v. Applegate, 266 App. Div. 412, 42 N.Y.S.2d 768 (1943).

[3] See Dumont v. Raymond, 49 N.Y.S.2d 865 (Sup. Ct. 1944); Howell v. McClosky, 373 Pa. 100, 99 A.2d 610 (1953).

[4] Casey v. Woodruff, 49 N.Y.S.2d 625 (Sup. Ct. 1944).

[5] Evans v. Armour & Co., 241 F. Supp. 705 (E.D.Pa. 1965); Abrams v. Allen, 297 N.Y. 52, 74 N.E.2d 305 (1947); Steinberg v. Altschuler, 158 N.Y.S.2d 411 (Sup. Ct. 1956); Howell v. McClosky, 375 Pa. 100, 99 A.2d 610 (1953).

[6] Geddes v. Anaconda Copper Mining Co., 254 U.S. 590 (1920); Alster v. British Type Investors, 83 F. Supp. 949 (S.D.N.Y. 1949); Shlensky v. South Parkway Bldg. Corp., 19 Ill. 2d 268, 166 N.E.2d 793 (1960); Bayer v. Beran, 49 N.Y.S.2d 2 (Sup. Ct. 1944).

[7] SEC v. Chenery Corp., 318 U.S. 80 (1942); Perlman v. Feldmann, 219 F.2d 173 (2d Cir. 1955), *cert. denied* 349 U.S. 952 (1955); Zahn v. Transamerica Corp., 162 F.2d 36 (3d Cir. 1947); Lebold v. Inland Steel Co., 125 F.2d 369 (7th Cir. 1941), *cert. denied* 316 U.S. 675 (1942); Remillard Brick Co. v. Remillard-Dandini Co., 109 Cal. App. 2d 405, 241 P.2d 66 (1952); Guth v. Loft, 23 Del. Ch. 255, 5 A.2d 503 (Sup. Ct. 1939); Kavanaugh v. Kavanaugh Knitting Co., 226 N.Y. 185, 123 N.E. 148 (1919).

[8] He who is in such a fiduciary position cannot serve himself first and his *cestius* second. . . . He cannot use his power for his personal advantage and to the detriment of the stockholders and creditors no matter how absolute in terms that power may be and no matter how meticulous he is to satisfy technical requirements.

Pepper v. Litton, 308 U.S. 295, 311 (1939).

[9] 221 A.2d 487 (Del. 1966).

See also Case v. New York Central R.R., 15 N.Y.2d 150, 204 N.E.2d 643, 256 N.Y.S.2d 607 (1965), reversing 19 App. Div. 2d 383, 243 N.Y.S.2d 620 (1963). This case involved a suit by minority shareholders in a Central subsidiary challenging an agreement between the two linked corporations. The agreement, entered into by interlocking directors, provided

holder in Western Insurance Securities Co. Securities, a personal holding company, was organized for the purpose of controlling Western Casualty and Surety Co.; its only substantial asset being a controlling block of stock in Casualty. The individual defendants, majority shareholders in Securities,[10] were officers and/or directors of both companies. In 1953, when it became necessary to obtain additional capital and to broaden the public ownership of Casualty, the defendants approved a plan to issue new stock with the purchase rights going to Casualty shareholders. The defendants, in their capacity as directors of Securities, then rejected Securities' rights in the issue and sold the rights to the underwriters handling the issue for Casualty. Similar new issues were made by Casualty in 1959 and 1962 and again Securities sold its rights. These combined transactions led to a reduction of Securities' holdings in Casualty from 92 to 41 per cent and a corresponding reduction in the equity Securities' shareholders had in the profits of Casualty. The loss suffered by the shareholders was magnified by the fact that Securities' stock had always sold at a 25 to 50 per cent discount from the value of its assets. The Supreme Court of Delaware, affirming the Chancellor's grant of summary judgment for defendants,[11] held that the plaintiff was not entitled to an accounting from the individual defendants for losses resulting from the transaction or to the appointment of a receiver for the liquidation or reorganization of Securities.[12]

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for the allocation to Central of almost all of the tax savings realized from the consolidation of the tax returns of the two companies. The Court of Appeals, reversing the Appellate Division, held that the transaction was fair when analyzed from the viewpoint of the "system" as a whole, indicating that what was good for the system of railroads was good for the constituent parts. While the court did not specifically mention the business judgment rule, it would seem that this decision also offers an illustration of the expansion of the rule into the traditional area of fiduciary duty.

[10] The defendants held fifty-five per cent of the stock in Securities. The fact that a majority of the stock in the corporation was owned by less than five shareholders and that Securities sole income was from dividends earned on its holdings in Casualty led to its classification as a personal holding company. The retained earnings of a personal holding company are taxed at a confiscatory rate. See Int. Rev. Code of 1954, §§ 541-42.

[11] Warshaw v. Calhoun, 213 A.2d 539 (Del. Ch. 1965).

[12] The plaintiff sought to have a receiver appointed to liquidate, reorganize, or merge Securities with Casualty in order to eliminate the disadvantages inherent in Securities corporate form. The court held that the severe tax consequences of the personal holding company status did not justify the appointment of a receiver and that the continuation of the corporation in this form was not illegal. The court indicated that the plaintiff's

There were sound business reasons advanced by defendants that, on the face of the transaction, would seem to justify the application of the business judgment rule. Securities, a personal holding company,[13] was subject to a confiscatory tax[14] on retained earnings and was without the necessary funds to exercise the rights itself. The underwriter advised that a plan to pass the rights on to the shareholders of Securities would increase the cost and risk the success of the underwriting. Also the plan would defeat one of the primary purposes of the new issue, *i.e.* to broaden the public ownership of Casualty stock. The court listed these factors and said, "Whether or not this be so, we think that the decision as to what Securities should do with its rights to subscribe to Casualty stock was a matter to be decided in accordance with the sound business judgment of the directors of Securities."[15]

The court gave only passing reference to the plaintiff's claim that defendants were remiss in not transferring the rights to Securities' shareholders and that this was done in order to perpetuate defendants' control over Casualty through their control of Securities. There would seem to be sufficient evidence of a conflict of interest such as would hamper defendants in giving the transaction the disinterested consideration required for application of the business judgment rule.[16] Where there is such a taint on a transaction, the court should examine all of the circumstances surrounding the decision to determine if in fact it was in the best interest of the corporation.[17] Here the court should have weighed the possible increased cost and threatened risk involved in passing the rights on to the shareholders against the loss suffered. The court should have also determined if there were other means of accomplishing the purpose of the issues without depleting the shareholders interest. If these factors had been considered the court may have determined that the directors did not act in the best interest of the corporation.

Cheff v. Mathes[18] offers another example of this use of the business judgment rule to uphold a transaction blocking a potential

remedy was to withdraw from the corporation by the sale of her stock. Discussion of this aspect of the case is beyond the scope of this note.

[13] See Int. Rev. Code of 1954, § 542.

[14] See Int. Rev. Code of 1954, § 541.

[15] 221 A.2d 487, 492 (Del. 1966).

[16] See note 7 *supra* and accompanying text.

[17] See note 23 *infra* and accompanying text.

[18] 199 A.2d 548 (Del. 1963).

shift in control. Here the plaintiff brought a derivative suit to hold the directors of Holland Furnace Corporation liable for losses resulting from the allegedly improper use of corporate funds to purchase the corporation's own stock. The controlling shareholders, who were members of the corporation's founding family and who made up the board of directors, learned that one Maremont was buying large quantities of Holland stock on the market. Maremont had a reputation for realizing quick profits from the sale or liquidation of corporations he acquired and there was some indication that he intended to change corporate policy. The board of directors, fearing such a take over, caused the corporation to purchase Maremont's shares at a price in excess of the market value. Plaintiff, a minority shareholder, attacked the transaction, alleging that its sole purpose was the perpetuation of the incumbent directors' control. The Vice Chancellor, agreeing with the plaintiff, disallowed the purchase on the grounds that there was no substantial evidence that any real threat was posed to the corporation.[19] The Supreme Court of Delaware reversed, holding that the directors, having satisfied the burden of proof by showing that they had reasonable grounds to believe that a substantial threat to the corporation or its policies existed, would not be penalized for an honest mistake in judgment.

The direct effect of this transaction was to insure that the control held by the incumbent directors was preserved through the use of corporate funds. A purchase by the corporation of its own shares in order to maintain control is an abuse of corporate power and a breach of fiduciary duty,[20] yet the court did not give full consideration to the question of conflicting interest. One commentator has questioned the immediacy of the threat because it would be necessary for Maremont to obtain a majority of the stock or support from a majority of the shareholders before he could control the board of directors and influence corporate policy.[21] Also, before upholding such a transaction it would seem that the court should have determined if there were other means, using non-corporate funds, to have eliminated the danger. The founding family should have resorted to their own resources before those of the corporation.

One possible explanation of the holdings in these cases is that

[19] Mathes v. Cheff, 190 A.2d 524 (Del. Ch. 1963).

[20] See Kahn v. Schiff, 105 F. Supp. 973 (S.D. Ohio 1952); Yasik v. Wachtel, 25 Del. Ch. 247, 17 A.2d 309 (1941).

[21] Note, 50 CORNELL L.Q. 302 (1965).

the plaintiffs purchased shares in corporations with well established control patterns. In *Warshaw,* Securities was organized by the defendants as a device to insure their control over Casualty while in *Cheff* the founding family had set corporate policy and controlled the corporation from the outset. It may be that by using the business judgment rule in these cases the court is merely saying that the plaintiffs accepted these circumstances when they purchased their shares and cannot now complain.[22] If so, the court is overlooking the realities involved in a stock purchase. The purchaser does not agree to future action by those in control that will cause corporate losses in an effort to maintain that control.

The court in each of these cases probably reached the correct result as the challenged transactions, all factors considered, may well have been in the best interest of the corporations. By using the business judgment rule, however, the courts avoided analysis of the essential question presented—the possible self-dealing of the directors. The basis of the rule is to allow directors freedom to act without fear of being "second-guessed" by a court should they make a mistake. Where the loss is caused by such a conflict of interests that the directors are deprived of their ability to exercise impartial judgment this reason for the rule fails. In this situation the courts, in order to protect the minority shareholders, have a duty to "second-guess" the directors and to carefully scrutinize the transaction.[23]

[22] In Goodman v. Futrovsky, 213 A.2d 899 (Del. 1965), the court was faced with an attack by a minority shareholder on an arrangement whereby a concern owned by the majority shareholders was the sole supplier of the supermarket corporation's produce requirements. Prior to 1959, when there was a public issue of supermarket stock, the majority shareholders owned both businesses. The prospectus for the issue set forth this relationship between the two companies and explained the interest of the majority shareholders. The court held that because the present holders of supermarket stock trace their title to the purchase of the 1959 issue "they are bound by their acquiescence, with full knowledge, of their predecessors and are now precluded from attacking the . . . relationship. *Id.* at 903. The court in *Warshaw and Cheff* may have been thinking along these lines in deciding those cases.

[23] *Cf.* Litwin (Rosemarin) v. Allen, 25 N.Y.S.2d 667 (Sup. Ct. 1940) where the court said that a director

> owes loyalty and allegiance to the corporation—a loyalty that is undivided and an allegiance that is influenced in action by no consideration other than the welfare of the corporation. Any adverse interest of a director will be subjected to a scrutiny rigid and uncompromising. He may not profit at the expense of his corporation and in conflict with its rights; he may not for personal gain divert unto himself the opportunities which in equity and fairness belong to his corporation. He is required to use his independent judgment.

The minority shareholder in a modern corporation is essentially without a voice in the management of the corporation.[24] The one remaining device with which he can protect his investment from the self-dealing of those in control is through a shareholders derivative action on behalf of the corporation. Through such an action he can enforce the fiduciary duties owed by the management. The courts, by permitting the expansion of the business judgment rule into the traditional enclave of the director's "duty of loyalty," are removing a substantial portion of this protection. In most situations where directors enter into such a transaction, they will be able to put forth plausible business reasons in its support, but they may not always be able to satisfy the demands of undivided loyalty.

REED JOHNSTON, JR.

Criminal Law—Committed Patient's Right to Treatment in Public Mental Hospitals

Nineteenth century attitudes toward insanity were responsible for the conception of a lunatic asylum as an institution for the public safety. The conditions in the asylums reflected the wild beast notion of mental illness[1]—the essential function of the asylum was

Id. at 677.

In the analogous situation where the directors contract with their own corporation, or where corporations with common directors contract together, the majority rule calls for close scrutiny of the contract to insure its fairness. See Bank of United States v. Cuthbertson, 67 F.2d 182 (4th Cir. 1933), *cert. denied* 291 U.S. 665 (1933); Guaranty Trust Co. v. United States, 44 F. Supp. 417 (E.D. Wash. 1942), *aff'd* 139 F.2d 69 (9th Cir. 1942); Tucson Federal Sav. & Loan Ass'n v. Aetna Inv. Corp., 74 Ariz. 163, 245 P.2d 423 (1952); Kennedy v. Emerald Coal & Coke Co., 28 Del. Ch. 405, 42 A.2d 398 (1944); Everett v. Phillips, 288 N.Y. 227, 43 N.E.2d 18 (1942).

[24] The modern large American corporation enjoys almost complete independence from its stockholders, the principal source of external intereference. While lip service is always paid to democratic control by the owners, it is recognized in practice that any extensive and effective interference by stockholders in management would be exceedingly damaging.

GALBRAITH, ECONOMIC DEVELOPMENT IN PERSPECTIVE, 65-66 (1962).

Ownership of wealth without appreciable control and control of wealth without appreciable ownership appear to be the logical outcome of corporate development.

BERLE & MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY, 69 (1933).

[1] Rex v. Arnold, 16 How. St. Tr. 695, 764 (1742).

custody, the doctor was the keeper. However, a recent case questions the custody-function theory and poses a dilemma over the civil rights of patients in public mental hospitals: may the state involuntarily commit an individual and yet neglect to provide therapy in the hospital, or, if overcrowding and understaffing make therapy impractical, is the patient entitled to his liberty in spite of danger to himself or the community? In *Rouse v. Cameron*[2] the Court of Appeals for the District of Columbia held that a patient involuntarily committed after being acquitted by reason of insanity on a misdemeanor charge has a *right to treatment,* on the basis of a District of Columbia statute which provides: "a person hospitalized in a public hospital for a mental illness shall, during his hospitalization, be entitled to medical and psychiatric care and treatment."[3]

Rouse had been committed to St. Elizabeth's Hospital. Four years[4] passed and he brought habeas corpus proceedings in the district court, contending that he was receiving no treatment, or alternatively, that he had recovered his mental health and was entitled to release. The district court refused to hear the treatment issue on the ground of lack of subject-matter jurisdiction. The Court of Appeals remanded for a hearing, holding that if Rouse was not receiving treatment, he was in custody in violation of a federal statute and was entitled to habeas corpus relief.[5] Appropriate relief, the court indicated, might be to remand the patient to custody and

[2] 373 F.2d 451 (D.C. Cir. 1966).

[3] D.C. CODE § 21-562 (Supp. V. 1966).

[4] He was acquitted of carrying a dangerous weapon, a misdemeanor carrying a maximum sentence of *one* year. D.C. CODE ANN. § 22-3215 (1961).

[5] The statute created a right to therapy. Therefore mere custodial care is unlawful. The court indicated that the statute required only that the patient receive some therapy representing a good faith effort at individualized treatment of his disorder. Whether so called milieu therapy—mere presence in the controlled environment of the hospital—complies with the statute, depends, the court said, upon its suitability to individual patient needs. 373 F.2d at 459. It should be noted that the standards of proof in establishing the inadequacy of particular therapy will be similar to those used in medical malpractice suits, with which the courts are familiar. Whether individual patients will be able to bring these standards to bear on their situations, however, may depend upon their financial resources. It is to be presumed that hospital psychiatrists will be predisposed to testify that milieu therapy is adequate in a given case. The patient then must come forward with his own expert testimony, which will involve a private diagnosis. Quaere whether the court will be inclined to rubber stamp the judgment of the hospital psychiatrist in cases where the patient is unable to put on his own expert testimony?

direct the hospital to begin treatment, or, if the opportunity for treatment had been exhausted, to release the patient conditionally or unconditionally.[6]

Since the decision rested on a statute, rather than on constitutional grounds,[7] its implications beyond the District of Columbia depend in a formal sense on the existence of a similar statute wherever the issue may be litigated. While, apparently, there is no statute in other federal jurisdictions,[8] the statutes of thirteen states expressly recognize a right to treatment, and in twenty-four additional states the statutes could be construed to permit the result reached in *Rouse*.[9] With regard to judicial decisions, *Rouse* is a case of first impression.

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[6] *Id.* at 458.

[7] An exhaustive treatment of the constitutional issues is beyond the scope of this note, but a few observations can be made. The court in *Rouse* noted that there were serious constitutional objections to confinement without therapy, but decided the case on the basis of the statute. The constitutional justification for compulsory commitment is grounded in two concepts: the general police power of the state to protect society against breaches of the peace, and the doctrine of the state as parens patriae. See Ross, *Commitment of the Mentally Ill,* 56 MICH. L. REV. 945, 955 (1959). Summary commitment on a verdict of not guilty by reason of insanity does *not* rest on a finding of present insanity, or dangerousness, and therefore cannot be predicated on the police power. See Lynch v. Overholser, 369 U.S. 705 (1962). The theoretical basis is the parens patriae concept, which requires that *only* the interests of the defendant be taken into account. And only therapy, not mere custody, is in the defendant's interests.

The argument can be made that absent therapy involuntary hospitalization is tantamount to imprisonment, which the court could not constitutionally impose on a not guilty verdict. Ragsdale v. Overholser, 281 F.2d 943, 950 (D.C. Cir. 1960). Second, the argument can be made that any involuntary hospitalization without the benefit of therapy represents incarceration because of a status—being mentally ill—and as such is a cruel and unusual punishment forbidden by the eighth amendment under the doctrine of Robinson v. California, 370 U.S. 660 (1960). See Driver v. Hinnant, 356 F.2d 761 (4th Cir. 1966); Easter v. District of Columbia, 361 F.2d 50 (D.C. Cir. 1966). See 44 N.C.L. REV. 818 (1966).

[8] Senator Robert Kennedy has introduced a bill applicable to federal jurisdictions other than the Distirct of Columbia which includes a provision identical to the *Rouse* statute. S. 3689, 89th Cong., 2d Sess. § 4249(b) (1966).

[9] Least typical (two states) and most like the District of Columbia statute, are the statutes which create an unqualified right to treatment. ILL. REV. STAT. ch. 91½, § 100-7 (1966); OKLA. STAT. ANN. tit. 43A, § 2 (1954). A second group of statutes (eleven states) expressly recognizes a right to treatment, but with the qualification stated in, for example, the Ohio statute: "Every patient shall be entitled . . . *to the extent that facilities, equipment and personnel are available,* to medical care and treatment." OHIO REV. CODE ANN. § 5122.27 (Supp. 1966). *See also* GA. CODE ANN. § 88-1614 (1963); IDAHO CODE ANN. § 66-344 (Supp. 1965); ME. REV. STAT. ANN. tit. 34, § 2252 (1965); MO. ANN. STAT. § 202.840 (1962); N.J. REV. STAT. § 30:4-24.1 (Supp. 1966); N.M. STAT. ANN. § 34-2-13 (1954); N.D.

Assuming the substantive law recognizes a right to therapy on statutory or constitutional grounds, there is the question of choice of remedy. Causes alleging illegal or abusive confinement are typically litigated on habeas corpus or in an action under the federal civil rights statute. The issue in *Rouse* was presented in a petition for habeas corpus. The relief which the District of Columbia court indicated could be given on remand reflects its policy of treating a petition for habeas corpus according to its substantive merit—if it substantively merits injunctive relief, for example, it will be treated as a petition for an injunction.[10] On the other hand, the weight of the federal cases follow the common law rule that habeas corpus will only issue to procure *release* of the petitioner from confinement.[11] This would preclude relief in the form of compulsory processes against the hospital. In between these polar extremes are several federal courts which have developed a special circumstances

CENT. CODE § 25-03-18 (1960); TENN. CODE ANN. § 33-306 (Supp. 1966); UTAH CODE ANN. § 64-7-46 (1961); WYO. STAT. ANN. § 25-70 (Supp. 1965). A third group (eighteen states) creates a duty on the part of responsible authorities to provide therapy, rather than creating a patient right. ALASKA STAT. § 47.30.010 (1962); ARIZ. REV. STAT. ANN. § 36-521 (Supp. 1966); ARK. STAT. ANN. § 59-229 (Supp. 1965); CONN. GEN. STAT. REV. § 17-211 (1960); IOWA CODE ANN. § 225.15 (1949); KAN. GEN. STAT. ANN. § 59-2927 (Supp. 1965); KY. REV. STAT. § 210.040(4) (1962); MD. ANN. CODE art. 59, § 18 (1957); MICH. STAT. ANN. § 14.802 (Supp. 1966); MINN. STAT. ANN. § 246.012 (1959); MONT. REV. CODES ANN. § 38-103 (1961); NEB. REV. STAT. § 83-307 (1958); N.H. REV. STAT. ANN. § 135:6(a) (1964); N.Y. MENTAL HYGIENE LAW § 22; S.C. CODE ANN. § 32-922 (1962); S.D. CODE § 30.0202 (1960); TEX. REV. CIV. STAT. ANN. art. 5547-70 (1958); VT. STAT. ANN. tit. 18 § 2503 (Supp. 1965). North Carolina provides that it is the duty of "duly constituted authorities of the State Hospitals . . . for the mentally ill to receive all such mentally ill persons as shall be committed to said institutions . . . and to treat and care properly for the same until discharged." N.C. GEN. STAT. § 122-89 (1964). A fourth group of statutes (six states) state that the maintenance of adequate medical care is either the state policy or is the purpose in establishing institutions such as the state mental hospital. COL. REV. STAT. ANN. § 71-1-23 (1964); IND. ANN. STAT. § 60-1359 (1961); ORE. REV. STAT. § 426.010 (1965); R.I. GEN. LAWS ANN. § 26-1-1 (1957); W. VA. CODE ANN. § 27-1A-1 (1966); WIS. STAT. ANN. § 51.005 (1957). In addition, three states charge the responsible authorities with the duty of making a periodic inquiry into the medical care being received by mental patients. CALIF. WELFARE AND INST. CODE § 6621; HAWAII REV. LAWS § 81-13 (1955); MISS. CODE ANN. § 6902 (1953).

[10] *E.g.*, Miller v. Overhouser, 206 F.2d 415, 421 (D.C. Cir. 1953). In accord is the Court of Appeals for the Fourth Circuit. *E.g.*, Roberts v. Pegelow, 313 F.2d 548 (4th Cir. 1963).

[11] *E.g.*, Miller v. Gladden, 341 F.2d 972 (9th Cir. 1965); Haskins v. U.S., 292 F.2d 265 (2d Cir. 1961); McGann v. Taylor, 289 F.2d 820 (10th Cir. 1961); Williams v. Steele, 194 F.2d 32 (8th Cir. 1952); Sarshik v. Sanford, 142 F.2d 676 (5th Cir. 1944).

rule.[12] The problem of limited usage of habeas corpus can be avoided entirely, however, by bringing an action under the federal civil rights statute,[13] in which Congress has expressly provided that the federal court may grant any relief available under federal law, and any relief available under the law of the forum state if federal relief is found to be inadequate.[14] The only necessary allegation is that the patient is being denied a federally protected civil right by persons acting under color of state or territorial law.[15] In a number of

[12] *E.g.*, Harris v. Settle, 322 F.2d 908 (8th Cir. 1963). In this case it was held that compulsory processes would issue on habeas corpus against prison officials only when the alleged mistreatment amounted to a cruel and unusual punishment. In McNally v. Hill, 293 U.S. 131 (1934), the United States Supreme Court followed the common law rule, holding that the writ of habeas corpus would only issue when a resolution favorable to the petitioner would result in his release from confinement. This view was reaffirmed in Parker v. Ellis, 362 U.S. 574 (1959), with four justices dissenting. There is reason to believe that the present Court would overrule *McNally* if given the opportunity to do so. One member of the *Ellis* majority (the majority opinion was per curiam) has been replaced by Justice Fortas, who normally votes with the four Justice *Ellis* minority. The dissenters in *Ellis* argued strongly for a more flexible approach to the use of habeas corpus. *Id.* at 577, 595. Since *McNally* the Court has taken an increasingly liberal view of the latitude allowable to a litigant on habeas corpus. See 44 N.C.L. REV. 844 (1966). At the Court of Appeals level, *McNally* was not followed by the Sixth Circuit Court of Appeals in Coffin v. Reichard, 143 F.2d 443 (6th Cir. 1944), where it was held that compulsory processes would issue on habeas corpus in the case of abusive, but lawful, detention of prisoners. The Court of Appeals for the Fourth Circuit and the Court of Appeals for the District of Columbia later developed their own rules. See note 10 *supra* and accompanying text. The position of the courts which do not follow the *McNally* view is based on the language of 28 U.S.C. § 2243 (1959), which provides that on a habeas corpus petition the "court shall summarily hear and determine the facts, and dispose of the matter *as law and justice require.*"

[13] REV. STAT. § 1979 (1875), 42 U.S.C. § 1983 (1964).

[14] REV. STAT. § 722 (1875), 42 U.S.C. § 1988 (1964). See, *e.g.*, Sherrod v. Pink Hat Cafe, 250 F. Supp. 516 (N.D. Miss. 1965).

[15] REV. STAT. § 1979 (1875), 42 U.S.C. § 1983 (1964). Several courts hold that this section may not be used to circumvent the exhaustion of state remedies requirement of habeas corpus. *E.g.*, Johnson v. Walker, 317 F.2d 418 (5th Cir. 1963). Other courts hold that state remedies need not be exhausted as a condition precedent to bringing suit. *E.g.*, Cooper v. Hutchinson, 184 F.2d 119 (3rd Cir. 1950). Another view is that state *administrative* remedies must be exhausted. *E.g.*, McKissick v. Durham, 176 F. Supp. 3 (M.D.N.C. 1959). It would seem that the same considerations of comity which underlie the habeas corpus exhaustion of state remedies requirement would apply to suits under this section. A novel view is to permit a Section 1983 claim for denial of a civil right to be brought up on a habeas corpus petition. U.S. *ex. rel.* McCode v. Pennsylvania, 246 F. Supp. 801 (E.D. Pa. 1965). Only one court has expressly held that a habeas corpus petition *cannot* be converted into a Section 1983 claim. U.S. v. Bibb, 249 F.2d 839 (7th Cir. 1957). Note that the District of Columbia is a territory

actions brought under this section, prisoners denied medical treatment by prison authorities have secured injunctive relief.[16]

Whichever procedure is employed, if *release* from the hospital on the basis of lack of therapy is sought, the court must face a perplexing problem. It would seem that the real power to force change in the policies of institutions such as St. Elizabeth's lies in the court's authority to order the release of patients whose presence in the community is unwanted.[17] That a maximum effective use of judicial power comprehends thwarting a basic objective of the criminal law—the segregation of dangerous persons—is reflected in the cases in which the United States Supreme Court has asserted its control over state criminal procedure. The Court's ever increasing use of the exclusionary rule in reversing state convictions figuratively raised the spectre of emptying the prisons. The states' response was to require that police respect the federal constitution as least so far as their practices related to the admissibility of evidence. This response was gradual and in proportion to the stringency of the exclusionary rule ordained at a given time. A classic example is the events surrounding the line of cases dealing with the admissibility of confessions, running from *Brown v. Mississippi*[18] to *Miranda v. Arizona*.[19] It is accurate to say that only through the

within the meaning of Section 1983. *E.g.*, Hurd v. Hodge, 334 U.S. 24, 31 (1948).

[16] *E.g.*, Edwards v. Duncan, 355 F.2d 933 (6th Cir. 1966); Talley v. Stephens, 247 F. Supp 683 (D. Ark. 1965). The textual discussion is not intended to be an exhaustive treatment of the remedies open to patients denied therapy. There are a number of possibilities: (1) state habeas corpus, where available, based on the state statute, or state or federal constitution; (2) federal habeas corpus, based on a federal statute or the federal constitution; (3) where the patient is in a federal or territorial hospital, an action under Section 1983, or a Section 1985 action for money damages; (4) a petition for an injunction or mandamus under 28 U.S.C. § 1651 (1948); (5) tort suits for money damages against state or federal officials. *E.g.*, U.S. v. Munz, 374 U.S. 150 (1963). For federal jurisdiction over Section 1983 claims see 28 U.S.C. § 1343 (1962).

[17] See Birnbaum, *The Right to Treatment*, 46 A.B.A.J. 499 (1960).

[18] 297 U.S. 436 (1936).

[19] 384 U.S. 436 (1966). The confession exclusionary rule moved from an initial reliance on factual unreliability, *e.g.*, Ward v. Texas, 316 U.S. 547 (1941), to an abandonment of any causal requirement between police conduct and the voluntariness of the confession, Ashcraft v. Tennessee, 322 U.S. 143 (1944). Yet twenty-four years after the Court had, in Brown v. Mississippi, 297 U.S. 436 (1936), established the principle that physical abuse was ground for exclusion, the Court in Reck v. Pate, 367 U.S. 433 (1960), found it necessary to reverse because the suspect had been deprived of sleep. Escobedo v. Illinois, 378 U.S. 478 (1963), abandoned the voluntariness rule altogether, and in Miranda v. Arizona, 384 U.S. 436 (1966),

power to haunt the public mind with freed criminals—however tragic the consequences—could the Court have had any impact at all on state practices.[20] So too, it seems that the most effective route, perhaps the only effective route, to achieving policy changes in public mental hospitals by judicial leverage is simply to order the release of patients who are confined without therapy.

As it was not material to disposition of the issue at hand, the *Rouse* decision did not specify when the District of Columbia court would consider release appropriate relief for patients denied therapy. The commitment and release of persons acquitted of a crime on the basis of insanity is governed by statutory standards in the District of Columbia.[21] Commitment is mandatory and summary; when release is sought the statute puts the burden on the patient to prove that he has recovered his mental health, and will not in the reasonably foreseeable future be dangerous to himself or others. The court has interpreted the dangerous propensity element to mean dangerousness which is related to a mental illness.[22] In analyzing the statute, Professors Goldstein and Katz have stated that the optimum allocation of decision making power, as between the psychiatrist and the court, is for the psychiatrist to determine whether the patient's mental health has been restored, and what propensities he has, and for the court to determine if such propensities are sufficiently dangerous to warrant further hospitalization.[23] Their position is that the court is better equipped than the psychiatrist

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the Court made it impossible for the states to admit any confession unless a detailed procedure had been first followed in the police station. So the Court has moved from a concern with prejudice to the rights to particular defendants to laying down a code of criminal procedure for the states to follow. Query whether the Court would have tread the same path had all reports of police station physical abuse, for example, ceased after Brown v. Mississippi, 297 U.S. 436 (1936). The point is that the Court has found it necessary to take extreme measures to achieve minimum objectives.

[20] Consider, for example, that in New York it is a misdemeanor for a public officer to delay taking a person under arrest before a magistrate N.Y. PEN. LAW § 1844. The statute has been in effect for eighty-six years, yet not a *single* prosecution has been reported under it. On the other hand, *immediately* after the *Miranda* exclusionary rule was decided, police officers in Los Angeles County, California, were instructed to warn all criminal suspects of their rights before questioning them. YOUNGER, DORADO-MIRANDA SURVEY (1966).

[21] D.C. CODE ANN. §§ 24-301(d), (e) (1961).

[22] Overholser v. O'Beirne, 302 F.2d 853 (D.C. Cir. 1962).

[23] Goldstein and Katz, *Dangerousness and Mental Illness, Some Observations on the Decision to Release Persons Acquitted by Reason of Insanity*, 70 YALE L.J. 227, 231 (1960).

to sense the needs of the community with respect to the risks the community is willing to take.

What will result when *Rouse v. Cameron* is superimposed on this commitment-release scheme is unforeseeable. It seems unlikely that a court can force basic policy changes by the use of compulsory processes against the hospital authorities on a case by case basis. The money, personnel and facilities necessary for therapy are simply not available.[24] And an order to the director of St. Elizabeth's requiring him to provide individualized treatment for the entire patient population would clearly be beyond the realistic limits of judicial power. Unless there is legislative initiative, it seems that a court will be faced with the knowledge that the only way to realize results—as the experience of the U.S. Supreme Court with the exclusionary rule demonstrates—is to turn patients denied therapy loose on the community. Presumably, in individual cases, the court will make a determination of dangerousness, and go through some process of balancing the interests involved.

SAMUEL HOLLINGSWORTH, JR.

Income Tax—Original Issue Discount

In a never-articulated effort to prevent tax avoidance,[1] the courts have engrafted a number of judicial concepts on the statutory definition of capital assets in spite of the all-inclusive language used by Congress.[2] By far the most famous, or infamous, of these is the assignment of income doctrine[3] which had its true beginning in

[24] The opinion of the American Psychiatric Association is that no tax-supported institution in the United States can be considered adequately staffed. U.S. SURGEON GENERAL'S AD HOC COMMITTEE ON PLANNING FOR MENTAL HEALTH FACILITIES, PLANNING OF FACILITIES FOR MENTAL HEALTH SERVICES 39 (1961).

[1] Bowden, *Assignment of Income Reconsidered,* 20 TAXES 67 (1942).

[2] The Int. Rev. Code of 1954, § 1221, defines a capital asset as all property unless it falls within one of five specifically excluded groups. Some courts have limited the class of preferred capital gains property by straining to find an exclusionary category satisfied. See, *e.g.,* Hollis v. United States, 121 F. Supp 191 (N.D. Ohio 1954).

[3] See generally, Lyon & Eustice, *Assignment of Income,* 17 TAX L. REV. 293 (1962). Another equally clear area of judicial legislation was established by Corn Prods. Ref. Co. v. Commissioner, 350 U.S. 46 (1955). There the Court conceded that futures contracts which were "an integral part of its [the company's] business" did not come within the exclusionary clauses

Lucas v. Earl[4] in 1930. The doctrine itself totally escapes definition or delineation, but in general it can be divided into two broad areas of concern with underlying policies and distinctions that crisscross the whole field of income taxation. In donative transactions the theory is to tax the donor in order to prevent the spreading of income among the members of a group to take advantage of the lower tax rates.[5] In commercial transactions the theory is to tax the sale or exchange of an income right at ordinary income tax rates so as to limit the range of preferred capital gains treatment and prevent the erosion of the ordinary income tax base.[6] It is in this later category that most of the confusion has resulted.[7]

In *United States v. Midland-Ross Corp.*,[8] the Supreme Court was faced with conflicting opinions in the circuits as to the disallowance of capital gains treatment for earned original issue discount.[9] The taxpayer bought noninterest-bearing promissory notes from the issuers at prices discounted below face value, held the notes for more than six months, and sold them for a profit. The difference between purchase price and sale price was not influenced by market fluctuations; it was conceded to be the economic equivalent of interest. Two basic elements for the application of the assignment of income doctrine were present: the character of the gain as essentially equivalent to earned ordinary interest income, and the maturity or ripeness of the accrued economic gain.[10] These two factors taken together served to deny capital gain treatment.

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of the capital asset definition, but still found that gains and losses on the sale of these contracts were ordinary gains and losses. The capital asset definition does not provide for a distinction between business property and investment property, but the Court excluded these contracts on the theory that the underlying purpose of capital asset treatment was to relieve investors from excessive hardships when they converted their investment into cash.

[4] 281 U.S. 111 (1930).

[5] Helvering v. Horst, 311 U.S. 112 (1940); Helvering v. Clifford, 309 U.S. 331 (1940); Lucas v. Earl, 281 U.S. 111 (1930).

[6] Commissioner v. P. G. Lake, Inc., 356 U.S. 260 (1958); Hort v. Commissioner, 313 U.S. 28 (1941); Burnet v. Harmel, 287 U.S. 103 (1932).

[7] See generally, Del Cotto, *Property in the Capital Asset Definition: Influence of "Fruit and Tree."* 15 BUFFALO L. REV. 1 (1965); Note, *Capital Gains: Can the Confusion be Eliminated?*, 49 IOWA L. REV. 89 (1963); Note, *The Troubled Distinction Between Capital Gain and Ordinary Income*, 73 YALE L.J. 693 (1964).

[8] 381 U.S. 54 (1965).

[9] *Id.* at 56 n.2.

[10] The presence of these two factors in combination caused an ordinary income result upon the sale of a life insurance policy immediately prior to

Using its usual definitional approach,[11] the Court determined that earned original issue discount is but interest in another form[12] and is outside the judicial definition of a capital asset.[13] The gain on the transaction was measurable and predictable and represented simply the amount earned by the investment up to the time of sale rather than an appreciation in value over a period of time. The Court concluded that realization of this profit through the sale device was essentially a substitute for payments that would, if received in another manner, be characterized as ordinary income.[14] The Court relied heavily upon the cases holding that the present realization of future ordinary income, even though cast in the form of a sale, will be taxed at ordinary income rates.[15] This principle is appropriately applied only by analogy because in *Midland-Ross* there was no sale of future income; the income element there involved had already accrued. Despite the factual distinction, the Court was logically correct in its conclusion. Since the sale of a right to future ordinary income will result in ordinary gain,[16] a fortiori, if the right to such income has

its maturity despite an ostensible compliance with the statutory requirements. Commissioner v. Phillips, 275 F.2d 33 (4th Cir. 1960).

[11] The Court relied upon its usual canon of construction that the term "capital asset" must be construed narrowly in order to afford capital gains treatment only in situations typically involving the realization of appreciation in value accrued over a substantial period of time (citing Commissioner v. Gillette Motor Transp., Inc., 364 U.S. 130 (1960)) and to exclude property representing income items or accretions to the value of a capital asset themselves properly attributable to income (citing Hort v. Commissioner, 313 U.S. 28 (1941) and Commissioner v. P. G. Lake, Inc., 365 U.S. 260 (1958)). 381 U.S. at 57.

[12] The Court illustrated the disguised interest component of original issue discount by stating, "The $6 earned on a one-year note for $106 issued for $100 is precisely like the $6 earned on a one-year loan of $100 at 6% stated interest." 381 U.S. at 58.

[13] Int. Rev. Code of 1954 § 1232(a)(2) provides that any portion of the gain attributable to original issue discount on notes or bonds issued after January 1, 1955 will be treated as ordinary income. The provision does not apply to pre-1955 notes as were involved in *Midland-Ross*.

[14] Hort v. Commissioner, 313 U.S. 28 (1941) first introduced the "substitute for ordinary income" phraseology. Since the market price of any asset represents anticipated future profits plus the discounted value of the proceeds expected upon resale, all gain on property transactions could be characterized as a substitute for ordinary income. Fortunately, the courts have not thus extended the substitute for ordinary income doctrine to its logical extreme. But compare Donald J. Jones, P-H Tax Ct. Mem. ¶ 66-136 (1966).

[15] Commissioner v. Gillette Motor Transp., Inc., 364 U.S. 130 (1960); Commissioner v. P. G. Lake, Inc., 365 U.S. 260 (1958); Hort v. Commissioner, 313 U.S. 28 (1941).

[16] *Ibid.*

already matured, and the income has been earned, its sale will similarly result in ordinary income.

An auxiliary ground for the result reached in *Midland-Ross* is the principle that where both an income producing asset and the right to accrued income from that asset are sold together, the purchase price must be allocated between the two and only the former is a capital asset.[17] As the courts recognize, the capital gains section of the Internal Revenue Code makes no distinction between an income-producing asset and the income which it produces; a literal reading of the statute would make the entire gain on the sale of the notes in *Midland-Ross* capital gain.[18] But an increasing number of courts have recently been closely scrutinizing the factor of ripeness or maturity of a taxpayer's accrued economic gain,[19] and holding that the right to collect ordinary income from a capital asset is not transmuted into capital gain by a sale of the capital asset together with the right to receive the ordinary income. Clear examples of the application of this principle can be seen in the denial of capital asset status to the sale of a partnership interest where part of the price is attributable to accrued ordinary income,[20] the sale of a life insurance policy shortly before it matures,[21] the sale of stock upon which a dividend has accrued,[22] and the sale of an orange grove where part of the value is attributable to an unmatured annual crop.[23] In *Midland-Ross,* the Court expressly approved this view, stating that the amount received on sale or retirement of the discount note must be broken down into its component parts and a differentiation made depending upon the source of the proceeds.[24]

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[17] Commissioner v. Ferrer, 304 F.2d 125 (2d Cir. 1962); Jaglom v. Commissioner, 303 F.2d 847 (2d Cir. 1962).

[18] Lubin v. Commissioner, 335 F.2d 209 (2d Cir. 1964); Jaglom v. Commissioner, 303 F.2d 847 (2d Cir. 1962).

[19] Increased interest in the factor of maturity is a result of taxpayers' recent attempts to avoid the "sale or exchange rule" denying capital gain treatment to the mere "collection" of a claim. Fairbanks v. United States, 306 U.S. 436 (1939); Ogilvie v. Commissioner, 216 F.2d 748 (6th Cir. 1954). See generally, Eustice, *Contract Rights, Capital Gain, and Assignment of Income—The Ferrer Case,* 20 TAX L. REV. 1, 20 (1964).

[20] Jaglom v. Commissioner, 303 F.2d. 847 (2d Cir. 1962); Tunnell v. United States, 259 F.2d 916 (3d Cir. 1958); United States v. Snow, 223 F.2d 103 (9th Cir. 1955); Helvering v. Smith, 90 F.2d 590 (2d Cir. 1937). The same result is now reached by Int. Rev. Code of 1954 §§ 741, 751.

[21] Phillips v. Commissioner, 275 F.2d 33 (4th Cir. 1960); Abram Nesbitt 2d, 43 T.C. 629 (1965); Boling Jones, Jr., 39 T.C. 404 (1962).

[22] Brundage v. United States, 275 F.2d 424 (7th Cir. 1960), *cert. denied,* 364 U.S. 831 (1961).

[23] Watson v. Commissioner, 345 U.S. 544 (1953).

[24] 381 U.S. at 65.

The holding of *Midland-Ross* is clearly sound. Since a gift of such income would be taxable to the donor,[25] it should follow that he cannot convert that income into capital gain through a sale or exchange. That Congress prefers such a result is evidenced by section 1232(a)(2) of the Internal Revenue Code which now expressly adopts the *Midland-Ross* result when there is an original issue discount. While obviously correct on its particular facts, the *Midland-Ross* decision is subject to misinterpretation unless a distinction is recognized between "original issue discount" which serves the function of stated interest, and "market discount" which reflects a true appreciation to capital.[26] Upon analysis of these latter gains, it becomes evident that they are not "essentially substitutes" for payments characterized as ordinary income under the gross income definition, but represent the normal appreciation in value of a capital asset due to market factors completely beyond the taxpayer's control. However, the Court specifically declined to pass upon the tax treatment of gains arising from "market discount" or attributable to fluctuations in the interest rate and market price of obligations where there has been a discount purchase.[27]

The recent decision of Donald B. Jones[28] overlooks the distinction between original issue discount and market discount, and hands down a theory which, if followed, would result in an ordinary income aspect to the sale of any item purchased at a discount. The taxpayer had purchased a contingent trust remainder in a specific dollar amount from a dealer as a speculative investment. Of course

[25] Helvering v. Horst, 311 U.S. 112 (1940) necessarily requires that income already accrued and matured at the time of gift is taxable to the donor where the underlying obligation is not concurrently given. Rev. Rul. 275, 1958-1 CUM. BULL. 22 (gift of back interest coupons taxable to donor). Commissioner v. Anthony, 155 F.2d 980 (10th Cir. 1946). See generally Lyon & Eustice, *Assignment of Income,* 17 TAX L. REV. 293, 353-62 (1962).

[26] Market discount represents the fluctuation in price of an obligation due to market factors once it has passed out of the hands of the original holder, and, unlike original issue discount, has never been classified as interest income. The distinction is discussed in Lubin v. Commissioner, 335 F.2d 209 (2d Cir. 1964) and Ted Bolnick, 44 T.C. 245 (1965). As stated in United States v. Harrison, 304 F.2d 835, 838 (5th Cir. 1962):

> The gain realized from such a transaction (bond purchased in a depressed market later redeemed at par) is a form of capital appreciation that resembles the capital gain received when stock or real estate is purchased and later sold at a profit, in contrast to an original issue discount gain which represents the interest or compensation paid for the use of money loaned.

[27] 381 U.S. at 54 n.4.

[28] Donald J. Jones, P-H Tax Ct. Mem. 66-136 (1966).

the purchase was at a considerable discount because of the many risks involved. The Court of Appeals for the Third Circuit ignored the fact that the discount element was a product of the risks inherent in such a purchase and remanded to the Tax Court to determine what portion of the gain was attributable to interest income in the nature of "issue discount."[29] The Tax Court determined that the purchaser had received a six percent interest discount that would be taxable as ordinary income. The result gives the commissioner authority for asserting that in all discount purchases there is an imputed interest element which will not qualify for capital gains treatment. Such a theory would appear to be erroneous because it transposes the imputed interest factor from the deferred payment sales context[30] into the entirely distinct discount purchase context. Further, it results in the denial of capital gain treatment to the normal appreciation of an admitted capital asset due to market factors, and ignores the fact that the condemnation in *Midland-Ross* resulted because that discount was the economic equivalent of interest.

R. WALTON MCNAIRY, JR.

Labor Law—Effect of 9(c)3 on Duty to Bargain

The Labor Management Relations Act, section 9(c)3, prohibits holding a representation election in a bargaining unit "within which in the preceding twelve-month period, a valid election shall have been held."[1] The issue in *Conren, Inc. v. NLRB*[2] was whether this prohibition prevents enforcement of an order to bargain issued because of the employer's refusal, nine and one-half months after the union had lost an election, to grant recognition on the basis of authorization cards signed by a majority of his employees.

The Court of Appeals for the Seventh Circuit enforced the NLRB's order to bargain, with Circuit Judge Kiley dissenting. The majority reasoned that the affirmative reference to "election" in 9(c)3 should not be construed to preclude representation based

[29] Jones v. Commissioner, 330 F.2d 302 (3d Cir. 1964).
[30] Int. Rev. Code of 1954, § 483.

[1] 61 Stat. 143 (1947), 29 U.S.C. § 159(c)3 (1964).
[2] 368 F.2d 173 (7th Cir. 1966), *cert. denied*, 35 U.S.L. Week 3330 (U.S. Mar. 21, 1967).

upon a majority showing achieved by means less formal than an election. The absence, in 9(c)3, of any reference to less formal means, such as authorization cards, was construed as an express exclusion of such means. The court asserted that to hold otherwise would "usurp a legislative prerogative."[3]

The legislative history of 9(c)3 can hardly be construed to support the majority view. Before enactment of the Labor Management Relations Act, the NLRB had evolved a "reasonable time rule" that protected a union's certified status, usually for one year, after it had won an election.[4] Even while the NLRB was following this "reasonable time rule" one authority[5] argued that the policy of the act, to encourage "the practice and procedure of collective bargaining and . . . [to protect] the exercise by workers of full freedom of association,"[6] could best be achieved through a period of stability following an election. He analogized a representation election to any election in our society in which the results are final:

> Similar considerations would seem to require that once a bargaining representative has been duly designated, that designation, except in extraordinary circumstances, must, in the interest of stability, remain operative for a reasonable period of time and cannot be revoked at every whimsy of the electorate. . . . *The price of freedom to bargain collectively is responsibility in the exercise of the freedom of choice.*[7]

In 9(c)3 Congress codified the administratively evolved doctrine of the "reasonable time rule" and applied it also to situations in which a union had lost an election. The majority report of the bill explained the change this "election bar" would make:

> This amendment [9(c)3] prevents the board from holding elections more often than once a year . . . . At present, if the union loses, it may on the presentation of additional membership cards

[3] *Id.* at 174.

[4] See Brooks v. NLRB, 348 U.S. 96, 98 (1954), in which Justice Frankfurter discusses Board practice before enactment of the Taft-Hartley Act.

[5] Bernard Cushman was serving as Chief of the Legislative and Bureau Services Section of the Solicitor's Office, Department of Labor, when he wrote the article cited.

[6] National Labor Relations Act (Wagner Act) § 1, 49 Stat. 449 (1935), 29 U.S.C. § 151 (1964).

[7] Cushman, *The Duration of Certifications by the NLRB and the Doctrine of Administrative Stability,* 45 MICH. L. REV. 1, 8 (1946). (Emphasis added.)

secure another election within a short time, but if it wins its majority cannot be challenged for a year.[8]

In the absence of any clarifying debate, the inference that Congress intended this "election bar" to include less formal means of gaining recognition after an election had been lost seems at least as justified as the majority's inference that Congress intended to exclude such means.[9] The "industrial stability" which Congress sought to insure by enactment of 9(c)3[10] is considerably weakened if the "election bar" is interpreted as not precluding less formal means of achieving representation rights.

An election results in either formal designation of a bargaining agent or formal repudiation of any representation. The issue in *Conren* was whether informal designation of a bargaining agent will be allowed in situations where formal designation by election is not permitted. No other case has considered this question. Decisions of federal courts and the NLRB, however, have ruled that the act prevents informal repudiation of a union majority within a year after formal designation.[11] An election victory for a union compels the employer to bargain with the certified union even after he receives notice that a majority of his employees no longer wish to be represented by the union. The Supreme Court held, in *Brooks v. NLRB*,[12] that this result was necessary because:

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[8] S. REP. No. 105, 80th Cong., 1st Sess. 25 (1947). Senator Taft commented on this provision, 9(c)3, stating: "The bill also provides that elections shall be held only once a year so that there shall not be a constant stirring up of excitement by continual elections." 93 CONG. REC. 3838 (1947). The Senate amendment was adopted by the conference committee in lieu of the House amendment which would have allowed a decertification election inside of a year upon petition by employees. 93 CONG. REC. 6375 (1947) (report of conference committee).

[9] What is today known as the *Joy Silk* doctrine, an order to bargain without election upon showing of majority support, had been judicially recognized by Judge Learned Hand in NLRB v. Federbush Co., 121 F.2d 954, 956 (2d Cir. 1941). It is therefore just as reasonable to assume that Senator Taft knew of this situation and intended to include it as to assume he either did not know of the decision or else intended to exclude it.

[10] See Brooks v. NLRB, 348 U.S. 96, 103 (1954) (underlying purpose of statute is industrial peace); Colgate-Palmolive-Peet Co. v. NLRB, 338 U.S. 355, 362 (1949) (stability of labor relations was primarily objective of Congress); NLRB v. Holly-General Co., 305 F.2d 670 (9th Cir. 1962).

[11] See Brooks v. NLRB, 348 U.S. 96 (1954); NLRB v. Holly-General Co., 305 F.2d 670 (9th Cir. 1962); Montgomery Ward & Co., 162 N.L.R.B. No. 27 (1966).

[12] 348 U.S. 96 (1954).

> Congress has discarded common-law doctrines of agency. It is contended that since a bargaining agency may be ascertained by methods less formal than a supervised election, informal repudiation should also be sanctioned where decertification by another election is precluded. This is to make situations that are different appear the same.[13]

The Supreme Court, finding in the act a policy of industrial stability, refused to sanction informal procedures, within a year after an election, that were designed to determine a union's representation rights. Thus it would appear that Judge Kiley's contention that "the converse of the holding in *Brooks* ought to control this decision [*Conren*]" is correct.[14]

The most persuasive ground for Judge Kiley's dissent in *Conren* was the "congressional purpose of the act . . . and . . . the spirit of the developing statutory law."[15] Relying on *Brooks,* he pointed out that the concept of industrial stability was the guiding principle behind the one-year spacing of elections enacted by 9(c)3 and that solicitation of cards within a year of the valid election "is as disruptive of industrial peace as a second election."[16]

A second ground for dissent involved consideration of the reliability of informal means in determining a union's majority status. Reviewing several cases, Judge Kiley concluded that the policy of the NLRB and the courts was to accept only the most reliable means "in order to insure the employees' freedom of choice."[17] Since the union has lost a valid election within a year, the less reliable showing of majority status by authorization cards should preclude charging Conren with an 8(a)5[18] violation.

The dissenting opinion implies that recognition of such informal

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[13] *Id.* at 103, 104. The Court also discussed the policy behind the "election bar" including responsibility of the electorate, renunciation of choice by a procedure equally as solemn as the first, and minimization of strife. *Id.* at 99, 100.

[14] Conren, Inc. v. NLRB, 368 F.2d 173, 177 (7th Cir. 1966) (dissenting opinion). In NLRB v. Holly-General Co., 305 F.2d 670, 675 (9th Cir. 1962), the court enumerated three reasons for following *Brooks* when a union had been informally repudiated eleven months after an election: (1) stability in labor-management relations, (2) ease in enforcement by the Board, and (3) clear delineation of the time for good faith bargaining.

[15] 368 F.2d at 175.

[16] *Id.* at 177.

[17] *Id.* at 176.

[18] "It shall be an unfair labor practice for an employer . . . to refuse to bargain collectively with the representatives of his employees . . . . 49 Stat. 452 (1935), 29 U.S.C. § 158(a)5 (1964).

means would be an unwarranted extension of the *Joy Silk*—"no good faith doubt"—rule. The NLRB applies this rule when issuing an order to bargain[19] after a union has acquired a majority of authorization cards and made a demand to bargain upon an employer who refuses to bargain but has no good faith doubt that the union represents a majority of his employees.[20] Judge Kiley felt that an employer, regardless of the prohibition in 9(c)3, could indeed have a good faith doubt about a union's majority status within a year after a formal election. Judge Kiley might also have related this policy of accepting only the most reliable determination of a union's status to his argument for industrial stability, the purpose the courts have found in the act.

Congress in 9(c)3 barred any election for a period of one year after a valid election. Since this most formal means of establishing a bargaining relationship has been precluded by affirmative Congressional action, it would seem illogical to assert that a less formal and less reliable[21] means of establishing a bargaining relationship should be allowed to subvert the policy of industrial stability fostered by the act. This seems to be the gist of the Supreme Court's opinion in *Brooks*. Such reasoning is implicit, though not articulated, in Judge Kiley's dissent.

Since common-law doctrines of agency have been abolished,[22] and Congress has clearly made labor-management relations a matter

[19] The Labor Management Relation Act (Taft-Hartley Act) § 9(c)1, 61 Stat. 144 (1947), 29 U.S.C. § 159(c)1 (1964), provides the only means for certification, an election. An order to bargain is not certification and the period of time that an employer must bargain in good faith after such an order is in the Board's discretion. See NLRB v. Pool Mfg. Co., 339 U.S. 577 (1950); NLRB v. Mexia Textile Mills, 339 U.S. 563 (1950).

[20] In Snow & Sons, 134 N.L.R.B. 709, 710 (1961), *enforced*, 308 F.2d 687 (9th Cir. 1962), the NLRB stated that "the right of an Employer to insist upon a Board-directed election is not absolute." Furthermore, "where the employer's unfair labor practices are clearly established . . . the good faith of his doubts of the union majority may properly be regarded with some suspicion." NLRB v. Cumberland Shoe Corp., 351 F.2d 917, 921 (6th Cir. 1965).

[21] See Comment, *Union Authorization Cards*, 75 YALE L.J. 805 (1966). "Authorization cards are an unreliable index of employee choice. Compared with the secret ballot they replace, their solicitation is a woefully defective process . . . ." *Id.* at 818. See also NLRB v. Johnnie's Poultry Co., 344 F.2d 617 (8th Cir. 1965), in which a union received twenty-seven votes after acquiring fifty-five cards. More than a year later when the union again sought to bargain with the employer, the Court of Appeals for the Eighth Circuit reversed a NLRB order to bargain holding that employer had a good faith doubt as to the union's majority status.

[22] See note 13 *supra* and accompanying text.

of federal policy, an analogy to elections in a political context is valid. Employees' freedom of choice exercised in a formal election should be binding, short of an unusual circumstance, until another election is possible. Congress has sought to establish a period of stability after an election. This formality of an election is meaningless if the NLRB can, within one year after an election, disrupt the stability by issuing orders to bargain, based upon showings of majority status attained through informal means. Stability in labor-management relations can best be achieved within a context of certainty. Decisions such as *Brooks* make this certainty mandatory when an election results in victory for a bargaining agent. To apply a different rule when a certified election results in defeat of a union is arbitrary and unfair.

GEORGE CARSON II

Labor Law—'Outsiders' As Agents of the Employer

Any coercive, antiunion activities by persons acting as agents of an employer covered by the Labor Management Relations Act[1] will be imputed to him and the union concerned will have a remedy before the National Labor Relations Board.[2] However, those persons found not to be agents are beyond the reach of the law and consequently are free to continue at will their antiunion activities. Thus, an important aspect of labor legislation is the concept of agency, as it will often determine employer responsibilities.

Under the original provision of the Wagner Act of 1935,[3] the term "employer" included "any person acting in the interests of an employer, directly or indirectly. . . ."[4] Using this language of the act, the NLRB imputed to employers the actions of third parties, even those only remotely connected with the employer.[5] This was

[1] Labor Management Relations Act (Taft-Hartley Act) § 2(2), 61 Stat. 137 (1947), 29 U.S.C. § 152(2) (1965).

[2] Hereinafter referred to as NLRB.

[3] Act of July 5, 1935, § 2(2), 49 Stat. 450.

[4] Act of July 5, 1935, § 2(2), 49 Stat. 450.

[5] H.R. REP. No. 244, 80th Cong., 1st Sess., 18 (1947). The committee report said:

> The Board frequently "imputed" to employers anything that anyone connected with an employer, no matter how remotely, said or did, notwithstanding that the employer had not authorized the action and in many cases had even prohibited it.

Ibid.

done even though there existed no principal-agent relationship.[6] However, Congress, in passing the Taft-Hartley Act of 1947, deleted the above language and inserted in section 2(2) language more favorable to management by defining an employer as including "any person acting as an agent of an employer, directly or indirectly. . . ."[7] The purpose of this section seems to have been to restrict the prior liberal agency principles of the Wagner Act by requiring a common law principal-agent relationship between the employer and the third party.[8] At the same time, in section 2(13) of the Taft-Hartley Act, Congress also provided that in determining whether a person is acting as an agent of another, "the question of whether the specific acts performed were actually authorized or subsequently ratified shall not be controlling."[9] This section was apparently designed primarily to liberalize prior strict agency principles applicable to *unions* so that they would be more amenable to unfair labor practice charges and suits for damages in courts of law.[10]

Where supervisory employees commit the alleged coercive acts, these sections seem to have effected little change in the law that existed prior to their enactment. In general the cases rely upon *International Assoc. of Machinists v. NLRB*,[11] decided before

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To the same effect Sen. Pepper said:

> Under present law [prior to 1947], it is not necessary to have a directly authorized agent of a corporation to bind it if a wrong is done a worker. If a trade association acted *in the interests* and *with the point of view* of the employer, the employer, therefore, might have been responsible for a large number of acts of people acting in his interests against workers. . . . [The Taft-Hartley Bill] . . . carefully limits the employers liability to the acts of duly authorized agents.

93 CONG. REC. 6521 (1947). (Emphasis added.)

[6] H.R. REP. No. 244, 80th Cong., 1st Sess., 18 (1947).

[7] Labor Management Relations Act (Taft-Hartley Act) § 2(2), 61 Stat. 137 (1947), 29 U.S.C. § 152(2) (1965).

[8] See note 5 *supra*. See also 93 Cong. Rec. 7001 (1947).

[9] Labor Management Relations Act (Taft-Hartley Act) § 2(13), 61 Stat. 137 (1947), 29 U.S.C. § 152(13) (1965).

[10] Section 2(13) was directed primarily at labor. Prior to the Taft-Hartley Act, the Supreme Court held in United Brotherhood of Carpenters & Joiners v. United States, 330 U.S. 395 (1947), that very strict rules of agency were applicable to unions. The proponents of the Taft-Hartley Act wanted to enact laws prohibiting union unfair labor practices and to give employers rights to sue for damages in courts of law. So they enacted section 2(13) to insure that the rule of *United Brotherhood of Carpenters* would not be applied by liberalizing the law of agency applicable to unions. See 93 CONG. REC. 7000 (1947). See also UMW v. Patton, 211 F.2d 742 (4th Cir. 1954).

[11] 311 U.S. 72 (1940).

sections 2(2) and 2(13) were enacted. There the Court held that the employer was liable for the unauthorized acts of supervisory employees. It indicated that if strict principles of *respondeat superior* were to be applied, the employer might not be liable.[12] While the legislative history indicates that section 2(2) was designed in part to overrule the *Machinists* case,[13] the courts seem consistently to cite section 2(13) for the proposition that the decision has not been overruled. In *NLRB v. Arkansas-Louisiana Gas Co.*,[14] the court said that in "interpreting . . . [section 2(13)] . . . the courts have held that strict principles of agency are not required . . . in determining an employer's liability for the union activities of its supervisory employees."[15]

Where unauthorized activities are carried on by "outsiders" or "volunteers," the real change created by these sections appears. These outsiders are non-employees, such as local police, businessmen, public officials, religious leaders, or members of the employer's family. Generally, by applying these sections the NLRB is able to impute outsiders' acts to the employer on the basis of apparent authority or ratification where there is some nexus of identification between the employer and the outsider such that the employees could

[12] *Id.* at 80.

[13] "The apparent intention of the redefinition of section 2(2) is to change the rule, adopted by the Supreme Court in International Association of Machinists v. NLRB (311 U.S. 72), that an employer is responsible for the actions of his supervisory employees, even though he might not be under strict common law rules." 93 CONG. REC. 6660 (1947) (remarks of Sen. Murray). Senator Murray was an opponent of the Taft-Hartley Act. No statement could be found in the legislative history by any proponent of the Act specifically stating that the *Machinists* case was to be overruled. However, Senator Taft repeatedly said that the intention was to require the application of common law agency principles, which the Court in *Machinists* had refused to do. See 93 CONG. REC. 4561, 6690, 7001 (1947).

[14] 333 F.2d 790 (8th Cir. 1964).

[15] *Id.* at 796. In Local 636, Plumbing & Pipe Fitters Independent of the United States v. NLRB, 287 F.2d 354, 359 (D.C. Cir. 1961), it was said: "We know of nothing in the Act of 1947 or in the Labor-Management Reporting and Disclosure Act of 1959, 29 U.S.C.A. § 401 *et seq.*, which affects the vitality of . . . [the *Machinists* doctrine]." See also NLRB v. Champa Linen Service Co., 324 F.2d 28 (10th Cir. 1961); NLRB v. Des Moines Foods Inc., 296 F.2d 285 (8th Cir. 1961); NLRB v. Birmingham Publishing Co., 262 F.2d 8 (5th Cir. 1969).

Where non-supervisory, rank and file employees commit the unlawful acts, the employer generally will not be liable unless he authorizes or ratifies such conduct. Daykin, *Liability of Unions and Employers Under the Labor-Management Relations Act*, 42 IOWA L. REV. 370, 371 (1957).

reasonably assume that the outsider spoke with his approval.[16] This determination is, of course, a factual one and depends upon the circumstances of each case. For example, where the outsider is a member of the employer's family, the NLRB has little difficulty in imputing these acts to the employer since the family relationship gives rise to the requisite identification between the employer and the third party.[17]

Applying this same rationale, the NLRB has also found principal-agent relationships where the outsiders are local businessmen or public officials. These determinations are usually based upon facts that indicate a close relationship between the employer and the outsider, such as where the outsiders helped to establish the plant[18] or where the employer allowed them to come to the plant to make unlawful speeches.[19] When this relationship exists, the employer will be liable even though he had no knowledge of the outsider's antiunion activity.[20] However, he can escape liability if he effectively disavows the outsiders' acts and communicates his disavowal to the employees.[21] If no effective disavowal is made, he will be deemed to have acquiesed in the illegal acts of the outsiders.[22] Where no close relationship exists, it seems that the common law agency requirements of section 2(2) prevent imputing the

[16] See, *e.g.*, Colson Corp. v. NLRB, 347 F.2d 128 (8th Cir.), *cert. denied* 382 U.S. 904 (1965).

[17] See, *e.g.*, Star Baby Co., 140 N.L.R.B. 678 (1963); Forston Co., 139 N.L.R.B. 561 (1962); Mansbach Metal Co., 83 N.L.R.B. 797 (1953); Taylor Mfg. Co., 83 N.L.R.B. 142 (1949).

[18] *E.g.*, Colson Corp. v. NLRB, 347 F.2d 128 (8th Cir.), *cert. denied* 382 U.S. 904 (1965); A. M. Andrews Co., 112 N.L.R.B. 626 (1956).

[19] *E.g.*, Byrds Mfg. Co., 140 N.L.R.B. 147 (1962); Pearson Corp., 138 N.L.R.B. 910 (1962); Wayline, Inc., 81 N.L.R.B. 511 (1949). *Cf.* Livingston Shirt Co., 107 N.L.R.B. 400 (1948).

However, the rules normally applied to outsiders are not followed where the police engage in anti-union activity. At least one circuit has indicated that it is more difficult to impute the acts of police to the employer, even where they are engaging in coercive activity, because they also act within the scope of their legal duty. See NLBR v. Bibb Mfg. Co., 188 F.2d 825 (5th Cir. 1951); NLRB v. Russel Mfg. Co., 187 F.2d 296 (5th Cir. 1951).

[20] Pearson Corp., 138 N.L.R.B. 910 (1962). *But see* Byrds Mfg. Co., 140 N.L.R.B. 147 (1962).

[21] The disavowal is not sufficient to allow the employer to escape liability unless it is communicated to the employees. NLRB v. Fulton Bag & Cotton Mills, 175 F.2d 675 (5th Cir. 1949); Indiana Metal Products, 100 N.L.R.B. 1040 (1952). And the employer cannot wait until the last minute before making his disavowal known to his employees. See Colson Corp. v. NLRB, 347 F.2d 128 (8th Cir.), *cert. denied* 382 U.S. 904 (1965).

[22] *E.g.*, Byrds Mfg. Co., 140 N.L.R.B. 147 (1962); Wayline, Inc., 81 N.L.R.B. 511 (1949).

acts of outsiders to the employer. The aggrieved union does have a remedy in representation election cases. Here, notwithstanding the lack of an agency relationship, the NLRB will set aside the election where the laboratory conditions necessary for a free election have been destroyed.[23]

The recent case of *Amalgamated Clothing Workers v. NLRB*[24] is an example of application of the above rules. There the local businessmen of a small town were desirous of improving its economy. They were successful in inducing a large shirt manufacturer to locate a subsidiary, the respondent company, there. They agreed to float a bond issue to finance a permanent physical plant, and also recommended certain people for jobs. Within a short period of time the Amalgamated Clothing Workers began to organize. At the same time, the local businessmen, fearful that the plant would move if unionized, began their antiunion campaign. They enlisted the support of a local minister who spoke to his parishioners, many of whom were employees, to the effect that the plant might move. Workers were visited in their homes and were told of adverse economic conditions that might follow if the union were successful in its organization of the plant. An advertisement was placed in the local paper asking that the workers vote "no" at the representation election. Although the employer did not engage in the open antiunion campaign and stated that the plant would not move if the union came in, he was at one time evasive when questioned on this point.

The trial examiner found the outsiders' acts to be in violation of section 8(a)(1)[25] and imputed them to the employer.[26] The NLRB adopted his opinion as its own and enforcement was granted by the Circuit Court of Appeals for the District of Columbia.[27] The trial examiner found that the employer did not authorize the outsiders to speak for him in that there was "no evidence that the

[23] See, *e.g.*, James Lee & Sons, 130 N.L.R.B. 290 (1961); Monarch Rubber Co., 121 N.L.R.B. 81 (1958); Great Atl. & Pac. Tea Co., 120 N.L.R.B. 765 (1958); Falmouth Co., 114 N.L.R.B. 896 (1955).

[24] 63 L.R.R.M. 2581 (D.C. Cir. Dec. 15, 1966), *enforcing* Hamburg Shirt Corp., 156 N.L.R.B. No. 51 (Dec. 30, 1965).

[25] National Labor Relations Act § 8(a)(1), 41 Stat. 452 (1935), 29 U.S.C. § 158(a)(1) (1965), reads "It shall be an unfair labor practice for an employer—(1) to interfere with, restrain, or coerce employees in the exercise of their rights guaranteed in section 7;. . . ."

[26] 156 N.L.R.B. No. 51 at 18.

[27] 63 L.R.R.M. 2581 (D.C. Cir. Dec. 15, 1966).

respondent requested these men to make such threats."[28] He said it was apparent that "they did so of their own volition . . . [because] they feared that the respondent would not accept the plant if the union came in. . . ."[29] Notwithstanding this lack of actual authority, the employer was found liable in that his silence was taken as a ratification of the acts of the businessmen.[30]

Three factors seem to underlie this decision. First, the local businessmen, after initially identifying themselves with the employer, continued to be more than mere "passive spectators"[31] in that they spoke to employees about their shortcomings in terms of output and production. Also, they not infrequently visited the plant. Second, the employer himself engaged in questionable activity, which the court termed "marginal promises of benefit and portents of reprisal to avoid recognizing the union until its status could be undermined."[32] Third, the employer failed to unequivocally repudiate the acts of the outsiders, and was evasive as to whether the plant would move if the union were successful in its organization drive.[33]

Clothing Workers represents the traditional approach taken by the NLRB where outsiders engage in antiunion activity. However, certain language of the court of appeals seems to have opened the way for a return to the principles of the Wagner Act.[34] The court affirmed the NLRB finding that the employer had ratified the outsiders' acts.[35] In so doing the court relied upon section 2(13) for the proposition that "responsibility . . . is not controlled by the law of agency."[36] This language seems to indicate that by utilizing section 2(13), the agency hurdles of section 2(2) may be overcome to expand employer responsibility to cover a broader range of conduct on the part of non-employees who engage in unlawful acts.

In recent congressional hearings several union leaders pointed out the problems of outside community pressure to the House Subcommittee on the National Labor Relations Board.[37] The sub-

[28] 156 N.L.R.B. No. 51 at 18.
[29] *Ibid.*
[30] *Ibid.*
[31] 63 L.R.R.M. at 2583.
[32] *Id.* at 2583.
[33] *Id.* at 2583.
[34] See note 3 *supra* and accompanying text.
[35] 63 L.R.R.M. at 2583.
[36] *Id.* at 2583.
[37] STAFF OF SUBCOMM. ON THE NATIONAL LABOR RELATIONS BOARD, HOUSE COMM. ON EDUCATION AND LABOR, 87TH CONG., 2D SESS., ADMINIS-

committee heard testimony that some outside community pressure exists in the form of local liscensing ordinances that purport to require liscensing for soliciting membership in organizations or distributing literature.[38] While the constitutionality of these ordinances has been successfully challenged,[39] the necessary litigation results in frustrating delay.[40] The subcommittee found that this form of community pressure was violative of rights secured by the Constitution and laws of the United States, often occurring under color of law, and recommended that the Department of Justice determine whether the situation could be dealt with under existing civil rights statutes.[41] It remains to be seen whether criminal prosecutions can be had under the civil rights statutes of those found to be acting pursuant to these ordinances.[42] In the meantime it is hoped that

TRATION OF THE LABOR-MANAGEMENT RELATIONS ACT BY THE NLRB 59-61 (Comm. Print 1961). The committee report said in part:

> This subcommittee has received testimony that union organizers have been physically escorted by local law enforcement agents to the town limits and told not to return. This subcommittee has received evidence that town bankers call in loans of union adherents on the eve of elections. This subcommittee has received evidence that local merchants, including grocers, inquire as to the prounion attitude of the customer before extending credit.

One union leader testified that "these volunteers are no more volunteers than the Chinese Communists that invaded North Korea against the United Nations. They are nothing but willing henchmen and associates of employers." Statement of Jacob Scheinkman, General Counsel, Amalgamated Clothing Workers, AFL-CIO, *Hearings Before the Subcommittee on the National Labor Relations Board of the House Committee on Education and Labor*, 87th Cong., 1st Sess., Pt. 1, at 601 (1961) [hereinafter cited as *1961 Hearings*].

[38] *1961 Hearings* Pt. 1, at 562.

[39] See, *e.g.*, Denton v. The City of Carrolton, 235 F.2d 481 (5th Cir. 1956).

[40] *1961 Hearings* Pt. 1, at 562.

[41] STAFF OF SUBCOMM. ON THE NATIONAL LABOR RELATIONS BOARD, note 37 *supra*.

[42] The pertinent civil rights statutes are 18 U.S.C. §§ 241, 242 (1950). Section 242 makes it illegal to deny, under color of law, inhabitants of the United States their rights secured by the Constitution or laws of the United States. Research reveals no reported case wherein a person has been charged under this provision of violating another's section 7 rights. See note 43 *infra*. Section 241 makes it illegal for two or more persons to conspire to injure, threaten, intimidate, or oppress any citizen in the exercise or enjoyment of any right or privilege secured to him by the Constitution or laws of the United States. In United States v. Bailes, 120 F. Supp. 614 (S.D.W.Va. 1954), the defendants were charged under section 241 with conspiring to violate a person's right under section 7 *not* to join, form, or assist a labor union. The court held that section 241 protected rights that citizens possess as such or rights wholly dependent upon an act of Congress. The court said that the right not to join a union did not fall within either

courts will follow the precedent of *Clothing Workers,* i.e., the application of liberal agency principles. Such results would appear desirable since outside community pressure seems a major obstacle to the attainment of basic section 7 rights,[43] one that merely setting aside the representation election cannot fully remedy.[44]

TOMMY W. JARRETT

Labor Law—Representation Elections—Union Right to Employee Mailing Lists

In February, 1966, the National Labor Relations Board expounded a new rule governing future cases involving representation elections. The rule provides that after an election has been agreed to by the parties or directed by the regional director, the employer is required to "file with the Regional Director an election eligibility list, containing the names and addresses of all the eligible voters. The Regional Director, in turn, shall make this information avail-

category because section 7 rights are guaranteed to *employees,* not to citizens generally and because the right not to join a union, as guaranteed in section 7, is not wholly dependent upon an act of Congress because this right is only the embodiment of employees' pre-existing rights. *Id.* at 628. The court also stated that the NLRB and not the courts is to determine what constitutes an unfair labor practice. Furthermore, the court reasoned that since the Taft-Hartley Act only covers acts by employers, unions, or their agents, the states, and not the federal government, must punish others who might conspire to violate the rights of workers. *Id.* at 631. See also United States v. Moore, 129 Fed. 630 (N.D.Ala. Cir. 1904), where the court held that section 241 was not available to protect a miner in his right to organize because this right existed because of his status as an employee, not because of his being a citizen. *Cf.* UMW v. Patton, 211 F.2d 742 (4th Cir. 1954) (court denied recovery of punitive damages).

[43] Section 7 is the basic provision of labor law. It reads in part: Employees shall have the right to self-organization, to form, to join, or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in other concerted activities for mutual aid or protection, and shall also have the right to refrain from any or all such activities. . . . National Labor Relations Act § 7, 41 Stat. 452 (1935), as amended, Labor Management Relations Act (Taft-Hartley Act) § 7, 61 Stat. 140 (1947), 29 U.S.C. § 157 (1965).

[44] Once the requisite laboratory conditions have been upset, it seems that they, to a large degree, remain so during the second election. It was found that after the election was "tainted," the party losing has about a one-in-three chance of winning the second. Pollitt, *NLRB Re-Run Elections,* 41 N.C.L. REV. 209 (1963). Also, it seems that antiunion elements, particularly in the South, have a ready made issue to use against unions in the form of race hate. See Pollitt, *The National Labor Relations Board and Race Hate Propaganda in Union Organizational Drives,* 17 STAN. L. REV. 373 (1965).

able to all parties in the case."[1] Noncompliance with this rule is grounds for setting the election aside.[2] The basis for this rule seems to be the imbalance in opportunity for each side in the election proceeding to reach the electorate with its arguments, an imbalance felt by the NLRB to exist when employee mailing lists are not made available to the labor organization involved.[3] The NLRB said,

> [W]e regard it as the Board's function to conduct elections in which employees have the opportunity to cast their ballots for or against representation under circumstances that are free not only from interference, restraint, or coercion violative of the Act, but also from other elements that prevent or impede a free and reasoned choice. Among the factors that undoubtedly tend to impede such a choice is a lack of information with respect to one of the choices available.[4]

In support of its ruling the NLRB maintained that "by providing all parties with employees' names and addresses, we maximize the likelihood that all the voters will be exposed to the arguments for, as well as against, union representation."[5] Additional reasons given were that mailing lists are usually not available from other sources,[6] and that the rule set forth here is commonly found in other election settings.[7] The Board rejected the employer's arguments that a valid

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[1] Excelsior Underwear Inc., 156 N.L.R.B. No. 12 (Feb. 4, 1966).

[2] *Id.* at —. The rule as announced was to be applied prospectively only, to elections directed or consented to thirty days from the date of decision, this "to insure that all parties to forthcoming representation elections are fully aware of their rights and obligations as here stated." *Id.* at n.5.

In ruling as it did the NLRB was apparently well within its authority. "Congress has entrusted the Board with a wide degree of discretion in establishing the procedure and safeguards necessary to insure the fair and free choice of bargaining representatives by employees." NLRB v. A. J. Tower Co., 329 U.S. 324, 330 (1946). See, *e.g.*, NLRB v. Waterman S.S. Corp., 309 U.S. 206, 226 (1940).

[3] As a practical matter, an employer, through his possession of employee names and home addresses as well as his ability to communicate with employees on plant premises, is assured of the continuing opportunity to inform the entire electorate of his views with respect to union representation. On the other hand, without a list of employee names and addresses, a labor organization, whose organizers normally have no right of access to plant premises, has no method by which it can be certain of reaching all the employees with its arguments in favor of representation, and, as a result, employees are often completely unaware of that point of view.

156 N.L.R.B. at —.

[4] *Id.* at —.

[5] *Id.* at —.

[6] *Id.* at —.

[7] *Id.* at —. Examples cited were public, shareholder, and intraunion elections.

property interest exists in such a mailing list,[8] that the employees' rights are infringed by the giving out of such a list without their consent,[9] that the Board's rule creates a danger of harassment and coercion of the employees in their homes,[10] and that other avenues of union communication with the employees are available.[11] In both its rule and its reasoning, the NLRB had the prior support of many commentators.[12]

Another reason given by the NLRB in behalf of its new rule was that there is a public interest in the speedy resolution of questions of representation. The NLRB maintained that with

> little time (and no home addresses) with which to satisfy itself as to the eligibility of the 'unknowns', the union is forced either to challenge all those who appear at the polls whom it does not know or risk having ineligible employees vote. The effect of putting the union to this choice, we have found, is to increase the number of challenges, . . . thus requiring investigation and resolution by the Regional Director or the Board. Prompt disclosure of employee names as well as addresses will, we are convinced, eliminate the necessity for challenges based solely on lack of knowledge as to the voter's identity.

Id. at —.

[8] The NLRB found that there was not an employer interest here of such significance as to warrant protection. *Id.* at —.

[9] The NLRB found no merit in this argument, pointing out that the employees could express their wishes by their vote in the election. *Id.* at —.

[10] The NLRB maintained that such union conduct cannot be assumed, but that if it happened, the Board would provide an appropriate remedy. *Id.* at —.

[11] Rejecting this argument the NLRB maintained that "the existence of alternative channels of communication is relevant only when the opportunity to communicate made available by the NLRB would interfere with a significant employer interest." Since there is no significant employer interest in the secrecy of the names and addresses of his employees, there is no need for the NLRB to consider the existence of alternative channels of communication. *Id.* at —.

[12] See, *e.g.*, SUBCOMM. ON NATIONAL LABOR RELATIONS BOARD, HOUSE COMM. ON EDUCATION AND LABOR, 87TH CONG., 1ST SESS., ADMINISTRATION OF THE LABOR MANAGEMENT RELATIONS ACT BY THE NLRB 4 (Comm. Print 1961); Bok, *The Regulation of Campaign Tactics in Representation Elections under the National Labor Relations Act*, 78 HARV. L. REV. 38, 99-100 (1964); Pollitt, *The National Labor Relations Board and Race Hate Propaganda in Union Organization Drives*, 17 STAN. L. REV. 373, 407 (1965); Note, 72 YALE L.J. 1243, 1263-64 (1963). See also, Summers, *Judicial Regulation of Union Elections*, 70 YALE L.J. 1221, 1227-28 (1961).

In attempting to enforce its *Excelsior* rule by means of a subpoena ordering production of the employee mailing list, the NLRB has two successes in federal district courts. NLRB v. Rohlen, 64 L.R.R.M. 2168 (N.D. Ill. 1967), and NLRB v. Wolverine Indus. Div., 64 L.R.R.M. 2060 (E.D. Mich. 1966). In enforcing the NLRB's subpoena, both decisions found the merits of the cases involved to be in accord with the finding in

As a general proposition, in representation cases the NLRB strives to cure any imbalance which tends to prevent the voters from being fairly informed of the issues involved in the election.[13] Where employees are denied a free and fair election choice, the results may be set aside even though there has been no commission of an unfair labor practice.[14] A brief examination of some earlier cases may aid in explaining how the Board reached the *Excelsior* decision.

One group of cases demonstrates that the Board has long balanced the employer's right to free speech against the employees' right to have a free choice in selecting their bargaining representative. At times the result was a finding that an employer's speech amounted to an unfair labor practice,[15] especially if the Board felt that the employees had been restrained or coerced in the exercise of their rights to organize and to engage in collective bargaining.[16] In 1947, Section 8(c),[17] the so-called "free speech proviso," was added to the National Labor Relations Act. It limited the NLRB in its finding of an unfair labor practice in this situation to cases in

Excelsior. No express jurisdictional issue was discussed in *Wolverine*. In *Rohlen* jurisdiction was based expressly on 61 Stat. 150 (1947), 29 U.S.C. § 161(2) (1964) (§ 11(2) of the N.L.R.A.), which gives United States district courts jurisdiction to issue orders enforcing Board subpoenas "to produce evidence" or "to give testimony touching the matter under investigation," and 28 U.S.C. § 1337 (1964), which gives the district courts jurisdiction over "any civil action or proceeding arising under any Act of Congress regulating commerce." In two other similar cases, the NLRB was unsuccessful. NLRB v. Hanes Hosiery Div., 63 L.R.R.M. 2513 (M.D.N.C. 1966), and NLRB v. Montgomery Ward & Co., 64 L.R.R.M. 2061 (M.D. Fla. 1966). Neither decision ruled on the merits of *Excelsior*, both decisions declining jurisdiction to enforce the NLRB's subpoena. In *Hanes* jurisdiction was expressly denied under 61 Stat. 150 (1947), 29 U.S.C. § 161(2) (1964) on the ground that an employee mailing list had no relation to "evidence" or "testimony touching the matter under investigation." The court also declined, in its discretion, to take jurisdiction under 28 U.S.C. § 1337 (1964). Jurisdiction in *Montgomery Ward* was denied on the same ground as in *Hanes*.

[13] In election proceedings, it is the Board's function to provide a laboratory in which an experiment may be conducted, under conditions as nearly ideal as possible, to determine the uninhibited desires of the employees. It is our duty to establish those conditions; it is also our duty to determine whether they have been fulfilled. When, in the rare extreme case, the standard drops too low, because of our fault or that of others, the requisite laboratory conditions are not present and the experiment must be conducted over again.
General Shoe Corp., 77 N.L.R.B. 124, 127 (1948).

[14] *Id.* at 126.

[15] NLRB v. Federbush Co., 121 F.2d 954 (2d Cir. 1941).

[16] *But see* NLRB v. Virginia Elec. & Power Co., 314 U.S. 469 (1941).

[17] 61 Stat. 140 (1947), 29 U.S.C. § 158(c) (1964).

which the employer's speech amounted to a "threat of reprisal or force or promise of benefit."[18] However, many other cases decided subsequent to the passage of 8(c) have held that even though the employer's speech was not an unfair labor practice, it might nevertheless upset the requisite "laboratory conditions" surrounding an election to such an extent that a new election was necessary.[19]

In another group of cases the NLRB has employed a balancing process in deciding the validity of company rules prohibiting union solicitation or the distribution of union literature on company property. In the solicitation situation the Board must balance the right of employees to organize against the right of the employer to maintain discipline in his establishment.[20] The Board has said that a rule which prohibits solicitation by an employee on company property outside of working hours "must be presumed to be an unreasonable impediment to self-organization and therefore discriminatory in the absence of evidence that special circumstances make the rule necessary in order to maintain production or discipline."[21] Distribution of union literature is distinguished from solicitation, since distribution could result in littering work areas and impinging on the employer's right to engage in production. Therefore, the employer can limit distribution to non-work areas of his establishment, but a rule prohibiting employees from distributing literature anywhere on the employer's premises is invalid on its face.[22] Another distinction that is made in this area is that between organizing activities by employee and non-employee. An example is found in *NLRB v. Babcock & Wilcox Co.*,[23] in which the nondiscriminatory refusal of the employer to permit distribution of union literature by non-employee union organizers on company-owned parking lots was held not to have unreasonably impeded the employees' right to self-organization because the locations of the plants and of the living quar-

[18] Section 8(c) by its terms is limited to situations involving unfair labor practices and not those in which representation elections can be set aside because of the employer's speech.

[19] See, *e.g.*, Lord Baltimore Press, 142 N.L.R.B. 328 (1963) (election set aside where employer's promise to litigate was coupled with statements which pointed out that union might cause a strike and pursue other policies detrimental to the employees); Sewell Mfg. Co., 138 N.L.R.B. 66 (1962) (inflammatory mass of race hate literature by the employer to defeat union organizational attempts).

[20] Republic Aviation Corp. v. NLRB, 324 U.S. 793, 797-98 (1945).

[21] Peyton Packing Co., Inc., 49 N.L.R.B. 828 (1943).

[22] Stoddard-Quirk Mfg. Co., 138 N.L.R.B. 615 (1962).

[23] 351 U.S. 105 (1956).

ters of the employees did not place the employees beyond the reach of reasonable efforts of the unions to communicate with them by other means. However, where there are no other avenues of approach open to the union in its organization attempts, it is an unfair labor practice for the employer to deny the union access to its premises.[24]

Earlier cases having a more direct bearing on *Excelsior* are those in which the labor organization has sought an opportunity to reply to antiunion speeches made by the employer, a situation analogous to the union's demand for a mailing list in *Excelsior*. In *Bonwit Teller, Inc.*,[25] the employer had a no-solicitation rule which forbade solicitation during working and non-working time on the selling floors of a department store.[26] Pre-election antiunion speeches were made to employees in the selling areas but the employer refused the union's request for an opportunity to reply on equal terms. The Board's order required the employer to cease and desist from making such antiunion speeches unless, upon request, a like opportunity was accorded to the labor organization against which the speeches were directed. On appeal the Court of Appeals for the Second Circuit limited the Board's order to the extent that if the employer abandoned his broad no-solicitation rule, he would be free to make antiunion speeches without having to accord the union equal time.[27] The NLRB nevertheless continued to apply its "equal opportunity" principle in several later cases[28] until, in *Livingston Shirt Corp.*,[29] that principle was rejected by a majority of the Board.[30] In *Livingston* the employer, who had a no-solicitation rule in effect, made

[24] See NLRB v. Stowe Spinning Co., 336 U.S. 226 (1949), where the NLRB was upheld in finding an unfair labor practice where the employer discriminated against the labor organization by denying it the use of a company-owned meeting hall which was the only available meeting hall in a company town.

[25] 96 N.L.R.B. 608 (1951).

[26] Such a broad rule was privileged in the case of retail department stores. Famous-Barr Co., 59 N.L.R.B. 976, 981 (1944).

[27] Bonwit Teller, Inc. v. NLRB, 197 F.2d 640, 646 (2d Cir. 1952).

[28] Stow Mfg. Co., 103 N.L.R.B. 1280 (1953); Onondaga Pottery Co., 103 N.L.R.B. 770 (1953); Seamprufe, Inc., 103 N.L.R.B. 298 (1953); Metropolitan Auto parts, Inc., 102 N.L.R.B. 1634 (1953).

[29] 107 N.L.R.B. 400 (1953).

[30] [T]hat [*Bonwit Teller*] view rested on the belief that the employer exerted undue and unlawful influence upon the employees by monopolizing their workplace as a speechmaking platform. NLRB appraisal of the basic elements underlying this type of situation

noncoercive antiunion speeches to the employees, but refused to allow equal time to the union. The Board ruled that

> [I]n the absence of either an unlawful broad no-solicitation rule (prohibiting union access to company premises on other than working time) or a privileged no-solicitation rule (broad, but not lawful because of the character of the business), an employer does not commit an unfair labor practice if he makes a pre-election speech on company time and premises to his employees and denies the union's request for an opportunity to reply.[31]

This viewpoint was seemingly approved by the Supreme Court in *NLRB v. United Steelworkers of America*[32] [Nutone, Inc.], where the employer used methods of persuasion forbidden to the employees by a no-solicitation rule. The Court said that if "the opportunities for effectively reaching the employees with a pro-union message, in spite of a no-solicitation rule, are at least as great as the employer's ability to promote the legally authorized expression of his antiunion views, there is no basis for invalidating these 'otherwise valid' rules."[33] However, in that case there was no request made by the union for equal time so it may be maintained with certainty that the Supreme Court was approving the Board's denial of equal time to the union. Finally, in *The May Co.*,[34] the NLRB reaffirmed its "equal opportunity" rule in regard to retail department stores.[35] There, the Board recognized that the employer, because of the character of its business, was privileged to adopt a no-solicitation rule covering both working and nonworking time even though such a rule significantly restricted the employees' self-organization rights by foreclosing discussion of the advantages and disadvantages of organization among employees at their place of work. The Board

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persuades us that the Act does not require the employer, absent unusual circumstances, to accede to such a union request.

Id. at 405.

[31] *Id.* at 409.

[32] 357 U.S. 357 (1958).

[33] *Id.* at 364.

[34] 136 N.L.R.B. 797, *enforcement denied,* 316 F.2d 797 (6th Cir. 1963).

[35] "[T]he Board and court holding in the *Bonwit Teller* case, which we consider to be legally sound, squarely controls the issue in the present case." *Id.* at 799. The Court of Appeals for the Sixth Circuit reversed and denied enforcement of the NLRB's order, May Dep't Stores Co. v. N.L.R.B., 316 F.2d 797 (6th Cir. 1963), but the NLRB has continued to affirm its holding in *May.* See Montgomery Ward & Co., Inc., 145 N.L.R.B. 846, 848 n.4 (1964).

found that when the employer used the company premises and company time to make an antiunion speech to the employees, he "created a glaring imbalance in organizational communication." The Board then ruled that the employer could give such speeches but that he was under an obligation, in order to allow a proper balance to be maintained, to accede to the union's request to address the employees under similar circumstances.[36]

After *May,* the status of the law was that the NLRB was imposing an "equal time" rule on an employer only in retail department store cases and then only when the employer had in effect a broad, but privileged, no-solicitation rule. In other cases a union request for equal opportunity to address the employees has been refused where other avenues of approach have been open.[37] *Excelsior* seems to make an inroad on this practice since awarding the union a mailing list goes far toward putting it on a par with the employer.

In *General Elec. Corp.,*[38] decided the same day as *Excelsior,* the Board was asked to apply its department store rule of "equal time" to the industry in general. It refused, primarily because of its *Excelsior* ruling, saying that

> [I]n light of the increased opportunities for employees' access to communications which should flow from *Excelsior,* but with which we have, as yet, no experience, . . . we prefer to defer any reconsideration of current Board doctrine in the area of plant access until after the effects of *Excelsior* become known.[39]

After more than a year of NLRB administrative experience with the *Excelsior* rule, it appears safe to assume the rule has resulted in sufficient union accessability so that a stiffer rule is not needed at this time.[40]

GEORGE L. LITTLE, JR.

Taxation—Interest Deductions—Sham and Business Purpose Tests

The Internal Revenue Code of 1954 provides, "There shall be allowed as a deduction all interest paid or accrued within the taxable

[36] 136 N.L.R.B. at 802.
[37] NLRB v. United Steelworkers of America [Nutone, Inc.], 357 U.S. 357 (1958).
[38] 156 NLRB No. 112 (Feb. 4, 1966).
[39] *Id.* at —.
[40] See note 11 *supra* for cases in which the Board has sought to enforce its *Excelsior* rule in federal district court.

year on indebtedness."[1] Under this provision, interest is deductible without regard to whether the indebtedness is incurred in a trade or business, in connection with a profit-making activity, or in a purely personal matter.[2] The section, on its face, would allow deduction of all interest paid by any taxpayer, corporate or individual, with respect to a loan transaction between the taxpayer and lending agency.[3] Through several rationales the federal courts have imposed a "judicial amendment" on this section by which interest deductions are disallowed if the taxpayer could realize an economic gain only because of a reduction in taxes. These rationales have hinged, entirely or partially, on the courts' finding an absence of genuine indebtedness. A recent trend is to refrain from using this fiction of a lack of indebtedness and to base deductibility on the circumstances motivating the taxpayer to enter the loan arrangement.

The courts have imposed various, but somewhat analogous, tests to prohibit such deductions. One test, dating from pre-1960, involves a fiction by which the courts refuse to recognize a bona fide creditor-debtor relationship within the intent of the code. In 1960 a business purpose test was introduced to disallow an interest deduction if a transaction has no economic reality beyond a potential tax deduction, but this test has been clouded by continued insistence that genuine indebtedness is not present. A recent case[4] recognizes an actual indebtedness and applies the business purpose test without regard to the nature of the loan manipulation.

The pre-1960 test, which has continued to be applied in some circuits, may be divided into two categories. In the first the courts find a lack of indebtedness, resulting from the relationship of the parties, where there is no apparent intention that the transaction be binding on the parties. This is illustrated by *Woodward v. United States*[5] where the taxpayer made his wife a gift of insurance policies on his life. The wife later assigned the policies back to the taxpayer pursuant to a plan of placing the policies in trust for the wife and a

[1] INT. REV. CODE of 1954, § 163(a).

[2] STANLEY & KILCULLEN, THE FEDERAL INCOME TAX § 163 (4th ed. 1961). The section also states, "Sec. 163 (Interest) states somewhat too broadly that all interest paid or accrued within the taxable year on indebtedness is deductible."

[3] Deductibility of interest paid by a taxpayer with respect to his obligation to a third party, where the original loan transaction was between the lending agency and the third party, will not be considered.

[4] Goldstein v. Commissioner, 364 F.2d 734 (2d Cir. 1966).

[5] 208 F.2d 893 (8th Cir. 1953).

son. The taxpayer executed demand notes, equal to the cash value of the policies, payable to his wife and claimed deductions for the interest purportedly paid. In disallowing the deductions, the court found that there was no indebtedness and that the money paid was still the taxpayer's. It labeled the arrangement as camouflage and as acts of benevolence.[6]

The second category involves transactions, both arm's length and collusive, that are treated as shams, therefore failing to create indebtedness within the intent of the statutory deduction. In *Jockmus v. United States*[7] the taxpayer procured 1,000,000 dollars face amount United States Treasury Notes for a purchase price of 973,750 dollars. In plan, the taxpayer bought the notes from a securities corporation that purchased them from the original seller and delivered them to a finance and loan corporation (Corporate). Corporate loaned taxpayer the purchase price secured by the treasury notes. Meanwhile, Corporate directed a brokerage firm to make a short sale of 1,000,000 dollars in treasury notes which was accomplished by sale to the original seller. In actuality, the original seller delivered the notes to an exchange bank and then accepted redelivery of the same notes. All of the other transactions, except the taxpayer's promissory note to Corporate, were book entries only, and no money changed hands. Taxpayer borrowed 30,000 dollars from another finance and loan corporation (Court) and prepaid Corporate 41,384 dollars interest on the purchase price loan. The brokerage firm contrived the scheme, created Corporate as a loaning agency "front" with very limited capital, and controlled Court.

The court disallowed the interest deduction after finding a lack of a bona fide creditor-debtor relationship[8] as evidenced by Corporate's failure to advance funds or to obtain possession of the notes as security and by the intricate manipulations completely cancelling each other. Rather than a loan arrangement, the resulting obligation was labeled a contractual right to future delivery of the securities upon payment of an agreed price which was the amount of the purported loan.

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[6] *Cf.*, Foresun, Inc. v. Commissioner, 348 F.2d 1006 (6th Cir. 1965).

[7] 335 F.2d 23 (2d Cir. 1964).

[8] See, *e.g.*, Dooley v. Commissioner, 332 F.2d 463 (7th Cir. 1964); Gheen v. Commissioner, 331 F.2d 470 (6th Cir. 1964); Lewis v. Commissioner, 328 F.2d 634 (7th Cir. 1964), *cert. denied*, 379 U.S. 821 (1964); Nichols v. Commissioner, 314 F.2d 337 (5th Cir. 1963); Goodstein v. Commissioner, 267 F.2d 127 (1st Cir. 1959).

Taxpayer in *Jockmus* contended this transaction should be allowed since it was an arm's length transaction with the arrangements made by the brokerage firm, rather than by the taxpayer.[9] The court refused to distinguish the case from *Lynch v. Commissioner*[10] where interest deductions were disallowed in a similar plan but where the prearranged collusive scheme was known to and directed by the taxpayer.[11]

The case law in this area was expanded when the business purpose test, as applied to interest deductions, was advanced in *Knetsch v. United States*.[12] During 1953 the taxpayer purchased ten, thirty-year, 400,000-dollar face amount, single premium annuity bonds, bearing interest at two and one-half per cent annually, for an initial outlay of 4,000 dollars. The remaining purchase obligation was met by taxpayer "borrowing" 4,000,000 dollars from the insurance company, executing three and one-half per cent notes secured by the annuity bonds, and prepaying interest of 140,000 dollars. The annuity contract enabled the taxpayer to keep the cash or loan value reduced to 1,000 dollars by borrowing against each year's incremental increase at the beginning of the year in which the increase was to be realized. Five days after the initial purchase, the taxpayer borrowed 99,000 dollars of the first year's scheduled increase with a further prepayment of interest. Similar borrowing in 1954 and

[9] *Accord,* MacRae v. Commissioner, 294 F.2d 56 (9th Cir. 1961), where the court disallowed the deductions in an "arm's length transaction" and also stated that the payments made were in reality consideration for tax deductions, not for loans, hence, were not deductible as interest under the code. *Contra,* L. Lee Stanton, 34 T.C. 1 (1960).

[10] 273 F.2d 867 (2d Cir. 1959).

[11] The court relied on the often cited phrase, "Save in those instances where the statute itself turns on intent, a matter so real as taxation must depend on objective realities, not on the varying subjective beliefs of individual taxpayers." 335 F.2d at 28.

[12] 364 U.S. 361 (1960). The district court rendered judgment for the United States by disallowing the deduction and the court of appeals affirmed. 272 F.2d 200 (9th Cir. 1959). The Supreme Court granted certiorari due to a suggested conflict with United States v. Bond, 258 F.2d 577 (5th Cir. 1958), where deductions were upheld upon a finding that the transaction appeared, in form, to be what the statute intended, i.e., interest paid on indebtedness, and despite the realities of the transaction.

A sidelight to the Knetsch affair is the taxpayer's later attempt to deduct his out-of-pocket costs, under INT. REV. CODE OF 1954, § 165(c)(2), as a loss sustained in a transaction entered into for profit or, alternatively, under INT. REV. CODE OF 1954 § 212 as an ordinary and necessary expense incurred in the management and maintenance of property held for the production of income. The deduction was disallowed on both grounds in Knetsch v. United States, 172 Ct. Cl. 378, 348 F.2d 932 (1965).

1955 maintained the cash and loan value at 1,000 dollars. In 1956 he terminated the contract, surrendered the bonds, obtained cancellation of his indebtedness, and received the 1,000 dollars cash surrender value. For taxable years 1953 and 1954, the only taxable years involved, the taxpayer paid 290,570 dollars as interest, received 203,000 dollars in loans, and attempted to realize a tax savings of 233,297 dollars by deduction of interest.

The Supreme Court applied a business purpose test by which an interest deduction is disallowed if no economic gain is realized, or could be realized, beyond a tax deduction. The Court stated that the tax reduction motive or intent is immaterial and that the determinative question is "whether what was done, apart from the tax motive, was the thing which the statute intended."[13] This statutory intent as to indebtedness was found to be lacking since the taxpayer did not appreciably affect his beneficial interest except to reduce taxes.

While *Knetsch* added another rule to the Commissioner's repertory for disallowing interest deductions, its inherent value was weakened by the Court's further finding of no genuine indebtedness and, particularly, by its labeling the transaction as a sham. It has been suggested that a finding of sham is not compatible with a business purpose test.[14] The reasoning is that an indebtedness is not recognized in sham transactions, while a business purpose test should be applicable irrespective of a valid creditor-debtor relationship.

The uncertainty ensuing from the dual standard articulated in *Knetsch* is illustrated by *Bridges v. Commissioner*.[15] The taxpayer purchased 500,000 dollars face amount treasury notes for 486,875 dollars. A bank loaned 500,000 dollars on his promissory note, secured by the treasury notes, and the taxpayer prepaid interest of 19,687 dollars. A brokerage firm obtained the notes, arranged the financing, and forwarded the notes to the bank. The bank sold the notes at maturity and cancelled the indebtedness. Taxpayer's only involvement was signing the promissory notes. He claimed the interest as a deduction in 1956, when his adjusted gross income was

[13] 364 U.S. at 365. The Court adopted the business purpose test invoked to disallow capital gains treatment for securities distributed in a corporate liquidation in Gregory v. Helvering, 293 U.S. 465 (1935).

[14] Fuller, *Business Purpose, Sham Transactions and the Relation of Private Law to the Law of Taxation*, 37 TUL. L. REV. 355 (1963); Note, 46 CORNELL L.Q. 649 (1961).

[15] 325 F.2d 180 (4th Cir. 1963).

95,582 dollars, and reported 13,125 dollars as a long-term capital gain in 1957.

The court, relying on *Knetsch,* discussed the absence of a beneficial gain other than a tax deduction but seemed to support its disallowance of the deductions by finding that no genuine indebtedness existed and that the transaction was a sham. The court pointed to the taxpayer's outlay of more funds than he could possibly receive by an acceleration in value of the securities and emphasized that he never had uncontrolled use of the additional money, of the securities, or of the interest on the securities.

The potential of the business purpose test, divorced from the sham aspects, began to emerge in *Minchin v. Commissioner.*[16] The taxpayer prepaid interest on the purchase price loan for two ten-year, 200,000 dollar, single premium annuity contracts, the sole security for the loan. The annuity contracts provided for reduced interest on the loans after the sixth year and for deferment of the loan repayment until just prior to maturity of the annuities. The court relied on *Knetsch* and the business purpose test to disallow the interest deduction.[17] Due to the shorter deferred period and reduced interest payments after the sixth year, the court expressed doubt about the lack of genuine indebtedness aspects and did not call the transaction a sham. It adopted the view that such a net actual loss places the burden of showing the economic reality of the transaction on the taxpayer.

The business purpose test reached full bloom, unfettered by a sham stigma, in *Goldstein v. Commissioner*[18] where the taxpayer won a 1958 Irish Sweepstakes of 140,000 dollars. Apart from the sweepstakes proceeds, taxpayer and her husband had an income of 904 dollars for 1958. She borrowed 945,000 dollars in December 1958, purchased 1,000,000 dollars face amount Treasury Notes, pledged the notes as collateral for the loan, and prepaid interest of 81,396 dollars. The Tax Court,[19] following *Knetsch,* found as an

[16] 335 F.2d 30 (2d Cir. 1964). The *Knetsch* and *Minchin* litigation should be unnecessary today due to INT. REV. CODE OF 1954 § 264(a)(2) which disallows deduction of "any amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance, endowment, or annuity contract." This provision is only applicable to annuity contracts purchased after March 1, 1954.

[17] *Accord,* Kaye v. Commissioner, 287 F.2d 40 (9th Cir. 1961).

[18] 364 F.2d 734 (2d Cir. 1966).

[19] Kapel Goldstein, 44 T.C. 284 (1965). For a student note on the Tax Court decision, see 19 VAND. L. REV. 194 (1965).

ultimate fact that the taxpayer's purpose was not to derive an economic gain but solely to secure a large interest deduction as an offset to the sweepstakes proceeds, and held the transaction to be a sham.

The court of appeals rejected the sham or bona fide creditor-debtor rationale by pointing out that an *actual* loan arrangement existed which was indistinguishable from any other legitimate loan transaction. It found a transaction that had no substance, utility, or purpose beyond the tax deduction and stated that a deduction should not be allowed "when it objectively appears that a taxpayer has borrowed funds in order to engage in a transaction that has no substance or purpose aside from the taxpayer's desire to obtain the tax benefit of an interest deduction."[20] The court, further, appeared to adopt the dissenting view of *Gilbert v. Commissioner*[21] where Judge Learned Hand expressed his dislike of labeling transactions as "no substantial economic reality," "sham," or "dependent on the substance of the transaction" to bring them within the intent of the tax statutes and proposed a test that would turn on the taxpayer's motives at the time of entering the transaction.[22]

Application of the *Goldstein* view would result in disallowance of any interest deduction, irrespective of the type of loan manipulations, where it objectively appears that the taxpayer had no anticipation of an economic gain other than a tax benefit. By recognizing that an actual indebtedness exists, this view considers the realities of a loan obligation between creditor and debtor, which the previous tests glossed over, and avoids the fiction that no such genuine situation is present. It is still open for the taxpayer to obtain his deduction by showing that he entered the transaction as a purposive activity, to be financed through borrowing, with a reasonable expectation of economic gains.

In approximately seven years since its introduction into the interest deduction area, the business purpose test has evolved from an initial association with the sham considerations to a complete separation of these approaches and rejection of the sham test. The other

[20] Goldstein v. Commissioner, 364 F.2d 734, 741 (2d Cir. 1966).

[21] 248 F.2d 399, 410 (2d Cir. 1957) (L. Hand, J., dissenting). The majority disallowed deduction of a bad debt claim.

[22] *Id.* at 412 where Judge Hand stated, "When the petitioners decided to make their advances in the form of debts, rather than of capital advances, did they suppose that the difference would appreciably affect their beneficial interests in the venture, other than taxwise."

federal courts should adopt the independent application of this test[23] which enables a more realistic evaluation of the taxpayer's motives and the statutory intent in determining the deductibility of interest.

WILLIAM H. THOMPSON

Torts—Medical Malpractice—Rejection of "But for" Test

In *Hicks* v. *United States*[1] a navy doctor failed to test for bowel obstruction in a patient who complained of severe abdominal pains. The patient, treated only for a "bug," died some eight hours later, suffering from a strangulation of the intestine. On the basis of expert testimony, the doctor was found to have been negligent in failing to diagnose the obstruction. There was also testimony that if a correct diagnosis had been made, an immediate operation would have saved the patient's life. Testimony apparently was not given to indicate whether an immediate operation could have been performed or to indicate what dangers such an operation would have involved, if any.[2] On the basis of this testimony the Court of Appeals for the Fourth Circuit held that the trial judge was compelled to find negligence and "cause in fact" and to award a verdict to the plaintiff. The evidence of cause in fact is probably sufficient to meet the orthodox tests, but the court apparently rejected the usual test of cause in fact, saying that

> When a defendant's negligent action or inaction has effectively terminated a person's chance of survival, it does not lie in the defendant's mouth to raise conjectures as to the measure of the chances that he has put beyond the possibility of realization. If there was any substantial possibility of survival and the defendant has destroyed it, he is answerable.[3]

[23] The close family relationship will continue to pose a problem if it appears the taxpayer was "borrowing" his own money. In this situation the realities of a loan obligation may not be present.

[1] 368 F.2d 626 (4th Cir. 1966).

[2] The patient suffered from diabetes as well as from an "abnormal congenital peritoneal hiatus with internal herniation. . . ." *Id.* at 629. It seems doubtful that a layman could estimate the likelihood or non-likelihood of the patient's survival under these conditions, especially without knowing whether qualified personnel were on hand to operate. Compare George v. City of New York, 253 N.Y.S.2d 550 (Sup. Ct. 1964) where a barium enema penetrated the bowel wall; an operation was immediately performed, but the patient died. Nevertheless, the testimony in *Hicks* that an operation would probably have been successful is no doubt sufficient evidence of cause.

[3] 368 F.2d at 632.

This test evidently means that the defendant is liable, not only if his negligence in fact caused the injury suffered, but also if his negligence eliminated some "substantial" "chance" the plaintiff might have had of escaping injury even where actual causation cannot be shown.[4]

It is usually said that to hold a defendant liable for his negligence, a plaintiff must prove that the negligence was a "cause-in-fact" of the harm.[5] This cause-in-fact requirement is established when the plaintiff shows that, "but for" the defendant's negligent act the plaintiff would not have been injured.[6] If, on the other hand, the plaintiff would have been injured even without the defendant's negligent conduct, it is said that the negligence is not a cause-in-fact of the harm and the plaintiff may not recover. The "orthodox" view is that the plaintiff must prove facts showing causation, just as he must prove the other elements of his case, by a greater weight of the evidence. As with other matters of proof, this means that he must prove facts showing "but for" causation is more likely than not.[7] Courts sometimes depart from this orthodox view and hold that "causation" is sufficiently established if it is shown that defendant's negligence *may* have caused harm—that is, if the defendant's negligence reduced plaintiff's chances of escaping an injury.[8] This is the kind of view applied in *Hicks* to medical mal-

[4] Even a "substantial" chance may be less than a likely chance. A 10% chance may be "substantial," though it falls far short of any likelihood. The defendant has terminated the chance, whatever it is, and that seems to be enough under the court's test, so long as the chance is "substantial." The orthodox "but-for" test requires more than the termination of a ten percent or even a forty per cent chance; it requires a *likelihood* that the plaintiff would have avoided injury "but for" the defendant's negligence. This orthodox rule is sometimes abandoned; but there is, perhaps, a tendency to stay with it in malpractice cases. See Malone, *Ruminations on Cause-in-Fact,* 9 STAN. L. REV. 60, 87, n.66 (1956).

[5] See, *e.g.,* Waugh v. Suburban Club Ginger Ale Co., 83 App. D.C. 226, 167 F.2d 758 (1948); RESTATEMENT (SECOND), TORTS §§ 281, 431, 432 (1965).

[6] RESTATEMENT (SECOND), TORTS § 432 (1965); PROSSER, TORTS 242 (3d ed. 1964).

[7] See Bockman v. Butler, 224 Ark. 125, 271 S.W.2d 918 (1954) (recognizing that probability "will suffice," but holding that no one should mention this to the jury); Silvers v. Wesson, 122 Cal. App. 902, 266 P.2d 169 (1954).

[8] The Fourth Circuit had earlier applied this view in a case not involving malpractice; Gardner v. National Bulk Carriers, Inc., 310 F.2d 284, 91 A.L.R.2d 1023 (4th Cir. 1962), *cert. denied,* 372 U.S. 913 (1963). On this point generally, see Malone, *Ruminations on Cause-in-Fact,* 9 STAN. L. REV. 60 (1956).

practice cases, although it is probably correct, as Professor Wex Malone has supposed, that the plaintiff in medical malpractice cases "must usually establish the causal probabilities beyond peradventure."[9] Certainly there are decisions that clearly reject the very liberal view in *Hicks*,[10] though perhaps there are other malpractice cases that at least do not require "certainty."[11]

The "but for" test of cause-in-fact, plus the traditional rule that puts upon the plaintiff the burden of proving this cause, has many potentialities for injustice. As a result, courts have more or less admittedly done away with the cause-in-fact requirement—or at least with the "but for" test—in several lines of cases. These are primarily cases involving two or more wrongdoers or at least two or more "causes" of the plaintiff's harm.

One line of such cases is quite familiar: two drivers of automobiles are negligent and together cause a collision in which plaintiff is injured. Even if the acts of negligence are separated in time, the drivers may be called "concurrent tortfeasors" in many cases and they will be held liable together for the plaintiff's injuries, at least if those injuries are not separable and capable of being attributed in a certain part to each wrongdoer.[12] In such cases it is clear enough that one of the wrongdoers may be paying for injury he did not "cause" in fact under the "but for" test. A second line of cases

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[9] *Id.* at 86.

[10] Silvers v. Wesson, 122 Cal. App. 902, 266 P.2d 169 (1954): "It may well be that the chances of a patient's living longer . . . might, by early observation and treatment, be increased from ten percent to forty percent. But that is certainly not proof that such early observation and treatment would probably result in curing a cancer. . . ." In this case the doctor negligently (it is assumed) failed to examine cystoscopically, and accordingly did not discover a bladder tumor for two years. The court denied recovery on the ground that, even if the doctor had examined earlier, the cancer might have been incurable by that time anyway. Harries v. United States, 350 F.2d 231 (9th Cir. 1965) (must be probability or better formula, as in *Silvers* case). Sturm v. Green, 398 P.2d 799 (Okla. 1965) (no tests made, but no evidence whether they would have revealed deficiency, therefore failure to give tests is not shown to be causal of patient's death; court also held "no negligence.")

[11] *E.g.*, Price v. Neyland, 115 App. D.C. 355, 320 F.2d 674, 99 A.L.R.2d 1391 (1963); Walden v. Jones, 289 Ky. 395, 158 S.W.2d 609, 141 A.L.R. 105 (1942).

[12] Watts v. Smith, 375 Mich. 120, 134 N.W.2d 194 (1965), 44 N.C.L. REV. 249 (1965). The argument is largely gaged in terms of what injuries are "indivisible." See Maddux v. Donaldson, 362 Mich. 425, 108 N.W.2d 33 (1961). But see Caygill v. Ipsen, 27 Wis. 2d 578, 135 N.W.2d 284 (1965) (no joinder of defendants allowed where plaintiff alleged accidents five months apart in separate counties.)

is similar, but goes further. In the second line two defendants are negligent, and the plaintiff is injured as the result of the negligence of one of them, but no one is able to say which. For example, two hunters fire shotguns in the direction of the plaintiff. A pellet from one of the guns strikes the plaintiff. Both defendants are held liable,[13] though clearly enough one of them is not causal of any harm at all to the physical person of the plaintiff. A third line of cases may go even further. A fire is set by lightning and without negligence; if allowed to burn, it will (probably) harm the plaintiff's home. Another fire is negligently set by defendant. It combines with the first fire and the combined fire burns plaintiff's home. Under some cases[14] at least, defendant will apparently be held liable, even though the plaintiff would have suffered the same harm anyway. In cases like the shotgun-firing cases, each defendant is either the cause of the harm or the cause of obscuring the facts about causation. If both *A* and *B* fire, one of them hit the plaintiff and should be liable for that reason; the other, by firing, has made it impossible for us to know which fired the pellet that caused the harm. For this reason we feel justified in holding both liable.[15] Similar feelings prevail in the multiple automobile collision situation. The fire situation, however, goes further, where one fire is not set by anyone's fault. In such a situation, defendant's conduct in setting the fire is not causal under the "but for" test nor does it obscure the liability of anyone else, as in the hunter cases. These cases, then, reflect a certain amount of judicial agreement that at least in some circumstances cause in fact or "but for" is not an element to be insisted upon.

In other kinds of cases, however, where there is only one alleged cause of the plaintiff's harm, the results are mixed. There are cases in which courts have, in one way or another, eliminated the cause-in-fact requirement altogether, either by ignoring the problem[16] or by so enlarging the defendant's duty that he is liable if he causes

[13] Summers v. Tice, 33 Cal. 2d 80, 199 P.2d 1 (1948) (a leading case, rejecting the "concert of action" theory used in some cases.)

[14] Anderson v. Minneapolis, St. P. & S. St. M.Ry., 146 Minn. 430, 179 N.W. 45 (1920).

[15] See PROSSER, TORTS 243 n.24 (3d ed. 1964), and cases cited note 16 *infra*.

[16] See Rice v. Norfolk So. R.R., 167 N.C. 1, 82 S.E. 1034 (1914), where defendant negligently allowed drains to stop up; this created a pond. Later plaintiff, who lived in the vicinity, got malaria. A recovery was allowed.

the plaintiff to lose the "chance" of escaping injury or death.[17] Thus, for example, if the master of a ship does not make a reasonable effort to find the seaman who has fallen overboard, the master is liable, even though it is not at all probable that the seaman could be saved. In such a case, the defendant has a duty to use care to increase the seaman's chances, and it is enough for liability that the defendant's negligence is a cause-in-fact of the seaman's loss of a *chance.*[18]

On the other hand, there are many cases in which courts have been over-insistent upon proof of cause-in-fact. An establishment dealing with radioactive material negligently fails to provide its employees sufficient protection and they get cancer, but recovery may be denied because the employee has no means of proving causation.[19] Or the defendant sprays a tobacco crop from the air, and witnesses see a substance falling from the airplane over plaintiff's commercial fish ponds; later the fish jump and then die; but recovery is denied because causation is not proved by these facts.[20] Or the defendant negligently stores flammables and a fire breaks out nearby and spreads to the plaintiff's premises; but recovery is denied because causation is not proved by these facts.[21] Or defendant's defective machine spouts oil in plaintiff's eye, which burns and within 24 hours gets much worse; but recovery is denied because causation is not proved by these facts.[22] Some of these cases, at least, evince an impossibly strict notion of the value of circumstantial evidence.[23]

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[17] Malone, *Ruminations on Cause-in-Fact,* 9 STAN. L. REV. 60 (1956) is an excellent discussion.

[18] Gardner v. National Bulk Carriers, 310 F.2d 284, 91 A.L.R.2d 1023 (1962), *cert. denied,* 372 U.S. 913 (1963).

[19] Mahoney v. United States, 220 F. Supp. 823 (E.D. Tenn. 1963), *aff'd,* 339 F.2d 605 (6th Cir. 1964).

[20] Wall v. Trogdon, 249 N.C. 747, 107 S.E.2d 757 (1959); *cf.* Western Geophysical Co. v. Martin, 253 Miss. 14, 174 So. 2d 706 (1965) (well suddenly contaminated after underground blasts, cause not proved).

Inferences might be drawn against plaintiff on the causal issue if he does not produce all the evidence he has. In *Western Geophysical, supra,* the plaintiff did not examine the pump in his well. This clearly aided the court in holding against him. The court said, "This inference [of causation] is unnecessary because if the shot did cause the damage the [plaintiff] could have offered more direct proof. . . ." *Id.* at 31, 194 So. 2d at 715.

[21] Maharias v. Weathers Bros. Moving & Storage, 257 N.C. 767, 127 S.E.2d 548 (1962); a slight shift in the plaintiff's emphasis may get a different result: Chicago, M.S.P. & P.R.R. v. Poarch, 292 F.2d 449 (9th Cir. 1961).

[22] Reason v. Singer Sewing Mach. Co., 259 N.C. 264, 130 S.E.2d 397 (1963).

[23] See the language of the Hicks case itself on this point, *supra* note 4

Apart from such objections to these restrictive cases, however, it may be said that where the defendant's negligence has created a risk of the harm that in fact came about, and where the negligence obscures relevant evidence about causation, all doubts ought to be resolved against the negligent defendant, just as in the case of the two hunters.

Another reason for allowing recovery in some of these cases is that the "but for" test itself does not make a great deal of sense. The "but for" test asks us to determine the "fact" of causation by asking us to speculate about what would have happened if the defendant had not been negligent. If the defendant had not splashed hot lead upon the plaintiff, would plaintiff have contracted cancer?[24] If the defendant had not neglected to provide a life guard at a swimming pool, would the plaintiff's decedent have drowned?[25] In neither case can a "factual" answer be given; we can only speculate about what might have been, and there is no way to verify our guesses. We might as well ask what an elephant would have been if it had not been an elephant. Surely this is a kind of question that is unrewarding for a practical profession.

The speculative and sometimes misleading character of the "but for" test may be quickly illustrated. Suppose defendant owns a partly rotted tree, dangerous because it is likely to fall of its own

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and accompanying text, and the similar views expressed by Judge Sobeloff in Gardner v. National Bulk Carriers, Inc., 310 F.2d 284 (4th Cir. 1962), *cert. denied*, 372 U.S. 913 (1963). Where there are two tortfeasors or combined forces causing a single harm, this reasoning, or something like it, seems well accepted. See notes 12-14 *supra*. A less radical view would not resolve all doubts against the wrongdoer, but would do so only in situations where some policy about the wrongdoer's duty would dictate. *Cf.* Malone, *Ruminations and Cause-in-Fact*, 9 STAN. L. REV. 60 (1956).

Post hoc ergo propter hoc is, of course, fallacious, if we speak in absolute terms. But in practical affairs, like law, we speak in terms of probabilities, or even a good guess about probabilities. And we prove cause-in-fact by showing facts that will allow reasonable men to guess about probabilities; certainty is not required.

[24] Kramer Service, Inc., v. Wilkins, 184 Miss. 483, 186 So. 625 (1939) (blow on the head; skin cancer at point of blow, causation not established). Smith v. Leech Brain & Co., [1962] Weekly L.R. 148 (Q.B.) (causation established).

[25] Young Men's Christian Ass'n v. Bailey, 107 Ga. App. 417, 130 S.E.2d 242 (1963) (causation established); Justice v. Prescott, 258 N.C. 781, 129 S.E.2d 479 (1963) (causation not established, *semble*). Of course, if the question is the orthodox "but for" question, the variation in facts in various cases may justify a difference in results, since circumstantial evidence will be strong enough in some cases to justify a good guess about "but for" causation and not strong enough in others. The point here, however, is that it is necessarily a *guess*.

weight upon a passerby. It does fall on a passerby, but because it was blown down by an unforeseeable wind, a wind so strong that it would have blown down even a sound tree. The defendant is negligent, and the unforeseeability of the wind will not properly affect his liability, since the result itself—injury to the passerby—was foreseeable.[26] The "but for" test, however, tempts one to say that there is no cause-in-fact; even a carefully braced tree might have blown over in the strong wind. Yet we do not know that the tree would have been braced if defendant had not been negligent; it might have been chopped down.[27] If we assume that, if defendant had not been negligent, he would have braced the tree, the injury would have occurred anyway, and the negligence in not bracing the tree is not a cause-in-fact. But we assume that defendant would have chopped the tree down had he not been negligent, then clearly his failure to do so is a cause in fact of the harm, for the harm would not have occurred if no tree was there. There seems little negligence-law policy in favor of either assumption about what might have happened without defendant's negligence.[28] Thus the "but for" test seems to take us into speculation and metaphysics.

A more ordinary case may make the same point. In a well-known case,[29] the defendant stopped his truck at a light and when the light changed made a right turn. He did not signal the turn and he ran into a boy who had pulled up between the right side of the truck and the curb, evidently because the boy was not expecting the truck to turn right. Judge Edgerton—a great judge—said that defendant's failure to give a turn signal was not a "but for" cause, since there

[26] The defendant may be held even though he does not foresee "the particular injury precisely as in fact it occurred." Boone v. North Carolina R.R., 240 N.C. 152, 81 S.E.2d 380 (1954). And one is sometimes held liable where an act of God strikes. See Harris v. Norfolk S.R.R., 173 N.C. 110, 91 S.E. 710 (1917). And see Lawrence v. Yadkin River Power Co., 190 N.C. 664, 130 S.E. 735 (1925).

[27] Dean Page Keeton of the University of Texas School of Law used this illustration for a similar point at the Torts Roundtable of the Association of American Law Schools, December 1962.

[28] It can be argued that one should assume either a minimum change of conduct that would qualify as non-negligent or any change in conduct that would eliminate causation. Such assumptions would minimize the chance that defendant's negligence is causal and would maximize his freedom of conduct. This may be thought to be more consistent with negligence law and the risk principle. But if so, we are into problems beyond practical jury solution.

[29] Waugh v. Suburban Club Ginger Ale Co., 83 D.C. App. 226, 167 F.2d 758 (1948).

was no evidence that the boy, from a position to the right of the truck, could have seen such a signal. Yet one cannot be sure that a hand signal will not catch someone's eye,[30] or the noise of a light signal will not catch an ear. To ask the plaintiff, injured in a way defendant risked, to "prove" such a matter is to ask the impossible.

Perhaps one might feel that the problems in *Hicks* should not be solved by adverting to causation doctrines at all, but that they should be solved instead by considering the defendant's duty.[31] It might be said, for example, that the defendant doctor is under a duty to use care to maximize the patient's chances of survival. If this formula is used, it is clear that defendant's negligence caused the loss of something to which the patient was entitled—maximum chances. He may or may not have "caused" the loss of the patient's life, but he certainly caused the loss of some of the chances at keeping it. At least in some areas of tort law, this approach seems to have been followed.[32]

Clearly enough, the rule stated in *Hicks* rejects the orthodox "but for" test, and substitutes in the malpractice situation a liberal approach already applied in a few other situations. The defendant is held, not only if he caused the death or injury, but also if he caused the loss of plaintiff's chance of escaping death or injury. Presumably this rule applied only when the defendant is shown to have been negligent and to have created a risk of the kind of injury that in fact did occur. The effect of *Hicks* is likely to be great, although it is difficult to be sure, since the cause problem is so often ignored. In any event the decision seems sound. It might be argued that it is inappropriate to extend a liberalization into the medical malpractice field;[33] but this seems wrong. Physicians are already highly insulated from their negligence by the rule that they are liable only when their

[30] See also Rouleau v. Blotner, 84 N.H. 539, 152 Atl. 916 (1931).

[31] See Green, *The Causal Relation Issue in Negligence Law,* 60 MICH. L. REV. 543 (1962), reprinted in GREEN, THE LITIGATION PROCESS in TORT LAW, 249 (1965).

[32] See RESTATEMENT (SECOND), TORTS § 324, and comment *g* (1965). The comment indicates that if one gratuitously rescues another from a trench filled with poisonous gas, he cannot return him to the trench, thus "worsening" the victim's position. The duty, once undertaken, is not to worsen the position, even though it is clear that defendant's acts have not "caused" any loss to the plaintiff he would not have suffered anyway. See also Gardner v. National Bulk Carriers, Inc., 310 F.2d 284 (4th Cir. 1962), *cert. denied,* 372 U.S. 913 (1963).

[33] See Malone, *Ruminations on Cause-in-Fact,* 9 STAN. L. REV. 60, 85-88 (1956).

colleagues testify against them.[34] Thus, *Hicks* seems to be an important and desirable step.

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[34] This is the rule for most cases, see PROSSER, TORTS § 32 (3d ed. 1964). In a few cases res ipsa loquitur will apply, *e.g.* Beaudoin v. Watertown Mem. Hosp., 32 Wis. 2d 132, 145 N.W.2d 166 (1966) (vaginal operation, patient woke to find blisters on her buttocks).

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