THE CANCELLATION OF OIL AND GAS LEASES: AN ADMINISTRATIVE OR JUDICIAL FUNCTION? — Richard E. Blair

CONSCIENTIOUS OBJECTOR PROVISIONS: A VIEW IN THE LIGHT OF TORCASO v. WATKINS — Francis J. Conklin, S.J.

LABOR ARBITRATION AND THE 1961-1962 SUPREME COURT — Leo Weiss

FEDERAL PRE-TRIAL PRACTICE: A STUDY OF MODIFICATION AND SANCTIONS

RELIEF FOR COLLAPSIBLE CORPORATIONS UNDER SUBSECTION (e)

VOLUME 51 NUMBER 2 WINTER 1963
ARTICLES

The Cancellation of Oil and Gas Leases: An Administrative or Judicial Function? ... 221
By Richard E. Blair

By Francis J. Conklin, S.J.

COMMENT

Labor Arbitration and the 1961-1962 Supreme Court ... 284
By Leo Weiss

NOTES

Federal Pre-Trial Practice: A Study of Modification and Sanctions ... 309

Relief for Collapsible Corporations Under Subsection (e) ... 346

DECISIONS

Corporations—Corporation Not Responsible for Criminal Conduct of Employees Who Acted With No Intent To Benefit Their Employer (Standard Oil Co. v. United States, 307 F.2d 120 (5th Cir. 1962)) ... 386


Evidence—Confession Elicited During Illegal Detention Renders Inadmissible a Reaffirmation Obtained Twenty Hours Later but Before Accused Had Confessed With Counsel (Killough v. United States, No. 16398, D.C. Cir., Oct. 4, 1962) ... 394

Privileged Communications—Attorney-Client Privilege Is Inapplicable To Corporations, Though the Work-Product Doctrine Is Unaffected by the Client's Identity (Radiant Burners, Inc. v. American Gas Ass'n, 207 F. Supp. 771, aff'd on rehearing, 209 F. Supp. 321 (N.D. Ill. 1962)) ... 399
Restraint of Trade—Robinson-Patman Act's "Meeting Competition" Defense Does Not Exclude Good Faith Price Reductions Merely Because New Customers Are Obtained Thereby (Sunshine Biscuits, Inc. v. FTC, 306 F.2d 48 (7th Cir. 1962)) 404

BOOK REVIEWS

Competition and Monopoly: Legal and Economic Issues—Mark S. Massel
Reviewed by John T. Miller 409

Professional Staffs of Congress—Kenneth Kofmehl
Reviewed by Milton Eisenberg 414

Soviet Legal Institutions: Doctrines and Social Functions—Kazimierz Grzybowski
Soviet Administrative Legality: The Role of the Attorney General's Office—Glenn G. Morgan
Reviewed by Branko M. Peselj 416

BOOKS RECEIVED 424
If in the field of LABOR LAW research you desire to achieve completeness and accuracy, with minimum effort on your part, this booklet might well have been written for you.

It describes a method of research that:

1. Reveals with amazing simplicity the authoritative value of the Decisions and Orders of the National Labor Relations Board as well as federal labor decisions and statutes.

2. Offers new, easy access to the growing number of important articles on the subject appearing in labor law journals and periodicals.

3. Increases the value of your other labor services in legal research.

SHEPARD'S CITATIONS
COLORADO SPRINGS
COLORADO

Please mention the Journal when writing to Advertisers
Try LAW WEEK for three months at 1/2 the regular rate

LAW WEEK safeguards you against missing a single point of legal importance... saves your time by greatly reducing your reading load!

WHAT YOU GET—each week

- Significant federal and state decisions—all the precedent-setting cases establishing new principles of law. Typical headings: Antitrust, Taxation, Insurance, Public Contracts, Labor, Transportation, Trade Regulation, Criminal Law, Public Utilities, Railroads.

- Immediate notice of important new federal agency rulings—among them rulings in the fields of Money and Finance, Aeronautics, Taxation, Public Contracts, Shipping, Labor.

- Supreme Court Opinions, in full text—mailed to you the same day they are handed down—plus Supreme Court Orders, Journals, Docket, Arguments.

- Summary and Analysis—a five minute review of new law, including an incisive analysis of the leading cases of the week.

For further information on the Special LAW WEEK introductory offer, write:

THE BUREAU OF NATIONAL AFFAIRS, INC.
1231 — 24th Street, N.W., Washington 7, D.C.
Challenging the Secretary of Interior's practice of administratively cancelling outstanding oil and gas leases, the author contends that authority for this power can be found in neither the wording of the pertinent statutes nor their legislative history. Pointing out that the federal courts are presently divided on this question, Commander Blair concludes by suggesting that the effective administration of the federal leasing program demands that the courts resolve this dispute by definitively reserving to themselves all power of cancellation over such leases unless it is expressly provided otherwise by statute.

INTRODUCTION

The question of whether the Secretary of the Interior has the power of administrative cancellation over outstanding oil and gas leases issued under the Mineral Leasing Act\(^1\) of 1920 has been present for some time. The existence of such power was first claimed in 1938 in a departmental opinion which asserted that the validity of an issued lease could be determined by the Secretary and cancelled if found invalid.\(^2\) This assertion represented a complete reversal of departmental policy, for from the inception of the leasing program until that time, the government had taken the position that cancellation was possible only through judicial proceedings instituted by the Attorney General.\(^3\) As a result of this

* CDR, U.S. Navy; B.A., University of Washington; LL.B., Georgetown University Law Center; LL.M., Southern Methodist University; Editor, JAG Journal, Office of the Judge Advocate General of the Navy. The opinions and conclusions expressed in this article are those of the author and do not necessarily represent the views of the Department of the Navy, the Office of the Judge Advocate General or any other governmental department or agency thereof.

change of policy, leases on untold thousands of acres of public land have been cancelled by administrative action.4

Although this assertion of power and the resulting cancellations have rarely been challenged in the courts, the dearth of litigation on the point does not indicate an absence of fundamental questions as to the statutory validity of the Secretary’s position. Rather, the power has seldom been questioned because the great majority of leases cancelled covered only minor acreage in purely wildcat territory, and the investment involved was generally so small that it would have been more costly to litigate than to accept the administrative decision. Yet, the few times that the question has come before the courts have been sufficient to create an almost irreconcilable conflict among the circuits as to the state of the law. This conflict, when considered in conjunction with the size of the leasing program5 and with the fact that discovery of oil and gas in commercial quantities involves vast expense and financial risk, makes it clear that the orderly and efficient exploitation of these minerals demands a precise delineation of jurisdiction between the executive and judicial branches when lease cancellation is involved.

In analyzing this problem it should be immediately noted that, in general, lease cancellations, whether by administrative or judicial action, may be classified into two groups, according to the reasons which give rise to the necessity for cancellation. In the first category are those leases which require cancellation because of acts or omissions of the lessee which occur subsequent to issue. Such cancellations are apparently infrequent, and, as we shall see, procedures for such action are expressly laid down in the Mineral Leasing Act. In the second category are those leases cancelled for causes arising prior to issuance, generally because of fraud on the part of the lessee or mistake by the department in issuance. The great majority of leases cancelled fall into this latter category,6 and it is in this area that the major controversy exists. The Secretary

4 By the Secretary’s own figures, 1129 leases were administratively cancelled during the three year period ending June 30, 1960. Brief for Appellee, p. 16, Boesche v. Udall, 303 F.2d 204 (D.C. Cir. 1962), cert. granted, 31 U.S.L. Week 3155 (U.S. Nov. 6, 1962) (No. 332).

5 According to Department of Interior figures, as of June 30, 1960, there were 139,000 leases, covering 113 million acres, outstanding on the public lands. The total number of leases supervised by the Department under all programs—public lands, acquired lands, Indian lands, Naval Reserves, and outer continental shelf—was 159,000, covering 125 million acres. Id. at 15-16.

6 See Brief for Appellee, Boesche v. Udall, 303 F.2d 204 (D.C. Cir. 1962), cert. granted, 31 U.S.L. Week 3155 (U.S. Nov. 6, 1962) (No. 332).
argues that he must have the power of administrative cancellation because it is necessary to correct the departmental mistakes which the size of the program makes inevitable. On the other hand, the lessees insist that the risks and investments involved in oil and gas production necessitate a degree of certainty of title which cannot be obtained unless cancellation is restricted to judicial proceedings.

Although important problems are presented by both of these categories, this study will inquire only into cancellation for reasons arising before issuance of leases. It will be further restricted to an examination of the statutory powers granted to the Secretary. Collateral matters are discussed only insofar as they relate to these statutes or to the decisions which construe them. The approach to the problem is, then, premised upon the theory that if a power of administrative cancellation exists in the Secretary, it must either be expressly granted or implied from granted power. The purpose of this inquiry is thus to discover in these statutes and cases that point at which the administrative power of cancellation of an issued lease ceases, and the judicial power begins.

THE STATUTORY PROVISIONS

Congress, in the exercise of its constitutional powers7 has exclusive and plenary power to determine the time, conditions, and modes of transferring the public lands.8 This constitutional grant also extends to the prescription of conditions upon its acquisition and management, and allows Congress to exercise the same degree of control over the public lands as does a private individual over lands owned by him.9

Prior to 1920, the disposal of public lands containing oil and gas was governed by a procedure essentially similar to that controlling its disposal for other purposes. Under the Placer Mining Law,10 which by separate statute was made applicable to oil and gas lands,11 the prospector became entitled to a patent to the fee by occupation of the land combined with certain improvements,12 or by useful occupation for a period

7 U.S. Const. art. IV, § 3.
equal to the local statute of limitations on mining claims. However, the difficulties inherent in a system which allowed the entire estate to pass from the United States, depriving it of any future income from the production of minerals, soon proved the Placer Mining Law inadequate so far as oil and gas locations were concerned. The western oil lands passed so rapidly into the hands of private owners that the Secretary of the Interior was advised in 1909 that the government would soon be obligated to repurchase the oil that it had practically given away. This fear prompted the President to withdraw from location and settlement all lands which were considered valuable for their oil and gas deposits. It was against this background that the Mineral Leasing Act was drafted and enacted.

The Mineral Leasing Act of 1920 changed the disposal system from one of complete alienation of the fee to one which passed only a mineral leasehold and reserved to the United States a specific rental and royalty payment from production, when and if obtained. The prospecting permit was retained but the procedure calling for the issuance of patents upon entry and discovery of minerals was abolished. Under the new procedure the Secretary of the Interior was delegated the power to issue permits

15 This withdrawal was made without statutory authority. The President apparently had qualms concerning the constitutionality of his act, for in 1910 he requested Congress to ratify his action and to authorize the Secretary of the Interior to make future withdrawals to meet emergencies of this type. 45 Cong. Rec. 621-22 (1910). In response Congress passed the Pickett Act, 36 Stat. 847 (1910), 43 U.S.C. §§ 41-43 (1958), which gave the President power to withdraw lands temporarily. The Secretary of the Interior was delegated the power to withdraw lands by Executive Order No. 10355, 17 Fed. Reg. 4831 (1952).
which allowed the prospector to enter designated land to explore for oil and gas. If within two years he made a discovery of paying quantity, he was entitled to a renewable lease\(^{19}\) for twenty years on a designated fraction of the land covered by the permit. Lands situated within the known geological structure of a producing field were leased on a competitive basis, in blocks not exceeding 640 acres, for the same term and with the same renewal rights.\(^{20}\)

In 1935, the practice of granting prospecting permits was also abolished and provisions made for the issuance of a noncompetitive lease of lands not known to be within the geological structure of a producing field.\(^{21}\) This lease was to be issued for a primary term of five years and continue in effect so long thereafter as oil and gas was produced in paying quantities.\(^{22}\) As the term “noncompetitive” implies, the issuance of this lease was a purely ministerial act of the Department of Interior, and the statute provided that the first qualified person making application for such lands was to be entitled to a preferential right over all others.\(^{23}\)

The duty of administering these statutes governing the public lands has been delegated to the Secretary of the Interior. By the Act of March 3, 1849,\(^{24}\) he was charged with, among other things, “the supervision of public business relating to . . . public lands, including mines.” In addition, many of the statutes governing disposal contain sections authorizing him to prescribe necessary rules and regulations and to do any and all things necessary to carry out the purpose of the acts.\(^{25}\) Under these grants, the Secretary becomes, in effect, a general manager of the federally owned lands, a “guardian of the people of the United States, over the public lands” whose oath of office requires him to see that none

\(^{19}\) Mineral Leasing Act § 14, 41 Stat. 442 (1920), 30 U.S.C. § 223 (1958). The prospector was first issued an “A” lease, covering one-fourth of the lands embraced in the lease, or 160 acres, whichever was less. He also had a preference right to a “B” lease covering three-fourths of the land included in the permit. Ibid.

\(^{20}\) These leases could be renewed for successive periods of ten years each, under such terms and conditions as the Secretary of the Interior prescribed. Mineral Leasing Act § 17, 41 Stat. 443 (1920), 30 U.S.C. § 226 (1958).


\(^{22}\) Ibid.

\(^{23}\) Ibid.


of the public domain is wasted or disposed of to a party not entitled to it. In keeping with the broad language of these statutory grants, it has long been recognized that these statutes are to be liberally construed and have the effect of granting to the Secretary a vast amount of discretionary power in administering the public lands. The Court made this clear in Williams v. United States when, in speaking of the former statute, it said:

It is obvious, it is common knowledge, that in the administration of such large and varied interests as are intrusted to the Land Department, matters not foreseen, equities not anticipated and which are therefore, not provided for by express statute, may sometimes arise, and, therefore, that the Secretary of the Interior is given that superintending and supervising power which will enable him, in the face of these unexpected contingencies, to do justice.

Thus, under the disposal systems which culminated in the patent, these broad powers enabled the Secretary of the Interior to retain administrative control over the lands until a patent had been issued. It was recognized that a permit represented an equity which was protected by the due process clause of the fifth amendment; but since due process does not require judicial process, inquiry into the extent and validity of this equitable right was within the jurisdiction of the Secretary. The formalities of notice and a hearing required by the due process clause were accommodated by the Land Department, which the Court recognized as a special tribunal, with judicial functions constituted under the supervision of the Secretary, to administer all the various proceedings followed to obtain title, from their commencement to their close. Through this tribunal exclusive control of the disposal system was retained until the consummation of title by a grant. Once this consummation was complete, however, and a patent issued, all right to control the title or to examine its validity passed from the Secretary, and fraud or mistake in its issuance could be corrected only by judicial action.

29 Smelting Co. v. Kemp, 104 U.S. 636, 640 (1881); see United States ex rel. Riverside Oil Co. v. Hitchcock, 190 U.S. 316, 324 (1903).
30 United States v. Stone, 69 U.S. (2 Wall.) 525, 535 (1864). Even after the patent issued, however, the broad power of the Secretary was often felt, for the Court made it clear that since the jurisdiction of the land department was exclusive as to determinations upon which the issuance was based, its determinations could not be collaterally attacked in an action at law. If the patent was to be set aside, a direct proceeding in equity
The administration of the Mineral Leasing Act also was expressly given to the Secretary of the Interior. As we have seen, it is he who determines to whom a lease shall issue, although since 1935 this determination, so far as a noncompetitive lease is concerned, has been limited to the qualifications of the applicants and the order in which applications were made. He was also given the power to prescribe rules and regulations and to do all things necessary to effect the purposes of the statute.31

However, in opposition to these general powers, more restrained language of those same sections specifically dealt with cancellation and forfeiture of both permits and leases. Of these sections, only section 26 provided for administrative cancellation of permits for want of diligence on the part of the permittee in prosecution of prospecting operations in accordance with the terms of the permit.32 In contrast to this, section 27, after placing an acreage limitation upon the area which one person, association, or corporation could hold under the act, directed that leases which violated this limitation be forfeited by "appropriate proceedings instituted by the Attorney General for that purpose in the United States district court for the district in which the property, or some part thereof, is located."33 Section 31, which dealt exclusively with forfeiture and cancellation, similarly provided that:

Any lease issued under the provisions of [designated sections of the act] may be forfeited and cancelled by an appropriate proceeding in the United States district court for the district in which the property, or some part thereof, is located whenever the lessee fails to comply with any of the provisions of said sections, of the lease, or of the general regulations promulgated under said sections and in force at the date of the lease.34

It will be noted that these provisions are approximately parallel to the judicially imposed limitations on the Secretary's power over the land...
patent disposal systems, in that while administrative cancellation of permits was allowed, cancellation of a lease, like a patent, was reserved to the district courts. An analogy based only on the language of the statute cannot, however, be carried too far, for sections 27 and 31 were limited to cancellation for causes arising subsequent to issuance and the provision in section 27 was concerned only with leases which violated the quantitative limitations of that section. Although this latter provision was certainly broad enough to cover cancellation for both fraud and mistake resulting in a lease of land in excess of the permitted acreage, the act is otherwise silent concerning cancellation for reasons existing prior to issuance. Thus, without more evidence of legislative intent, there might be room to question whether the act was intended to limit administrative control over leases obtained through fraud or error on the part of the administrator, for certainly Congress could not have intended such leases to be unassailable.

In answer to this question, however, the legislative history of the act indicates that Congress intended to reserve all powers of cancellation to the courts. During the debate on the Senate floor, Senator Smoot, the author of the bill which subsequently became the leasing act, remarked that there was "no doubt in the world" that the Secretary of the Interior had no authority under the bill to cancel an outstanding lease.\textsuperscript{35} Similarly in the House, Representative Sinnot, who reported the bill from committee,\textsuperscript{36} announced on the floor that a lease, unlike a permit, could be cancelled \textit{only through court action}.\textsuperscript{37} In short, the total effect of this history presents strong evidence that Congress intended to reserve all lease cancellation to judicial action.

From this examination of the original act and its history, it appears that Congress originally intended to preclude administrative cancellation of any outstanding lease. Such, at least, was the interpretation adopted by the Court in \textit{Bell Oil & Gas Co. v. Wilbur},\textsuperscript{38} the only judicial construction of the act in its original form. In that case the Secretary threatened to cancel some leases for failure of the lessee to pay fifteen cents per barrel above the posted field price, and the lessee sued to enjoin the threatened proceedings. The decree of the district court dismissing the complaint was affirmed on the ground that cancellation must be by judicial action, and that the plaintiff, by defending such an action, had

\textsuperscript{35} 58 Cong. Rec. 4168 (1919).
\textsuperscript{36} Id. at 7299.
\textsuperscript{37} Id. at 7604.
\textsuperscript{38} 60 App. D.C. 256, 50 F.2d 1070 (1931).
an adequate remedy at law. In the course of its opinion the Court of Appeals for the District of Columbia Circuit stated that under the terms of the act the Secretary had no power to cancel the leases, but must accomplish such a result by a proceeding in the district court. 39 Although the threatened cancellation in this case was for causes subsequent to issuance, there is no such limitation in the court's language. On the contrary, since the statute contained no provision for administrative cancellation, it appears that the court was of the opinion that any cancellation must be by judicial decree.

Thus, the language of the act, its legislative history and the only available judicial interpretation all support a construction which would deny any power in the Secretary to cancel a lease by his own fiat. Any argument that such administrative power of cancellation exists must, therefore, be based not on the original act but on subsequent amendments.

The first of these amendments was in 1935, when the act was extensively revised and a provision added which authorized the Secretary to cancel any lease issued after August 21, 1935, for failure to comply with the terms of the lease, provided the lands covered were not known to contain valuable deposits of oil and gas. 40 However, concerning these excepted leases, the amendment expressly provided that they could be cancelled only in the manner provided by section 31, that is, by judicial action. This is the only power to administratively cancel an outstanding lease contained in the act, and it is significant that it is a narrow one, expressly restricted by clear and unambiguous language suggesting that if the Congress which passed this amendment had believed that the framers of the original act had intended a general power of administrative cancellation to exist, it would not have so carefully limited this provision. Its primary significance, then, lies not in the fact that it extends such a power to a lease, but in the fact that this power is so narrowly restricted.

The only other change in the language dealing with cancellation and forfeiture took place in 1946, when that portion of section 27 was amended to read:

If any interest in any lease is owned or controlled, directly or indirectly, by means of stock or otherwise, in violation of any of the provisions of the act, the lease may be cancelled or the interest owned may be forfeited or the person so owning or controlling the interest may be compelled to dispose of the interest,

39 Id. at 257, 50 F.2d at 1071.
in any appropriate proceeding instituted by the attorney general. Such a proceeding shall be instituted in the United States district court . . . 41

Like the earlier amendment, nothing in this language permits administrative cancellation of a lease, nor is there anything in any of the other changes made by the 1946 revision which could be construed as an extension of administrative power in this area. In fact, the only apparent significance to be drawn from this change of language is that Congress apparently considered the provisions of section 31 broad enough to include only leases of excessive acreage to individuals and intended this section to cover the narrow area of violations in the acreage limits through corporate entities.

It would then appear that in the two amendments discussed, Congress neither recognized an existing general power of cancellation, nor intended to create one. In fact, it seems indisputable that if such power resides in the Secretary of the Interior, it must have its source outside of the original act and its amendments. Certainly, the Mineral Leasing Act nowhere expressly granted it, and as the preceding discussion of the original act has shown, it is improbable that Congress intended it to exist.

In an attempt to sidestep this construction of the statute, the Secretary contends the cancellation provisions of the act were not intended to be exclusive. He argues that the act does not require judicial proceedings but provides only an alternative remedy which may be utilized or rejected as he chooses. 42 Inherent in this argument is the concept that his administrative control over the public lands, created by the delegation of general supervisory power, is exclusive unless expressly denied. Under this view the absence of such a limitation within the provisions of the act becomes dispositive. The position is somewhat fortified by the fact that the act's language does not purport to deal with cancellation for many of the causes existing prior to issuance, for which some remedy is necessary if the legislative purposes are to be accomplished, and by the fact that there is a section placing upon the Secretary the duty to do all the things necessary to carry out the purposes of the act.

Such a construction, however, appears at variance with the intention of Congress as well as the language of the statute. As we have seen, the evidence is strong that Congress intended the administrative remedies

provided by the statute to be exclusive, and nothing in the Secretary’s argument appears powerful enough to offer convincing refutation. It must be remembered that the Mineral Leasing Act created a new disposal system, and in so doing clearly delineated those areas in which administrative action is permitted and those which require judicial proceedings, and, as we have seen, no power of administrative cancellation was originally granted. When these provisions are considered in conjunction with the legislative history, it appears unreasonable to assume that Congress could have intended to give the Secretary an unfettered choice to accept or reject the only provisions made for cancellation.

The Secretary’s construction is also contradicted by the 1935 amendment. As has been pointed out, this single grant of power to administratively cancel a lease was carefully restricted both as to the leases to which it applied and to the reasons for which cancellation was permitted. If the Secretary was given a choice by the original act between cancellation by his own procedures or judicial proceedings, this amendment becomes quite superfluous. Indeed, these restrictions are meaningful only if the original act had intended judicial proceedings as the exclusive method of cancellation.

Furthermore, the Secretary’s construction would so seriously impair the practical operation of the act that such an intent should not, in the absence of explicit language, be attributed to Congress. It is common knowledge that the exploration for oil and gas is costly and involves substantial risk. And as the court in Pan American Petroleum Co. v. Pierson correctly observed, if the continued existence of a leasehold estate is to depend upon the fluctuating policies of government departments, their value as a title basis for oil and gas development is greatly diminished, if not practically destroyed.

The Secretary further supports his argument with a claim of congressional ratification. He bases this claim upon the fact that in 1960, section 27 was extensively revised and an early version of the bill made express provision for administrative cancellation except in cases of fraud against the United States or where the land was producing or known to contain valuable deposits of oil or gas. While the bill in this form was under consideration by the House Committee on Interior and Insular Affairs,

43 The legislative history makes it clear that the primary purpose of the act was and continues to be the encouragement of the exploration and production of oil and gas. See, e.g., 58 Cong. Rec. 4168 (1919).
45 Id. at 655.
the Department of the Interior vigorously protested the reservation of any cancellation proceedings to the courts, contending that it would unduly restrict the Secretary's *existing* power to cancel by administrative action. Thus, in its comments upon the bill, it stated:

This is an important material change from the present law since the Secretary now has full authority to cancel leases, whether on producing or nonproducing acreage, where fraud is proved in their acquisition. The present prohibition on the administrative cancellation of leases where producing acreage is involved is limited to leases which have been lawfully issued.46

The committee thereafter deleted the entire provision and returned to the existing language of section 27. The bill was enacted in this form.

In relying upon this chain of events, the Secretary invokes the familiar doctrine of legislative reenactment. No attempt need be made here to explore this doctrine in detail for it is sufficient to say that, despite its seemingly conclusive application in some Supreme Court opinions,47 legislative reenactment cannot be considered an authoritative indicium of congressional adoption of an administrative interpretation.48 Even in circumstances where, as here, there is evidence that Congress had knowledge of the interpretation, the doctrine should not be applied when Congress itself has otherwise explained its return to the original language. Here this was done. The House report was careful to state that because of the pendency of suits questioning the Secretary's asserted authority, "any legislation further fixing the jurisdictional boundaries in this field between the judiciary and the executive should await the outcome of, and be based upon the experience gained through, the pending actions."49

In the light of this statement, it must be concluded that the doctrine is inapplicable here. The only legitimate conclusion that can be drawn from the history of the 1960 amendment is that it represents neither approval nor disapproval of the Secretary's construction, but was manifestly intended to preserve the *status quo* until the cancellation provisions had faced further judicial scrutiny. Such an interpretation is fortified by the fact that, in returning to the existing language, Congress deleted not only the requirement for judicial cancellation in the above-mentioned

---

cases, but also the provision which would have allowed for administrative cancellation in most other situations.

THE "LAND PATENT" ANALOGY

Even if the evidence supporting the construction which the Secretary has placed upon the Mineral Leasing Act is rejected as inconclusive, the question remains as to whether administrative cancellation of an outstanding lease can be supported by the Secretary's general powers over the public lands. However, since the only judicial examination of these powers is to be found in cases arising under the patent disposal systems, the question can only be answered by reference to these principles.

It is inevitable that the Secretary's construction of the act must be premised upon the theory that a lease conveys to the lessee no greater right than that evidenced by a prospecting permit issued under the Placer Mining Law. Since a lease does not purport to pass a fee simple, as does a patent, the argument runs, it must be analogous to a permit. And since permits have been subject to administrative cancellation for over one hundred years, Congress must not have intended to restrict the power of cancellation to judicial proceedings.\(^6^0\) This line of reasoning has apparently enjoyed favor within the Department of the Interior ever since the power to cancel an outstanding lease was first asserted, for the rationale of the first case in which the power was claimed is found in its author's declaration that:

The purported lease gave the appellant no right whatever in the land or anything therein. There is no reason why the department should not have the authority to cancel such a lease just the same as if it had been a prospecting permit.\(^5^1\)

While such an assumption is based on an historically accurate appraisal of the Secretary's power over a prospecting permit, it appears to make an unwarranted assumption that the Mineral Leasing Act equates a permit and a lease. The original act distinguished between a permit and a lease and, as we have seen, provided a method of cancellation for each. By retaining the term "permit" in the original leasing act and by providing for administrative cancellation, it is not unreasonable to assume that Congress borrowed this concept from the earlier systems. But

---


\(^5^1\) Fenelon Boesche, No. A 21230, U.S. Dep't of Interior, p. 4, Feb. 21, 1938.
the lease was an innovation and it must be assumed that the term was carefully selected to introduce a concept different from anything in the early disposal systems. Moreover, this new term was accompanied by cancellation provisions requiring judicial action. Thus it would appear that the meaning of "lease" in the leasing act is more closely analogous to the "patent" of the earlier systems than to the "permit" as previously understood.

Such an analogy can be further perfected by a comparison of the interest conveyed by a mineral lease with those created by a permit and by a patent. As stated earlier, a prospecting permit did not convey an interest in the land, but created only an equity in its holder, while a patent was a muniment of title to the fee which evidenced the passage of title from the government. Based on the interests alone, it is a reasonable assumption that if a lease can be equated with a permit, Congress might have intended to leave cancellation for those conditions not expressly covered by the act within the administrative control of the Secretary. On the other hand, if a lease conveys a legal estate in the land or the minerals therein, such an assumption becomes difficult, if not impossible, to make.

Any discussion of the interest conveyed by a lease must start with an examination of the common law existing at the passage of the leasing act; for although the lease was a new concept in the public land disposal system, by 1920 it was a well-established concept in private transactions. It must be assumed, therefore, that Congress was influenced by these concepts.

Unfortunately, the law was far from settled in 1920 and remains so today. The jurisdictions that have considered the question were then and are now, not only in conflict, but often the decisions within the states are seemingly inconsistent with a single theory. Despite the fact that precise classification is virtually impossible, and that any classification courts oversimplification, it is possible to divide the jurisdictions into two general categories.

The earliest cases dealing with the question arose in Pennsylvania soon after the discovery of oil in that state. The Pennsylvania courts first adopted what has since become the minority view, denying that a lease could transfer any property interest in the minerals in place. Such minerals were analogized to percolating waters, and held incapable of ownership until reduced to possession. Hence, the lease granted a mere license to explore which the courts called a profit a prendre.
This view, however, was rejected by a majority of the states. In Texas and states following the ownership in place theory, the lease is considered a grant of the minerals in place beneath the land.\(^5^4\) Under this view the lease effects a horizontal severance of the lessor’s estate, creating two separate and distinct estates. Since the lease runs for a primary term, and so long thereafter as oil and/or gas is produced, the estate granted is termed a determinable fee.\(^5^5\) Some other states, while refusing to accept the determinable fee concept, have adopted a more qualified theory under which the lessee receives a freehold estate in the minerals in place which they term a profit a prendre in gross.\(^5^6\) Whatever term is used to describe the interest, however, all these states agree that the lease conveys an interest in real property, rather than a license, which exists for a primary term and so long thereafter as the minerals are produced in paying quantities.

The available history of the Mineral Leasing Act indicates that Congress intended to incorporate the majority view into the statute. During the debates Mr. Anderson spoke of “interests held,”\(^5^7\) and stated that once the resources pass out of the hands of the United States under the act, they “are no longer subject to the legislative action of Congress.”\(^5^8\) These statements, when considered in conjunction with the above-quoted remarks of Senator Smoot to the effect that under the original act the Secretary of the Interior had no power to cancel an outstanding lease,\(^5^9\) though by no means dispositive, at least suggest that something more than a mere license was to pass with the issuance of the lease.

Moreover, the 1935 amendment indicates that that Congress also had construed the act in this manner. It will be recalled that the power to administratively cancel granted by the amendment was denied where the lands leased were known to contain valuable deposits of oil or gas. Such a limitation is consistent with the view that the lease conveys a vested estate in the minerals, and the denial can be read as an oblique recog-

\(^5^4\) Funk v. Haldeman, supra note 52, at 243.

\(^5^5\) E.g., Transcontinental Oil Co. v. Emerson, 298 Ill. 394, 131 N.E. 645 (1921); Mills v. Mills, 275 Ky. 431, 121 S.W.2d 962 (1938); Stephens County v. Mid-Kansas Oil & Gas Co. 113 Tex. 160, 254 S.W. 290 (1923). See Walker, Fee Simple Ownership of Oil & Gas in Texas, 6 Texas L. Rev. 125 (1928).

\(^5^6\) Corzelius v. Harrell, 143 Tex. 509, 186 S.W.2d (1945).

\(^5^7\) Callahan v. Martin, 3 Cal. 2d 110, 118, 43 P.2d 788, 794 (1935).

\(^5^8\) 58 Cong. Rec. 7604 (1919).

\(^5^9\) Id. at 7643.
nition that administrative control should not be extended to leases by virtue of which an estate in the minerals in place has vested.

Unfortunately, the Supreme Court has never passed directly upon the question, but in another context it has rejected the theory which denies the possibility of ownership of the minerals in place. In *British-American Oil Producing Co. v. Board of Equalization of Montana* the Court was faced with the question of whether the state could levy a gross production tax on oil production from trust lands held by the United States for the benefit of the Blackfeet Indians. In the course of its opinion the court stated that a reservation of minerals "operates . . . to create a distinct estate consisting of the minerals." A reservation, of course, is quite distinct from a lease, but if ownership of minerals can be reserved there is no reason why a separate estate cannot be created by lease unless it is forbidden by either the concept of a lease, the statute, or by some provision of the lease itself.

There are, however, dicta in the Court's opinions in other cases which might appear to reject the concept of a leasehold as an estate in realty. In both *Burnett v. Harmel* and *Group No. 1 Oil Corp. v. Bass* there are statements to the effect that an oil and gas lease is considered something less than a sale of land. In *Burnett*, for example, the Court said that by virtue of the lease the lessee acquired a privilege to exploit the land for oil and gas and that "such operations in respect to a mine have been said to resemble a manufacturing business carried on by the use of the soil . . . rather than a sale of the land or any interest in it or in its mineral content." Such statements are, however, weak authority, for the issue in *Group No. 1 Oil Corp*. was whether income received from production of oil and gas on Texas land, under a lease from the state, was taxable to the lessee and *Burnett* was concerned with whether bonus payments under a private oil lease were taxable as capital gains. It is, of course, elementary that in cases such as these the courts ignore local property concepts, and construe tax statutes in a uniform manner consistent with the established scheme for collection of revenue. These two cases are excellent examples of that principle in operation, for neither involved a federal issue and the lease in each case was upon Texas land, a state which, as we have seen, has adhered to the determinable fee

60 299 U.S. 159 (1936).
61 Id. at 164-65.
62 287 U.S. 103 (1932).
63 283 U.S. 279 (1931).
64 287 U.S. at 107.
theory. Furthermore, in Burnett the Court was careful to point out that it was concerned with economic consequences rather than questions of property.65

From what has been said it appears that the federal lease issued under the act was intended to convey an estate in the minerals, an estate which vests upon its execution and endures in accordance with the habendum clause for a primary term so long thereafter as oil and/or gas are produced in paying quantities. The legislative history of the statute offers evidence that Congress legislated with the concept of a vested interest in mind. Such a theory is also consistent with the cancellation provisions of the original act and is supported by the restrictions imposed upon administrative cancellation by the 1935 amendment. Furthermore, there is nothing in the federal lease itself to negate such a theory. Rather, the granting clause of this lease is substantially similar to the granting clause of the lease typically used in private transactions.66

Close analysis thus reveals that the Secretary's attempt to compare a lease with a permit is not so cogent as it first seemed. On the contrary, as this study has indicated, in enacting the present leasing procedure Congress was apparently influenced by the principles governing land patents. Certainly, the leasing act offers internal evidence to this effect, for just as prior disposal systems proceeded from permit to patent, the original leasing system moved from permit to lease. The cancellation provisions were also similar, for while administrative cancellation of permits was allowed, the only provisions dealing with cancellation of leases required judicial proceedings. Finally, the legislative history indicates that Congress intended a lease to convey an interest which, while perhaps not a

65 Id. at 111.
66 U.S. Dep't of the Interior, Offer to Lease and Lease for Oil and Gas, Form 4-1158 (Aug. 1961), provides in part:

Section 1. Rights of the Lessee—The lessee is granted the exclusive right and privilege to drill for, mine, extract, remove, and dispose of all the oil and gas deposits, . . . in the lands leased, together with the right to construct and maintain thereupon, all . . . structures necessary to the full enjoyment thereof . . .

The typical “Producers 88” form provides:

[T]he lessor . . . does grant, demise, lease and let exclusively unto the lessee, with the exclusive right of mining, exploring by geophysical and other methods and operating for and producing therefrom oil and gas of . . . [whatsoever nature or kind] . . . and laying pipe-lines, telephone and telegraph lines, and building tanks, power stations, gasoline plants, ponds, roadways, and structures thereon to produce, save, and take care of said products, and the exclusive right of injecting water, brine and other fluids into sub-surface strata, and housing and boarding employees and any and all other rights and privileges necessary . . . for the production, saving, and taking care of oil [and] gas . . .

Belsheim, Modern Legal Forms ¶ 5355.1 (1962).
fee estate in the minerals, is certainly not analogous to the mere equity represented by a permit.

The question thus becomes: What guidelines were offered by the land patent cases for determining the method of lease cancellation for reasons about which the act is silent? At the beginning of such an inquiry we are confronted with those cases which hold that the administrative power to examine and determine rights relating to the public lands does not cease until legal title has passed.\textsuperscript{67} The early case of \textit{Moore v. Robbins},\textsuperscript{68} was one of the first to set forth this principle, setting out the theory that with the issuance of a patent, legal title passes from the government, and with it all power to control the title through its agents.\textsuperscript{69} However, if the actual passage of legal title from the government was the only point at which administrative control ended, the land patent cases run contrary to the construction which this study has placed upon the Mineral Leasing Act. Indeed, unless it can be proved that the federal lease actually conveys a determinable fee in the minerals, an attempt would have to be made to show that the act limited the Secretary's existing powers in order to support a conclusion that he has no general power to cancel an outstanding lease. The land patent cases make it clear, however, that \textit{Moore v. Robbins} is by no means a complete statement of the law governing cancellation of a patent. That case, like its progeny, which also speak in terms of the passage of legal title, involved a voidable patent. While its rationale is satisfactory when applied to instruments under which legal title actually passed, it fails to explain those cases involving patents issued under circumstances which made them void \textit{ab initio}. In such a case title remains in the government; yet, for almost a century administrative cancellation of such instruments has been consistently denied.\textsuperscript{70}

These void patent cases make it clear that it was the issuance of the patent instrument rather than the actual passage of legal title which marked the cessation of administrative control. Although the rationale behind this denial has never been satisfactorily explained, the early case of \textit{United States v. Stone},\textsuperscript{71} in its consideration of the void patent problem,

\begin{itemize}
\item \textsuperscript{68} 96 U.S. 530 (1877).
\item \textsuperscript{69} Id. at 533.
\item \textsuperscript{71} Supra note 70.
\end{itemize}
established what was to become the standard explanation. The Court there reasoned that the patent was the highest evidence of title and was conclusive until set aside or annulled by some judicial tribunal. The decision was based on the unexplained theory that cancellation of the instrument was a judicial function which required the judgment of a court rather than an administrative act which could be accomplished by the land department.

Yet this explanation, however satisfactory it may be as a conclusion, fails as a rationale; for it nowhere attempts to explain why cancellation is a judicial function. And it is insufficient merely to call cancellation a judicial act, for that does not explain why the power to cancel a void lease has been continually denied to an agency which the Court has repeatedly held able to act judicially upon all rights prior to issuance.72

It is submitted that the true rationale is to be found in the fact that the Department of the Interior has full power only over the actual process of disposal of oil and gas leases, and that once this process is complete the Department’s control terminates. The courts have spoken in terms of the passage of legal title because when these cases were decided the only existing disposal process terminated in the issuance of a fee patent, which is the indicium of legal title. Administrative power ceased upon issuance because at that point the administrator had performed the last act which the disposal statute required of him.

Although this rationale has never been directly articulated by the Supreme Court, it has received oblique recognition on at least two occasions. Thus, the Court in Smelting Co. v. Kemp, in speaking of the then existing disposal system, stated: “That the provisions may properly be carried out, a land department, as part of the administrative and executive branch of the government, has been created to supervise all the various proceedings taken to obtain the title from their commencement to their close.”73 And in Michigan Land & Lumber Co. v. Rust the Court said that “generally speaking, while legal title remains in the United States, the grant is in process of administration and the land is subject to the jurisdiction of the land department. . . .”74 Under such a view the passage of legal title or the issuance of the patent instrument is significant only because it represents the culmination of the statutory

73 Supra note 72, at 640. (Emphasis added.)
74 168 U.S. 589, 592 (1887). (Emphasis added.)
procedure. When this final act is complete, the administrative process ends, and the parties must thereafter look to the courts for a remedy.

It is submitted, therefore, that a proper construction of the Mineral Leasing Act denies the Secretary of the Interior the power to cancel administratively an outstanding lease for reasons arising prior to its issuance. As we have seen, no such power is expressly granted by the statute, and both its language and history negate the implication of an administrative remedy not contained in the statute. Although the accomplishment of the act’s purposes may undoubtedly require cancellation for reasons not specified in the statute, the preceding discussion has demonstrated that the administrative cancellation of such a lease cannot be justified through reliance upon the Secretary’s general supervisory powers as those powers were applied to the earlier disposal system. In the first place, there are no convincing grounds for comparing a lease with a permit. The act itself draws a distinction between the two, and both the legislative history and the common law at the time of its enactment suggest that Congress intended for the lease to convey a legal estate in the minerals in place. Certainly, by the terms of the statute, whatever the precise nature of the interest, there is a possibility that it will endure forever. Far more important, however, is the fact that a lease represents the termination of the statutory disposal process. Beyond its execution, no further act is required to pass the leasehold interest from the government to the lessee. Thus, under the rationale of the land patent cases, administrative control would cease at this point.

It is not contended, however, that it is beyond the pale for Congress to delegate such a power to the Secretary. As earlier stated, the power of Congress over the public lands is plenary, and so long as some interest remains in the United States, Congress may decide whether the tribunal for determining the validity of estates is to be administrative or judicial. The principles of the land patent cases do, however, require that such a delegation be expressed in the disposal statute and not implied from its silence. The only such delegation in the leasing act is the provision for administrative cancellation in section 31, and, as has been noted, that provision is narrowly restricted.\footnote{75 It should be noted, however, that the most which can be said for this interpretation of the statute is that it is a reasonable one, and the Secretary has, of course, placed a different construction upon it. As we have seen, the courts have recognized that he has a generous amount of discretionary power in his administration of the public domain and the statute itself gives him the authority to do all things necessary to carry out its purposes. This raises the question of whether this construction should be subject to judicial review, or there}
Judicial Construction of the Secretary's Cancellation Power Under the Mineral Leasing Act

The preceding section of this study has, with one exception, concerned itself entirely with an independent construction of the statute without regard to the judicial decisions dealing with the question of whether the Secretary of the Interior has a general power to cancel an outstanding lease. While it is perhaps an unorthodox approach, the subject lends itself to this type of organization, for the decisions in the two circuit courts of appeal which have dealt with this question are in such irreconcilable conflict that unanimous support for either of the constructions previously considered cannot be found. Furthermore, this conflict is compounded by the fact that the District of Columbia Circuit, where three of the four cases were decided, at first, all but denied the validity of administrative cancellation, thus providing the analogy upon which the Tenth Circuit based its subsequent denial, only to reject its own creation in a later case, and construe the act to allow administrative cancellation. The cases, then, are so related that it is appropriate to consider them as a group and in the sequence in which they developed, in order to determine, not only how they have construed the act, but also the validity of their constructions.

Twenty-six years after the decision in Bell Oil & Gas Co. v. Wilbur,76 which, as earlier noted, clearly indicated that the Secretary has no power outside the statute to administratively cancel an outstanding lease, the District of Columbia Circuit decided McKay v. Wahlenmaier.77 This

should be applied the rule that where wide discretion is given and the exercise of a duty requires the administrator to interpret the act, courts will not interfere with that construction so long as it is a reasonable one. E.g., United States ex rel. Hall v. Payne, 254 U.S. 343, 347, 348 (1920); Bates & Guild Co. v. Payne, 194 U.S. 106, 108, 109 (1904); United States ex rel. Dunlap v. Black, 128 U.S. 40, 48 (1888). It is submitted, however, that such deference to the administrator must be confined to its proper sphere, and that the rule is inapplicable to the problem under discussion here. A distinction must be drawn between these questions which are directly concerned with the methods of administering the disposal, and those which impose limitations upon the scope of administrative action. In the former, discretion is an indispensable part of the administrative process, and close judicial supervision of the details of administration would impede rather than serve the congressional design. But in the latter instance it should not be assumed that Congress intended to grant the administrator discretion to expand his power beyond the limits which the statute allows him. Judicial deference in such a situation would make statutory limitations largely meaningless. See Social Security Board v. Nierotko, 327 U.S. 358, 368-69 (1946). Cf., Johnson v. Towsley, 80 U.S. (13 Wall.) 72, 84 (1871).

76 60 App. D.C. 256, 50 F.2d 1070 (1931).
case warrants detailed consideration, for it is from its language that the Secretary has since supported his asserted power to cancel.

In that case Culbertson & Irwin, Inc., its president, Culbertson, and Irwin, a vice-president, had each filed individual applications for a non-competitive lease on lands in New Mexico which had become available for leasing under the act. The three applications were identical in form, prepared in the same office of the corporation, and acknowledged before the same notary, yet none of them made reference to the others. In accordance with a regulation of the Department of the Interior, a drawing was held to determine the priority of applicants. Culbertson’s name was drawn first and Wahlenmaier’s second.

After the lease was issued to Culbertson, Wahlenmaier protested, calling the Secretary’s attention to the facts set forth above. The Secretary found that Culbertson had violated regulations which required disclosure of his interests in the leases held by the corporation, but refused to cancel the Culbertson lease. The reasoning behind this refusal was apparently that the regulation was designed to point out situations in which, if the requested lease were issued, the lessee would receive more than the maximum allowable acreage. When he determined that issuance to Culbertson would not violate this limitation, he concluded that the violation was of no consequence. Moreover, the contest was primarily between Culbertson and Wahlenmaier, and at least one departmental decision indicates that it is against departmental policy to enter into disputes between contestants when its action would not restore the lands to the public domain.

Wahlenmaier then filed suit in which he asked the court to adjudge Culbertson an unqualified applicant. He also asked that the Secretary be directed to cancel the Culbertson lease and issue one to him. This relief was granted, and the Secretary appealed. The court of appeals affirmed the judgment, holding that the Secretary was “plainly wrong in refusing to cancel the lease.”

The opinion further stated:

78 43 C.F.R. 192.43 (d), 295.8 (Supp. 1962).
79 The specific regulation, 43 C.F.R. 192.42 (c) (Supp. 1946), which Culbertson allegedly violated provided that there be filed with the application “a statement of the interests, direct and indirect, held by the applicant in oil and gas leases, and applications therefor on public lands in the same State. . . .” 43 C.F.R. 192.42 (e)3 (1954) also requires disclosure of whether or not the holding will exceed the allowable acreage under the statute; and 43 C.F.R. 192.42 (b)4 (1954), required a corporation to disclose “the names and addresses of the stockholders holding 20% . . . .”
80 See Cooper Belt Silver Mining Co., 54 Interior Dec. 475 (1934).
The Secretary’s decision was probably based on confusion as to the nature of the question before him, and a misapprehension of his own power and duty to cancel a lease obtained as this one was.82

Clearly, the statute nowhere provides for administrative cancellation of leases issued under the facts upon which this case was decided; yet the quoted language places upon the Secretary a positive duty to cancel such instruments. From this the inference is unavoidable that the court did not consider the statute to impose a limitation upon the Secretary’s power to cancel leases which were improperly issued. This is exactly the position taken by the Department of the Interior, and we find Wahlenmaier cited as authority for cancellation after cancellation under circumstances not within the narrow confines of the administrative cancellation provisions of section 31.83

Significantly, neither Wahlenmaier nor the Secretary urged the prior precedent of Bell Oil and Gas Co., and for a very good reason. Neither party was interested in attacking the Secretary’s power to cancel the lease. Wahlenmaier’s complaint included a prayer that such cancellation be ordered, and the Secretary had no interest in attacking his frequently asserted power which he had simply chosen not to assert in this case. Thus, no party was before the court who was interested in challenging the Secretary’s power of cancellation, and there is no indication in the opinion that the court dealt with the problem on any deeper basis than the issue posed to it by the parties. So analyzed, Wahlenmaier becomes weak precedent, at best.

In 1958 the issue was again presented to the District of Columbia circuit by Seaton v. The Texas Co.84 In this case the Secretary relied upon the statement in Wahlenmaier to support his cancellation of a lease which the Texas Company had received through assignment from one Dorough. Dorough had originally filed for a noncompetitive lease under the Mineral Leasing Act, but upon being told by Department of the Interior officials that the acreage in question was acquired lands, he requested that the application be treated as one for acquired land, and in due course was issued a lease under the Acquired Lands Act of 1947.85 Subsequently it was discovered that the minerals had never left the public domain, and a noncompetitive lease was issued to one Snyder.

---

82 Ibid.
The Dorough lease was cancelled without notice. The Texas Company then filed suit in the district court, resulting in a decision which ordered the Snyder lease surrendered for cancellation and restoration of the Dorough lease.

The court of appeals wrote two opinions in the case. The first enunciated principles which support the construction which this study has placed upon the act. Had this first opinion been allowed to stand, perhaps the present confusion would have been avoided. But before it was printed a rehearing was granted and the opinion withdrawn. The withdrawn opinion stated:

But we think that Dorough's lease, even if in some manner irregular had acquired a status which necessitated judicial proceedings for its outright cancellation. Among the powers conferred by Congress upon the Secretary we find none which authorized his action in this case. If it exists it must be implied, for it is nowhere expressed. And the relevant considerations weigh against implying the power. . . . It has long been held that once a patent to public land is granted by the United States it may be cancelled only by a court in original proceedings, and not merely on limited judicial review of previous administrative cancellation. . . .

The court went on to distinguish its decision in Wahlenmaier on the following grounds:

We think McKay v. Wahlenmaier . . . does not decide that administrative cancellation was available to the Secretary in the present case. There we held that the Culbertson Lease should be cancelled, and ordered the Secretary to cancel it. We did say also that the Secretary could have cancelled in the situation there presented, but the fact is the cancellation was ordered by the court as a result of a judicial proceeding. . . .

In the second opinion this strong disapproval of the Secretary's asserted powers disappeared, and the case was decided on the more restricted ground that the cancellation was not valid administrative action. The court did not, however, abandon the principles of the earlier opinion, for it was careful to refer to it and to state that if the cancellation was not permissible under the principles of the land patent cases it should be set aside. But since it was of the opinion that the department's refusal to acknowledge Dorough as the first qualified applicant for a lease under

---

86 Although the lease in question was issued under the Acquired Lands Act, the difference is not significant, since such leases are issued on the same conditions as those on public lands. 61 Stat. 914 (1947), 30 U.S.C. § 352 (1958).
88 Id. at 7.
the Mineral Leasing Act was not valid administrative action, the court did not discuss the applicability of the land patent principles. There is, then, nothing in the language of the opinion which expressly denies that the Secretary has a general power to cancel.

The total effect of the two opinions, however, does imply that no such power exists. The reference to the withdrawn opinion and to the land patent cases clearly hints that the court believed them applicable. In the first place, there is nothing in the published opinion which disapproves of the earlier statement that the principles of the patent cases preclude implying a power of administrative cancellation. On the contrary, from the dicta referred to above, the inference is unavoidable that the court confined its discussion of valid administrative action to the treatment of Dorough's application; the phrase is also descriptive of the principles set out in the first opinion. Certainly, if the Secretary acted beyond his statutory power, his action could not be considered valid administrative action, and, as we have seen, there is every reason to believe the court considered that no such power existed.

Although the Seaton case appears to be the first time a court dealing with a mineral lease used the land patent principles to limit the Secretary's power over a lease to the express grants of the statute, the concepts there expressed were developed and refined by the Tenth Circuit in the 1960 case of Pan American Petroleum Co. v. Pierson. At issue there was the power of the Secretary to cancel leases obtained by fraud upon lands known to contain valuable deposits of oil or gas, thus for the first time bringing squarely before an appellate court the question of whether the statute, either by expression or by implication, grants the power of cancellation to the Secretary. Apparently drawing heavily upon the dicta in Seaton, a unanimous court answered this question in the negative.

The court proceeded from the proposition that the Secretary of the Interior has no powers except those granted or those implied from granted powers. It then examined the pertinent sections of the statute and concluded that a power to cancel the leases under consideration was nowhere expressly granted. The question then became whether such a power can be implied, and for its answer the court turned to the principles of the land patent cases. Its language in this connection is particularly significant, for it directly supports the interpretation which this study has given to those cases:

[T]he government, by the issuance of the lease, has performed the last act required of it to vest in the lessee the right to explore for, produce, market and sell the

---

oil and gas underlying the leased premises. Similarly, the issuance of a patent is the last act of the government in disposing of the non-mineral lands of the public domain. Upon the performance of this last act, administrative power to annul or cancel ends and judicial power begins.\textsuperscript{91}

The court went on to say that any difference in the interests created by a lease and a patent was no reason to deny the power to cancel a patent while recognizing a power to cancel a lease. The important point is not the interest conveyed, but the fact that each represents the final act which the statutory disposal process authorizes.

The Secretary filed a petition for rehearing and a request for a rehearing en banc which were denied on the grounds that "the defendant officials are without authority to cancel an oil and gas lease for fraud of a lessee precedent to issuance."\textsuperscript{92} This statement raises the question of whether the court was attempting to limit the scope of its decision to leases procured through fraud. It is, however, difficult to entertain any such assumption. The decision rests firmly upon the premise that once the statutory process is exhausted, the limit of administrative action is reached. Whether this final act was caused by fraud, mistake, or other reasons, the result must remain the same. The point of the matter is that the process is complete.

This opinion is the only full judicial treatment of the limitations imposed upon the Secretary under the Mineral Leasing Act. Although its force is, perhaps, weakened by a reluctance to bring the analogy between a lease and a patent closer through a comparison based on the interest conveyed by each and through an examination of the legislative history of the act, it is submitted that it correctly evaluates the Secretary's powers over an issued lease. As the preceding section has pointed out, such comparisons only lend weight to the court's position, and their absence in the opinion should not be allowed to detract from the validity of the decision.

Thus, following the \textit{Pan American} decision, it appeared that the courts which had considered the question were unanimous in their denial of a general power to cancel an outstanding lease. Certainly the \textit{Pan American} court, which had carefully examined the statutory provisions and the principles of the patent cases, had categorically rejected the existence of such a power. The law in the District of Columbia Circuit, however, though it pointed in this direction, was not so clear. The language of \textit{Wahlenmaier} recognized such a power, but \textit{Seaton}, which was decided

\textsuperscript{91} Id. at 654-55.
\textsuperscript{92} Id. at 657.
on a different ground, strongly implied that if the question had been reached, it would have been answered in the negative. Whatever confusion existed in this circuit was, however, quickly cleared away by Boesche v. Udall.93

There the court was faced with a cancellation of a lease issued on lands which, between issuance and cancellation, had become known to contain valuable deposits of oil and gas.94 The administrative cancellation was based upon the fact that Boesche's application, by not including eighty acres which the department determined to be unavailable for leasing, did not conform with departmental regulations. As in the other cases discussed here, the act was silent as to cancellation for such a reason, but here the additional consideration that the lands contained known mineral deposits brings into sharper focus the fact that the Secretary did not rely upon any expressly granted power to support his action.

The complaint challenging this action of the Secretary was dismissed, and the court of appeals, in a per curiam opinion affirmed. A petition for rehearing en banc was granted; but following reargument, a per curiam order reinstated the judgment of the panel.95

The opinion does not discuss the dicta in Seaton, but returns directly to the language of Wahlenmaier as precedent for the Secretary's power to cancel. Clearly, then, Boesche is a complete rejection of everything implied by that dicta and an affirmation that the standard of valid administrative action is the only limitation upon the Secretary's power over an issued lease.

With all due deference to the wisdom of that court, it is submitted that its emphasis upon the undefined and perhaps undefinable standard of valid administrative action has caused it to misread the limitations imposed upon the Secretary by the statute and the principles of the land patent cases. The preceding analysis of the act and its history offers convincing evidence that Congress intended the narrow grant of administrative power to cancel an outstanding lease to be the exclusive administrative remedy. By ignoring the statutory limitations and making the vague standard of valid administrative action the only restriction upon the Secretary, the court encourages him to further extend his hand beyond the bounds of his delegated power. This tendency to reach beyond the limits of the statutory grant was recognized almost a century ago in

93 303 F.2d 204 (D.C. Cir. 1962) cert. granted, 31 U.S.L. Week 3155 (U.S. Nov. 6, 1962) (No. 332).
94 Brief for Appellant, p. 41, Boesche v. Udall, supra note 93.
95 303 F.2d at 206.
connection with the land patent cases;\textsuperscript{96} and as the \textit{Pan American} court observed, any differences which might exist between the patent and the lease do not justify confining the Secretary to his delegated powers where a patent is concerned, but releasing him from them when a lease is involved.\textsuperscript{97} The governing principles being the same, the degree of restraint should not be different.

\textbf{Conclusion}

Having examined the statute, its background, the decisions which consider the question at hand, and suggesting that except where the statute provides otherwise, cancellation of an issued lease should be left to judicial action, it remains to examine the consequences of such a position. The Secretary urges that he must have the power to cancel because the volume of erroneously issued leases is so great and court proceedings so tedious, that anything other than his own administrative processes becomes burdensome to the government.\textsuperscript{98} The short answer to this is that administrative convenience must be balanced against the practical effect of such a practice upon the operation of the statute and the detrimental effect which it would have upon the individuals who expend time and money to discover and produce the minerals leased. As has been pointed out, discovery and development of oil and gas is costly and the financial risks involved are great. These considerations urge that the lessee's rights be given more protection for his claim than he can obtain at the hands of the Secretary of the Interior. Furthermore, it does not appear that the burden which such proceedings would place upon the courts is any greater than in the land patent cases, where the denial of such power seems not to have produced an unbearable burden.

It should also be recognized that the interest of the United States in its leases after issuance is limited. There is no selection of lessees or assignees in any sense of financial or technical qualifications. Any one of millions of persons are acceptable, and the only concern of the United States is that the rentals and royalties called for by the lease be paid. Thus, in the usual situation, it makes no difference who holds a lease and discharges the obligations imposed by its terms.\textsuperscript{99} This is not to

\textsuperscript{96} Johnson v. Towsley, 80 U.S. (13 Wall.) 72, 84 (1871).


\textsuperscript{98} Brief for Appellee, p. 22, Boesche v. Udall, 303 F.2d 204 (D.C. Cir. 1962), cert. granted, 31 U.S.L. Week 3155 (U.S. Nov. 6, 1962) (No. 332).

suggest that the case will never arise in which the Secretary will wish to initiate action leading to cancellation, but it is suggested that in the overwhelming majority of cases he can leave the contest to private litigation between the leaseholder and other aggrieved parties who believe their rights to particular leasehold acreage to be superior to those of the lessee.

In cases such as these the patent cases again suggest a solution. Johnson v. Towsley\(^ {100} \) was a case in which private parties contested the right to land after a patent had been granted to one of the parties. Trial was had on the merits and the court decided that a trust should be impressed upon the patent in favor of the party whose rights to the land were determined to be superior. The action of the United States in passing title to the land was not disturbed. The court looked beyond the mechanics of passing title and undertook only to lodge the title passed by the government's action in the party properly entitled to it.

The desirability of this approach in resolving the contentions which arise in the analogous situations surrounding the issuance of leases can be demonstrated in a few hypothetical cases. First is the case when a lease is erroneously issued and later finds its way into the hands of a bona fide purchaser. In such a situation the approach mentioned above is admittedly applicable and should result in the success of the bona fide purchaser in a contest of rights to the lease.\(^ {101} \) More difficult would be the case where the lease is erroneously issued to a party having an inferior right to the lease who takes the lease and expends great sums and is rewarded with the discovery of a valuable oil pool. If the party who had the superior right to the lease at the time of its issuance now challenges the right of the discoverer of oil, is he to prevail and profit from the expense and labor of the party to whom the lease was erro-

---

\(^ {100} \) 80 U.S. (13 Wall.) 72 (1871).

\(^ {101} \) The Act of Sept. 21, 1959, 73 Stat. 571, 30 U.S.C. § 184 (Supp. II, 1959-1960) gave some relief to the bona fide purchaser. This law provides that any party to a proceeding shall be promptly dismissed upon a showing that he was a bona fide purchaser when he acquired the interest which is being disputed. There is, however, one situation which deserves comment. If a company or individual engages the services of a broker to procure leases and the broker violates the law, the Secretary might well take the position that an agency relationship existed, thus placing the leaseholder beyond the provisions of the amendment.
neously issued on a mere showing that his right to the lease was originally superior? Although such a result would seem patently unjust and not in consonance with the desirable approach seen in Johnson v. Towsley,\(^2\) the rationale of the Boesche and Wahlenmaier cases, if followed to its logical conclusion, would permit such a result.

Further hypothesizing, let us posit the case in which there is but one applicant, so that any contest will be between the United States and the leaseholder. If such lease was erroneously issued, the government might initially have had the power to cancel it, but should the right to exercise this power be extended when the leaseholder has incurred great expense and been successful in his search for oil? Perhaps the power should be allowed, but in any event, the proper forum for testing the superiority of rights under the erroneously issued lease is manifestly a court which can objectively balance the equities involved and enter an appropriate decree. The desire of the Secretary to erase the embarrassment of the initially erroneous issuance is quite likely to bring the administrative machinery too close to the equities involved to strike an objective balance. Thus, the Towsley approach of looking directly to the rights of the parties would seem to effect the more equitable result.

The problem would seem likely to admit of two categories: 1) A minority of cases where, usually as a matter of principle, the Secretary may wish to seek cancellation of an issued lease, which he believes voidable, in accordance with his claim of statutory authority, or those where he may wish to effect cancellation of wholly void instruments in order to remove clouds from the title to land which he is charged with leasing. 2) A majority of cases involving disputes over issued leases, which can be left to litigation between leaseholders and aggrieved parties, including unsuccessful applicants.

In cases of the first type, cancellation procedures will usually not be necessary, as the Secretary's suggestion of voidness most often results in the lessee allowing his challenged lease to lapse for non-payment of rental, or else will surrender it. In cases of the second type the courts, through applications of principles of equity, can do substantial justice among the parties. Generally, such cases will involve a conflict of issued leases, one of which is for some reason void, with one of the litigants desiring to remove the cloud of the void instrument from the valid leasehold title. In these situations, the contest involves no property interest of the United States, for government title to the underlying fee is not challenged nor in any way put in issue. Only the leasehold

\(^2\) 80 U.S. (13 Wall.) 72 (1871).
interest of private parties is involved. Since the United States is not a party, there is no reason why the state courts could not have concurrent jurisdiction with the federal courts in the determination of the individual rights concerned. Such a utilization of both federal and state courts would serve to preclude the flood of litigation upon federal courts which the Secretary prophesies as attendant upon the denial of his power of administrative cancellation.

In summary, it will be recalled that this study has shown that nothing in the Mineral Leasing Act or in the general powers of the Secretary of the Interior over the public lands can be construed as a grant of power to administratively cancel an outstanding oil or gas lease for reasons existing prior to issuance. On the contrary, although the Mineral Leasing Act is largely silent on the method by which such cancellations are to be effected, the language of the cancellation provisions, the legislative history, and the tenor of the act as a whole present convincing evidence that Congress intended such actions to be reserved to judicial proceedings. An examination of these factors in light of the better reasoned decisions dealing with the question points to the conclusion that Congress intended the principles found in the land patent cases to control such questions. And, as we have seen, these principles will justify an assertion of the power of administrative cancellation only by an express grant, not by implication from silence.

Despite the arguments which the Secretary has advanced against such a proposition, it is nevertheless demonstrable that neither the practical operation of the leasing program, nor the orderly administration of justice will be impaired by such a limitation upon the department. Rather, the evidence is strong that the reservation of such power of cancellation to the courts, with its resultant increase in the certainty of title to leasehold estates, will encourage rather than impede the development of these mineral resources. It has also been pointed out that the threat of clogged court dockets and administrative chaos envisioned by the Secretary is far more apparent than real. Such gloomy forecasts are not to be allowed to so fill the foreground of the problem as to obscure the harm to the federal leasing program which results from administrative cancellation.

Finally, the determination of an individual’s right to an interest in land has traditionally been a power and function of the courts. Unless it can be shown that Congress has deemed it necessary to allow the Secretary of the Interior to share this function, this power should remain with the courts alone; and, as this study has attempted to show, analysis of relevant statutes reveals no such congressional intent.
CONSCIENTIOUS OBJECTOR PROVISIONS: A VIEW IN THE LIGHT OF TORCASO v. WATKINS

FRANCIS J. CONKLIN, S.J.*

Reviewing and evaluating the legislative and constitutional background of the conscientious objector exemptions, the author suggests that recent Supreme Court decisions not only create grave doubts as to the constitutionality of the present exemption provisions, but have placed obstructions in the path of future congressional attempts to devise a workable exemption provision. Father Conklin feels that the Supreme Court has removed the vital flexibility of the first amendment and urges that the objector provisions be reexamined, discounting this untoward rigidity.

INTRODUCTION

The Congress and the American people have historically been deeply concerned with protecting the free exercise of religion and respecting the scruples of those who for religious reasons claim they cannot conscientiously bear arms. Mirroring this attitude, any legislation based upon this recognition has almost exclusively limited relief to those whose claim is based upon a duty to a higher being, rather than a personal or political philosophy. In attempting to obtain a workable formula which will protect the religious liberty of the sincere conscientious objector, the major concern of Congress has been to enact a law liberal enough to achieve this objective, but strict enough to discourage the coward and the shirker.

There have been many formally distinguishable variations of this formula, but with few exceptions they have had as their basis the adjective, or some form of the adjective, “religious.” An examination of the historical materials relevant to this word, as it has been used in the various state and federal militia, draft, and selective service acts, clearly demonstrates that it was historically used in reference to a belief in a Supreme Being. With these historical precedents in mind it does not seem unusual that the Congress adopted the phrase “belief in a Supreme Being” in the conscientious objector provisions of the 1948 Selective Service Act. In this act the long-sought workable formula seemed to have been achieved.

However, what appeared to be the final solution has been returned to the realm of doubt by the recent Supreme Court decision in Torcaso v. Watkins. The sweeping language utilized in Torcaso all but explicitly

* LL.B., Georgetown University Law Center; LL.M., Yale University; Professor of Law, Gonzaga University.
rules the "belief in a Supreme Being" clause of the 1948 Selective Service Act\(^3\) unconstitutional. Moreover, it casts considerable doubt upon the constitutionality of the ministerial exemption provision in that same statute.\(^4\)

In that case the Supreme Court held that a provision in the Maryland Constitution which required a declaration of belief in the existence of God in order to qualify for the office of notary public, invaded Torcaso's freedom of belief and religion. The basis for this decision was expressed by the Court as follows:

We repeat and again reaffirm that neither a State nor the Federal Government can constitutionally force a person "to profess a belief or disbelief in religion." Neither can constitutionally pass laws nor impose requirements which aid all religions as against non-believers, and neither can aid those religions based on a belief in the existence of God as against those religions founded on different beliefs.\(^6\)

In effect, the Supreme Court has ruled that any governmental attempt to define the word "religion," as that word was used in the first amendment, will be unconstitutional if the definition excludes any philosophical, sociological, political or humanitarian belief which even the smallest

---


\(^4\) 62 Stat. 611 (1948), 50 U.S.C. App. § 456(g) (1958). An examination of the Selective Service Acts of 1940 and 1948, and the case law which has developed under them, reveals that the ministerial exemption provision does "aid all religions as against non-believers" contrary to the law as set forth in Torcaso. The present ministerial exemption reads:

Regular or duly ordained ministers of religion . . . and students preparing for the ministry under the direction of recognized churches or religious organizations, who are satisfactorily pursuing full-time courses of instruction in recognized theological or divinity schools, or who are satisfactorily pursuing full-time courses of instruction leading to their entrance into recognized theological or divinity schools in which they have been preenrolled, shall be exempt from training and service . . . .


The Senate bill provided for the exemption from training and service of regular or duly ordained ministers of religion and of theological and pretheological students. The House amendment broadened this exemption to include Christian Science readers and practitioners and those persons who have been recognized by the officials of their church, synagogue, or sect as having given definite and acknowledged intention of entering into full-time religious work.

The conference agreement adopts the provisions of the Senate bill with respect to exemption of ministers and theological and pretheological students, for the reason that it felt that to include any specific sect or religion by name in this provision would logically compel the inclusion of many others or, by interpretation, indicate that other such sects would be excluded were the original House provisions accepted.


\(^5\) 367 U.S. at 495.
minority chooses to call a "religious" belief. As the brief for appellant, Torcaso, clearly demonstrated, in reaching its decision the Court had to repudiate the definitions of religion given in a whole series of previously decided cases. However, the Court's opinion, as is usually the case, contains no further indication of the revolutionary interpretation it had determined to give the word "religion" in the context of the first amendment.

The immediate purpose of this study is to briefly review the historical materials relevant to the word "religious" as used in the "religious scruples" provisions of the various state and federal military acts. It is submitted that these materials clearly demonstrate that the word "religious" has historically been used in reference to a belief in a Supreme Being. The ramifications of the Torcaso decision will then be examined in the light of these materials and its effect upon them discussed in detail.

As a prelude to this examination it is first necessary to take brief note of the two united yet contradictory theses which form the poles of the American dialectic. The first of these is contained in the simple formulation of Thomas Jefferson in the Declaration of Independence which expresses clearly and unequivocally the fundamental philosophy of government of the Founding Fathers themselves and the American people whom they represented. Prescinding quite legitimately from the various meta-

7 E.g., United States v. Macintosh, 283 U.S. 605 (1931); Church of the Holy Trinity v. United States, 143 U.S. 457 (1892); Davis v. Beason, 133 U.S. 333 (1890).
8 When in the course of human events, it becomes necessary for one people to dissolve the political bands which have connected them with another, and to assume among the powers of the earth, the separate and equal station to which the Laws of Nature and of Nature's God entitle them, a decent respect to the opinions of mankind requires that they should declare the causes which impel them to the separation. We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of Happiness.

The Life and Selected Writings of Thomas Jefferson 22 (Koch & Peden ed. 1944). Jefferson later expressed the role which the author had played in framing the Declaration:

Neither aiming at originality of principles or sentiments nor yet copied from any particular and previous writing, it was intended to be an expression of the American mind . . . . All its authority rests on the harmonizing sentiments of the day.

The Life and Selected Writings of Thomas Jefferson, op. cit. supra at 719. In the reply brief for the appellant in Torcaso, the first point made is that the Declaration of Independence, since it contains such phrases as "Creator," "Supreme Judge" and "Divine Providence" is totally irrelevant to any legal discussion of the problems of church and state in the United States, even though the Declaration has been cited in connection with this problem in such cases as Church of the Holy Trinity v. United States, 143 U.S. 457, 467-68 (1892).
physical connotations of the ambiguous words "natural rights" and "natural law," the consensus among the Founding Fathers was: Man is a creature of a higher being, called God. The political state is a creature of man. Thus, the rights of man—the inalienable, natural rights of man—make the dignity of the individual sacred and inviolable in the presence of the collective. For this reason, religion, or the duty one owes his Creator, is beyond the competence of merely human jurisdiction.

Throughout the course of this discussion we shall have frequent occasion to discuss and study this right of the individual and its clash, or apparent clash, with the second of these poles, the right of the collective. It should be made clear at the outset that in reality the clash is between the duty of the individual, i.e., the duty which he conceives himself to owe to a higher being, and the duty of the collective to preserve itself in existence by resort to armed conflict.

In attempting to resolve the clash between these interests, we must start with the premise that any truly democratic form of government must be grounded upon a philosophy of government which at least recognizes the dignity and unique character of the individual. Consequently, Rousseau's superficial characterization of democracy as a system of government which idolizes the will of the majority must be replaced with a clearer insight. This insight has been supplied, at least partially, in the concept of political pluralism.

It is important to note that this concept of political pluralism, as applied to religion, differs greatly from the concept of religious toleration. For to tolerate divergent religious beliefs suggests that the privileges enjoyed by minority groups are merely revocable concessions of an authoritarian and all-competent political state, while religious pluralism posits these as an inherent part of the democratic form of government.

Once it is recognized that the underlying philosophy of democratic government in the United States is essentially pluralistic in religious affairs, rather than one of toleration, the problem of making this concept an effective reality is brought into focus. In other words, rather than concerning ourselves with the "will of the majority," our serious attention must be brought to bear upon the rights of the minority. A true majority can always foster and protect itself in a democratic society; by the same token, unchecked majority rule can easily breed a tyranny over minority rights.

The clauses prohibiting an "establishment of religion" and guaranteeing the "free exercise" of religion in the first amendment to the Constitution represent a fundamental attempt to protect the religious rights
of minority groups in the United States. On the other hand, if political pluralism and minority rights are pushed to their logical extreme, the end result will be anarchy and the total disintegration of the collective. As a consequence the American genius has hit upon a conscious program of pragmatic inconsistency which pervades every aspect of life under the Constitution. From the very outset this government has attempted to embody two abstract political concepts—liberty and union—which are intrinsically self-contradictory. The American genius has pressed neither principle to its logical conclusion, but has always striven for a practical synthesis, often clumsy, perhaps inconsistent, but usually workable. Thus, we have sought union by the formation of a progressively stronger central government, yet have tried to preserve liberty by restricting this government internally through a complicated series of institutionalized checks and balances.

In the field of religious liberty the courts have striven to foster the ideal of minority rights and individual dignity embodied in the first amendment. At the same time they have sought to check the anarchical tendency inherent in the free exercise of any endeavor by emphasizing the rights of the collective to restrict religious practices. In short, politics is the art of the possible; and it is not practically possible to preserve peace and domestic tranquility and, at the same time, to permit human sacrifice, polygamy, or fraud and deceit in the name of free exercise of religion.

In this sense the famous remark of Justice Holmes that "the life of the law has been not logic: it has been experience,"9 finds historical validation in the problem of the conscientious objector. Our governing bodies since the Continental Congress and the legislatures of the newly emergent states have been acutely conscious of the principles of religious liberty and free exercise of religion in the enactment of military draft statutes. However, it is equally apparent that they have been just as conscious of the problem of distributive justice: that all citizens should bear proportionately the burden of personal risk and financial sacrifice which the collective must unwillingly parcel out to its constituents in time of war.

**HISTORICAL BACKGROUND**

*The Continental Congress and Early State Enactments*

On July 18, 1775, the First Continental Congress resolved to protect the rights of those who because of their "religious principles" could not

---

bear arms.10 This simple resolution, passed almost a full year before the Declaration of Independence, bears testimony to the depth of their conviction on the subject of man's higher duty to his Creator. Certainly the military needs, in the most elemental sense of the word, of the newly forming collective were never greater than they were during that summer of 1775. Yet, in fulfilling those needs the Congress did not fail to underscore its role as a political collective—a thing created by men—which had no power to interfere with the one relation which gave true dignity to the individual, his relationship to his Creator.

It must be recognized, however, that when the conscientious objector resolution was enacted in 1775, the Continental Congress enjoyed hardly more than advisory powers over the affairs of the disjointed colonies. Consequently, to understand the actual state of the law during the Revolution and in the post-revolutionary period, the early state enactments are of far greater importance than the resolves of the Continental Congress.

Besides the enactments of the Continental Congress, the constitutions of Vermont,11 New York,12 and Pennsylvania13 during the early revolutionary period granted the conscientious objector who was religiously opposed to bearing arms an exemption from military service. Similarly, a Rhode Island act specifically exempted Christians who conscientiously objected to war. However, it also provided that these objectors must register and that they must do work of a charitable or merely civil nature when the exigencies of the situation so demanded.14

Statutes in New Hampshire, Georgia, Maryland, Massachusetts, North Carolina, South Carolina, and Virginia also provided exemptions from military service, as an act of grace for Quakers and other religious conscientious objectors.15 As in the case of the Rhode Island statutes, however, this exemption was almost universally coupled with a condition that the conscientious objector either supply the military forces with a substitute or else provide funds to hire a substitute.16 In each of these

10 2 Journals of the Continental Congress 189 (1905).
12 5 Thorpe, op. cit. supra note 11, at 2637.
13 Id. at 3083.
16 For example, in Massachusetts the Militia Act of June 15, 1758 provided that the
statutes a universal reference to religious duties and duties of conscience in the exemption provisions of the military draft acts shows how the philosophy expressed in the Declaration of Independence was applied in the case of conscientious objection.

The Adoption of the First Amendment

The fragmentary record of the 1789 debates about what would eventually become the first amendment must, of necessity, leave much to conjecture. Nevertheless, we do know that several attempts were made to amend the Constitution to include a provision that no religiously scrupulous person should be compelled to bear arms.17 Some wished to limit this exclusion to persons belonging to a religious sect,18 but it was argued that this would eliminate many Quakers who were willing to fight even though the majority of their sect taught that it was wrong to shed blood.19 Others wanted to insert a provision which would require the objector to pay an equivalent.20 However, this was criticized because the principles of the religiously scrupulous also were opposed to the securing of a substitute or the paying of an equivalent.

Eventually, after long deliberation and conflict between the Senate and House and among the members of the two bodies themselves, the Amendments were adopted without specific reference to the problem of the conscientious objector.21

public treasury must pay for a substitute for each Quaker drafted, but the public purse was subsequently to be reimbursed by a special levy upon Quakers in the next tax act. 2 Background of Selective Service, op. cit. supra note 14, at 210-12.

18 Id. at 750.
19 Id. at 750-51.
20 Id. at 750.
21 The proposed Federal Draft Act of 1814, which never actually became law, was severely criticized as "unconstitutional and in derogation of the rights positively reserved to the several States." 28 Annals of Congress 100 (1815) [1789-1824]. Despite this opposition, the bill passed the Senate. However, the version which passed the Senate more than likely did not contain a conscientious objector provision. Id. at 109. On the other hand the House debates on the bill were partially concerned with an amendment primarily concerned with the protection of those consciously scrupulous of bearing arms because of membership in a "religious sect or denomination of Christians." Id. at 774. This amendment to the Senate bill was passed by the House by an overwhelming majority. Id. at 775.

The fact that an overwhelming majority approved the amendment would seem to imply that this group of legislators, so close in time to the Founding Fathers, were of the opinion that the rights of the conscientious objector had not been incorporated into the condensed language of the first amendment's "free exercise of religion" clause. However, another motive may have influenced some votes. The proposing speech by Joseph Lewis of Virginia,
The Civil War

At the outbreak of the hostilities between the North and the South there was no national draft act in force in the United States. Consequently, the men drafted to fill the ranks of the Union and Confederate Armies came through the circuitous and cumbersome route of the state militia acts. In many states, conscientious objectors were protected by the constitutional provisions; in the other states, bounty systems and fines protected the rights of conscience. Although it is manifestly impossible to trace the statutory provisions in force in the states within the reasonable confines of this discussion, the many state provisions indicate that the problem was, at least, given some formal consideration by a majority of the states.

The debates leading up to the enactment of the first federal draft act in 1863 are illustrative of just about all the possible attitudes towards the problem of conscientious objection. The first provision which came up for consideration sought exemption for those who did not wish to bear arms because of scruples of conscience, and who were excused therefrom by the constitution of any state. This was eventually withdrawn because of considerable opposition. Some felt it too narrow; others objected because the provision did not include payment of an equivalent; and a few feared possible problems in the area of states rights.

The next proposal was phrased in slightly different language. It referred to persons belonging to any religious sect whose faith or creed prohibited bearing arms. But this provision met difficulty in the disagreement over the exemption afforded clergymen and was subsequently defeated. Another proposal involving petition to a federal court, and relief upon proof of sincerity, also met defeat, and the first draft act

Id. at 774, and his subsequent vote against the bill, id. at 929, indicate that the provision may have been a device employed by opponents of the entire bill similar to the "no racial discrimination" amendments tacked on to impede the enactment of modern legislation. Eventually, the bill came to an ignoble death by being set aside for the next Congress.

22 Among the Northern States, the constitutions of Indiana, 2 Thorpe, op. cit. supra note 11, at 1089; Iowa, id. at 1132; Illinois, id. at 1004; Kansas, id. at 1190; and Pennsylvania, 5 Thorpe, op. cit. supra note 11, at 3111, contained general provisions protecting conscientious objectors; whereas only Texas, 6 Thorpe, op. cit. supra note 11, at 3559; and Alabama, 1 Thorpe, op. cit. supra note 11, at 105, had formal constitutional provisions of this type among the Confederates.


24 Ibid.

25 Ibid.

26 Id. at 1389-90.
became law without any provision directly exempting conscientious objectors.27

Under this act the conscientious objector had available only the provision for substitution or exemption upon payment of $300.28 Public reaction against the $300 commutation clause brought about many attempts to change it in the next Congress, and again the problem of the conscientious objector arose. Problems quickly followed in the discussions concerning those who were not only opposed to the bearing of arms but also opposed to paying any fine or commutation in lieu thereof.29 A prolonged discussion took place between the patriotic and the practical,30 and eventually the conscientious objector provision was enacted, providing for noncombatant duty upon sufficient proof of the objector's religious conscientious scruples.31

World War I

As a prelude to America's participation in World War I, Congress passed the National Defense Act of 191632 which under the term "Unorganized Militia" included both religious ministers and conscientious objectors. Relating to conscientious objectors, the act provided an exemption, subject to regulation by the President, for those professing that their objection was based on a "religious belief," but only if it was satisfactorily proved that the claim was conscientious. However, those allowed an exemption were still required to serve in "noncombatant" capacities.33

One year later Congress passed the Draft Act of 191734 which exempted only those conscientious objectors who were affiliated with historic peace churches.35 The fact that this exemption was granted solely on religious grounds was made clear by the fact that an amendment was proposed to exempt "all persons who have a conscientious objection to the undertaking of combatant services in the present war."36 The amendment which would presumably have exempted the political ob-

30 Ibid.
34 Act of May 18, 1917, ch. 15, 40 Stat. 76.
35 Act of May 18, 1917, ch. 15, § 4, 40 Stat. 78.
36 55 Cong. Rec. 1362 (1917).
jectors as well as those opposed to the bearing of arms because of religious scruples was subsequently defeated. Consequently, the 1917 act provided that no person could be compelled to serve in a combatant capacity who was a “member of any well-recognized sect or organization . . . whose existing creed or principles forbid its members to participate in war in any form . . . .”37 The act also provided that those exempted could be compelled to serve in capacities designated by the President to be “non-combatant.”38

This 1917 act constituted congressional recognition of only a few very well known religious sects and required that the objector profess not only a belief in God, but also that he adhere to one of the historic peace churches in order to qualify for recognition as a conscientious objector. For this reason the act was subjected to vigorous challenge.39 However, because of the difficulty of administering the 1917 act, the President subsequently issued a regulation defining noncombatant military services to which conscientious objectors could be assigned, which was worded broadly enough to include all those who had personal scruples against military duty, although not members of the historic peace churches.40

The enactment of the Draft Act of 1917 presented a fundamental constitutional problem: Does Congress have the power to compel an individual to serve in the national military forces? This question had been affirmatively answered in lower court decisions in connection with the Civil War Draft Act,41 but was bound to arise again under the 1917 act due to its limited exemption.

From what has been said about the establishment of religion, the restrictions which the 1917 act placed upon the free exercise of religion are rather clear. Under the 1917 act equal protection of the free exercise of religion was entirely lacking. Only those who were members of the historic peace churches could exercise their religious beliefs without incurring the disability of military court martial or civil imprisonment. Unquestionably, the “adherence to a sect” requirement of the draft act was included by Congress as a test of sincerity, but this did not negate the fact that the absence of a more liberal provision constituted a severe restriction of the free exercise of religion. Nevertheless, when this question was first presented to the Supreme Court in the Selective Draft

---

37 Act of May 18, 1917, ch. 15, § 4, 40 Stat. 78.
38 Ibid.
39 55 Cong. Rec. 1004 (1917).
40 Exec. Order No. 2823, March 20, 1918.
41 E.g., McCall’s Case, 15 Fed. Cas. 1225 (No. 8669) (E.D. Pa. 1863).
Law Cases, the Court concisely answered the constitutional objections by adopting the view that the power to wage war is the power to wage war successfully.

In Kramer v. United States, another case arising under the 1917 act, the Supreme Court also made clear the religious basis of that act's exemptions. There, appellant's objection to participation in the selective service process stemmed from conscientious objections to participation in any form. The motive for Kramer's objections was not what is commonly understood to be a religious motive but a philosophical, social or humanitarian belief. In the earlier decision of Davis v. Beason Justice Field had stated that "the term religion had reference to one's views of his relations to his Creator, and to obligations they impose." Since no one had seriously challenged this general understanding of the word it should cause little wonder that in 1917 Kramer's conscientious objections were not regarded as based on religious grounds. Indeed, Kramer was not refusing to cooperate with the federal authorities because of the duty he owed to a higher being. Consequently, it seemed safe to assume that the "free exercise of religion" clause was not directly before the Court. Kramer did not argue that he was denied the right to freely exercise his religion, nor that his religion was deprived of the equal protection of the laws, because of the exemption favoring the historic peace churches.

42 245 U.S. 366 (1918).
43 245 U.S. 478 (1918).
44 133 U.S. 333, 343 (1889).
45 Brief for Appellant, Kramer v. United States, 245 U.S. 478 (1918). In another closely related case, however, it was argued before the Supreme Court that since the Draft Act exempts conscientious objectors who are members of a "well-recognized religious sect" it "establishes a religion or prohibits the free exercise thereof and is a new combination of Church and State." Brief for Appellant, p. 33, Goldman v. United States, 245 U.S. 474 (1918). The argument continued:

You may have two persons of exactly the same religious conviction of opposition to participating in war in any form. They may believe firmly "Thou shalt not kill." . . . [B]oth derive their convictions from the same source, their conscience; but one of them belongs to a certain particular sect and the other does not. The one who belongs to the well-recognized religious sect is exempted from the duty of engaging in the combatant service of the war if those are its principles, and the other for his honest convictions, because he refused to serve, is made a felon and subjected to severe penalties. If this is not making a law "respecting an establishment of religion" and "prohibiting the free exercise thereof" . . . no such law can be devised.

Id. at 39.

The government replied that the Selective Draft Law neither establishes a religion nor prohibits its free exercise, because "the law recognizes the right of every citizen to choose religious affiliations without restriction, [and] it goes so far as to aid in the free exercise of those religions which forbid participation in war." Brief for Appellee, pp. 82-83, Goldman
Thus, the Supreme Court had little difficulty in affirming his conviction of conspiracy to violate the 1917 act.

**IS REFUSAL TO BEAR ARMS A CONSTITUTIONAL RIGHT?**

The first major question emanating from the subject of conscientious objection is whether or not the free exercise clause of the first amendment embraces the right to refuse to bear arms in the defense of the nation. The strongest argument in favor of conscientious objection as a constitutional right is that economy of language rather than a desire to exclude conscientious objection motivated the terse phraseology of the first amendment. From the forgotten ninth amendment—"The enumeration in the Constitution of certain rights, shall not be construed to deny or disparage others retained by the people"—a corollary argument may be made that although the conscientious objector provision was dropped from what is now the second amendment, this constitutional right was intended to be included in the general phraseology of the ninth amendment. But the latter amendment has been limited so far to the right to participate in partisan political activity.\(^4^6\)

The plain fact of the matter is that the historical materials prove as much for one side as for the other. The omission of the conscientious objector provision in the 1863 Draft Law, its inclusion in the 1814 proposals\(^4^7\) and the 1864 law really do not touch the constitutional issue. The provisions for military substitutes under those acts can be used to argue that Congress acknowledged the right but exacted a reasonable price for its exercise. Clearly, the government has always been thought to have the right to place reasonable restrictions upon the free exercise of the individual civil liberties.\(^4^8\) On the other hand, the fact that Congress moved

---


\(^{47}\) See supra note 21.

\(^{48}\) See Gitlow v. New York, 268 U.S. 652 (1925); Mormon Church v. United States, 136
into the field of conscientious objection as early as 1814 indicates that
the generation closest to the founding fathers did not feel that the first
amendment secured the rights of conscientious objectors.

The United States circuit courts of appeal, however, appear to be
unanimous in holding that there is no constitutional right to refuse
to bear arms in defense of the United States.49 These opinions,
more often dicta, reinforce each other by a process of interstitial refer-
ces to the other circuits. Yet, all seem to be traceable to the words
of the Supreme Court in two cases, United States v. Macintosh60 and
Hamilton v. Regents of the Univ. of Cal.61

In Macintosh the Supreme Court was faced with the question whether
Congress had included within the naturalization statute62 the requirement
of an oath to bear arms as a condition of naturalization. Macintosh, a
Canadian by birth, was a professor of theology at Yale University and
a former chaplain in the Canadian Expeditionary Force during World
War I. He applied for American citizenship in 1929. In response to the
query whether he was willing to take up arms in defense of this country
he wrote: "Yes; but I should want to be free to judge of the necessity."63
Later Macintosh submitted a memorandum stating that:

I am willing to do what I judge to be in the best interests of my country, but
only in so far as I can believe that this is not going to be against the interests
of humanity in the long run. I do not undertake to support "my country, right
or wrong" in any dispute which may arise, and I am not willing to promise
beforehand, and without knowing the cause for which my country may go to
war, either that I will or that I will not "take up arms in defense of this country,"
however "necessary" the war may seem to be to the Government of the day.64

The district court sustained the denial of citizenship by the Immigra-
tion Office. The circuit court of appeals reversed, finding that Mac-
intosh's views amounted to conscientious religious scruples, the latter
being an unalienable right of conscience which the citizen need not sur-
render and which the government or society cannot take away.65 Thus,

49 E.g., United States v. Kime, 188 F.2d 677 (7th Cir.), cert. denied, 338 U.S. 947 (1950);
Baxley v. United States, 134 F.2d 937 (4th Cir. 1943).
50 283 U.S. 605 (1931).
51 293 U.S. 245 (1934).
53 283 U.S. at 617-18.
54 Id. at 618.
55 Macintosh v. United States, 42 F.2d 845 (2d Cir. 1930), rev'd, 283 U.S. 605 (1931).
the court found that Macintosh's objections were religious objections in the historic sense of the word "religion" as defined in Davis v. Beason and Church of the Holy Trinity v. United States, i.e., as implying duties to a higher being.

After granting certiorari, the Supreme Court was faced with Macintosh's contention that the free exercise clause of the first amendment forbids Congress from interfering with the rights of conscience, and that his objection was a right of conscience. Macintosh's argument attempted to balance the rights of the individual vis-à-vis the collective:

Government by the majority acting through Congress is limited in its powers. It cannot override the conscientious religious scruples of a citizen by forcing him to bear arms in a war. The fifty-one percent majority rule cannot dictate to a citizen what action would be justified by the will of God. The two domains are separate. The collapse of a republican form of government with a substitution of anarchy is not a probable consequence of the refusal of a citizen to bear arms in a war against his conscientious religious scruples.

In other words, Macintosh felt that the oath requirement was an unreasonable and unconstitutional restraint upon his individual liberty, i.e., his right to the free exercise of religion.

The Supreme Court, in reversing the ruling of the court of appeals, apparently did not think highly of petitioner's contentions. Regarding the constitutional right to refuse to bear arms because of religious scruples the Court said:

This, if it means what it seems to say, is an astonishing statement. Of course, there is no such principle of the Constitution, fixed or otherwise. The conscientious objector is relieved from the obligation to bear arms in obedience to no constitutional provision, express or implied; but because, and only because, it has accorded with the policy of Congress thus to relieve him. The alien, when he becomes a naturalized citizen, acquires, with one exception, every right possessed under the Constitution by those citizens who are native born . . . . The privilege of the native-born conscientious objector to avoid bearing arms comes not from the Constitution but from the acts of Congress. That body may grant or withhold the exemption as in its wisdom it sees fit; and if it be withheld, the native-born conscientious objector cannot successfully assert the privilege. No other conclusion is compatible with the well-nigh limitless extent of the war powers as above illustrated, which include, by necessary implication, the power, in the last extremity, to compel the armed service of any citizen in

56 133 U.S. 333 (1890). Mr. Justice Field there stated that: "The term 'religion' has reference to one's views of his relations to his Creator, and to the obligations they impose of reverence for his being and character, and of obedience to his will." Id. at 342.
57 143 U.S. 457, 470-71 (1892).
Thus, the Court held that the native American has no constitutional right to refuse to bear arms because of religious scruples and that Congress can impose such qualifications and restrictions in this area as it feels are necessary.

However, the majority in the Supreme Court could not absolutely deny the validity of Macintosh's position. Obviously, no person who believes he owes a higher duty to a Supreme Being than he does to a political state can in conscience swear that he will shed blood in an unjust war, whether his denominational affiliation be Catholic, Protestant, Jewish, or Mohammedan. Consequently, the Court, rather ungracefully, tried to hedge, stating: "From its very nature, the war power, when necessity calls for its exercise, tolerates no qualifications of limitations, unless found in the Constitution or in applicable principles of international law." But, having struck down the "astonishing statement" that the federal constitution protects the rights of the religious dissenter, the Court presumably left it up to "applicable principles of international law" to protect the religiously scrupulous person, with the utility of the latter remedy being highly questionable, to say the least.

The cogent dissent of Mr. Chief Justice Hughes in Macintosh did not

---

59 283 U.S. at 623-24. Previously, in United States v. Schwimmer, 279 U.S. 644 (1929), the Supreme Court had rejected an application for naturalization because the petitioner's uncompromising views on the subject of pacifism cast doubt on her attachment to the principles of the Constitution. However, the majority opinion in Schwimmer does not really touch upon the conscientious objector problem. Mr. Justice Butler succeeded in shifting the emphasis upon petitioner's pacifist opinions to her former behavior and staunchly defended his position because he feared that petitioner's open advocacy of "peace at any price" would have a deleterious effect upon young men who were discontent or cowardly when confronted with the pressures of a national draft act and the perils of a shooting war.

60 The American Friends Service Committee's amicus curiae brief in Macintosh had taken pains to point out the dangers of totalitarianism and deification of the political state underlying any hasty approach to this delicate subject.

61 283 U.S. at 622.

62 Although the Supreme Court has, on occasion, turned to the customary principles of international law to determine what the applicable law might be in the absence of a congressional determination of policy, e.g., The Paquete Habana, 175 U.S. 677 (1900), no one has yet had the temerity to argue before the Court that the amorphous principles of international law limit the powers of Congress in the same way that the higher laws of judicial review and the Constitution restrain the Congress.

63 283 U.S. 605, 627 (1931). This opinion was concurred in by Justices Holmes, Brandeis, and Stone.
have to reach the constitutional question because it refused to read into the Naturalization Act any unconditional promise to bear arms. However, there was no hesitation to underscore the basic problem posited in the majority opinion:

Much has been said of the paramount duty to the State, a duty to be recognized, it is urged, even though it conflicts with convictions of duty to God. Undoubtedly that duty to the State exists within the domain of power, for government may enforce obedience to laws regardless of scruples. When one's belief collides with the power of the State, the latter is supreme within its sphere and submission or punishment follows. But in the forum of conscience, duty to a moral power higher than the State has always been maintained. The reservation of that supreme obligation, as a matter of principle, would unquestionably be made by many of our conscientious and law-abiding citizens. The essence of religion is belief in a relation to God involving duties superior to those rising from any human relation. As was stated by Mr. Justice Field, in Davis v. Beason, 133 U.S. 333, 342: "The term 'religion' has reference to one's view of his relations to his Creator, and to the obligations they impose of reverence for his being and character, and of obedience to his will." One cannot speak of religious liberty with proper appreciation of its essential and historic significance, without assuming the existence of a belief in supreme allegiance to the will of God . . . . There is abundant room for enforcing the requisite authority of law as it is enacted and requires obedience, and for maintaining the government, without demanding that either citizens or applicants for citizenship shall assume by oath an obligation to regard allegiance to God as subordinate to allegiance to civil power.64

Thus, despite their different statutory interpretations, it is clear that both the majority and minority used the term "conscientious objector" only in respect to "religious" convictions as Chief Justice Hughes defined that term, namely, that "the essence of religion is belief in a relation to God involving duties superior to those arising from any human relationship."65

During the October term 1934 the conscientious objector problem came before the Court once again. In Hamilton v. Regents of The Univ. of Cal.66 the petitioners questioned the constitutionality of an order of the University Board of Regents which effectively precluded them from attending the school. The order in question required all male students

---

64 Id. at 633-34. Some fourteen years later, in Girouard v. United States, 328 U.S. 61 (1945), the Supreme Court overruled the Macintosh holding as well as United States v. Bland, 283 U.S. 636 (1931), and United States v. Schwimmer, 279 U.S. 644 (1929), and ruled that the Naturalization Act does not require an oath to bear arms as a condition of naturalization. However, it is implicit in the Girouard opinion that Congress does have the power to make military service a condition of naturalization.

65 283 U.S. at 633.

66 293 U.S. 245 (1934).
attending the university to take a course in military science and tactics and allegedly interfered with the free exercise of pacifist religious beliefs. The appellants, members of the Methodist Episcopal Church, attacked the order on the grounds that it imposed compulsory military training upon religious and conscientious objectors, thus depriving them of religious liberty without due process of law, and that it violated the free exercise of religion clause of the first amendment. In response to these contentions, the Court reasoned that the appellants were not being forced to attend the state university and consequently their religious liberty was not being impaired. The Court then trailed off on the question of the duty of the citizen to support and defend the state as well as the federal government, and concluded by quoting with approval the lengthy excerpt from Macintosh, holding that the privilege of the native-born conscientious objector to avoid bearing arms comes not from the Constitution but from acts of Congress.

The concurring opinion of Justice Cardozo, with whom Justice Stone and Justice Brandeis joined, gives a better analysis of the case. Justice Cardozo noted that the requirement of the Board of Regents may be unwise, but that does not render it unconstitutional. Moreover, a review of our history since early colonial times underscores the fact that all of these exemptions were coupled with "collateral conditions." This seems to be a clear expression that there are no absolutes in the freedoms guaranteed, and that religious practices inimical to public order can be suppressed. As Justice Cardozo stated:

Manifestly a different doctrine would carry us to lengths that have never yet been dreamed of. The conscientious objector, if his liberties were to be thus extended, might refuse to contribute taxes in furtherance of any other end condemned by his conscience as irreligious or immoral. The right of private judgment has never yet been so exalted above the powers and the compulsion of the agencies of government. One who is a martyr to a principle—which may turn out in the end to be a delusion or an error—does not prove by his martyrdom that he has kept within the law.

---

67 Id. at 250.
68 Id. at 248.
69 Id. at 262.
70 Id. at 264.
71 Id. at 266.
72 Id. at 266-68.
73 Id. at 268. Prior to the above-mentioned statutory construction of the Naturalization Act by Girouard v. United States, 328 U.S. 61 (1945), another aspect of conscientious objection came before the Supreme Court in In re Summers, 325 U.S. 561 (1944). The Supreme Court of Illinois had refused to admit Summers to practice following the recommendation of
In summary, it seems safe to conclude that the principle enunciated in Macintosh, i.e., that refusal to bear arms is not a constitutional right, is still good law, although the Court has never really been squarely faced with the issue of the religiously motivated conscientious objector forced to bear arms in defense of his nation. However, under the new definition of religion adopted in Torcaso v. Watkins74 the Court will almost inevitably have to re-evaluate the free exercise problem with regard to conscientious objection, since the rights of the “non-believer” have not been safeguarded by the congressional exemption.

Evolution and Constitutionality of the Supreme Being Clause

World War II

In 1940, Congress, faced with the problem of incorporating a conscientious objector provision in the Selective Service Act of 1940, once again limited the exemption to members of well-recognized religious sects and also required that the creed of the sect must forbid its members to participate in war in any form.75 Both the Senate and the House of Representatives held hearings on this bill and the representatives of many religious denominations, as well as those from other interested organizations, came forward to denounce the narrow statutory language.76 During the hearings before the Senate Committee Dr. Howard Beale of the American Civil Liberties Union urged that the bill be amended so as to include “conscientious objectors on non-religious grounds who, by established membership in organizations like the Fellowship of Reconciliation, can establish the sincerity of their objections.”77 In reiterating this

its character and fitness committee, because Summers refused to swear to support and defend the constitution of Illinois by arms. Summers had been classified as a conscientious objector and it was precisely because of his religious scruples that he was unable to take the unqualified oath required by the Illinois Supreme Court. In sustaining the decision of the Illinois court, the Supreme Court relied upon the authority of the Macintosh and Hamilton cases, apparently confirming the view that the refusal to bear arms was not protected by the free exercise clause of the first amendment. The dissenting opinion of Mr. Justice Black, concurred in by Justices Murphy, Douglas and Rutledge, implied that the free exercise clause of the first amendment may be flexible enough to embrace the religious scruples of the conscientious objector. Id. at 573-78.

76 Hearings on S. 4164 Before the Senate Committee on Military Affairs, 76th Cong., 3d Sess. (1940); Hearings on H.R. 10132 Before the House Committee on Military Affairs, 76th Cong., 3d Sess. (1940).
77 Hearings on S. 4164, supra note 76, at 308.
view before a House committee, Dr. Beale proposed that the bill be amended to read: "Nothing contained in this act shall be construed to require any person to be subject to training . . . who is conscientiously opposed to participation in war in any form."78 Although this request was rejected by Congress, the pressure exerted by the various religious groups did result in the broadening of the original proposal to read: "Nothing contained in this act shall be construed to require any person to be subject to combatant training who, by reason of religious training and belief, is conscientiously opposed to participating in war in any form. . . ."79

In determining the qualifications of the person seeking the exemption under the 1940 act, a searching inquiry into the extremely subjective domain of personal sincerity was required, as it is today.80 However, our primary concern here is with the "objective" aspect of this inquiry. That is, before determining whether the young man claiming exemption qualifies as a conscientious objector a preliminary inquiry must be made into his "religious training and beliefs." The history of the past draft acts and the legislative history of the 1940 act indicate quite clearly that the qualification of "religious training and belief" is employed in the traditional sense of the term "religion," i.e., requiring a belief in a Supreme Being.81 Conscientious scruples by reason of religious training and belief had reference to a duty to a higher being. Congress did not then intend to exempt those who were conscientiously opposed to war for "non-religious" motives. In other words, the amendment proposed by the American Civil Liberties Union was considered and rejected.

However, in 1943, in United States v. Kauten,82 Judge Augustus Hand undertook to effectuate the policy desired by the American Civil Liberties

78 Hearings on H.R. 10132, supra note 76, at 191. (Emphasis added.)
79 Selective Training and Service Act of 1940, ch. 720, § 5(g), 54 Stat. 889. Perhaps the most significant gain which the conscientious objectors made under the 1940 act was the provision which allowed them to do work of national importance under civilian direction in lieu of induction into the military forces and subsequent furlough to civilian tasks. This provision was enacted to protect them from the menace of military court martial proceedings and to alleviate the conscientious scruples which association with the military forces occasioned for many during World War I. See Note, 6 Hastings L.J. 233 (1955).
81 See Russell, Development of Conscientious Objector Recognition in the United States, 20 Geo. Wash. L. Rev. 409, 426-28 (1952); Waite, Section 5(g) of the Selective Service Act, As Amended by the Court, 29 Minn. L. Rev. 22, 30-31 (1944).
82 133 F.2d 703 (2d Cir. 1943).
Union by redefining the term "religion" in the Selective Service Act of 1940. The defendant, Kauten, was an atheist who had evidenced an intense dislike of President Franklin Roosevelt and particularly of Roosevelt's foreign policy. In fact, Kauten regarded the war as a scheme devised by Roosevelt to solve the unemployment problem in this country, and felt that we should meekly submit to external aggression. Quite obviously these political views were never within the scope of the exemption intended by the Congress. However, Judge Hand went out of his way to interpret the statute so as to encompass the position proposed by the American Civil Liberties Union, despite what seems to be the clear legislative history of the act indicating that Congress had rejected that view.83 Judge Hand stated that:

The provisions of the present statute . . . take into account the characteristics of a skeptical generation and make the existence of a conscientious scruple against war in any form, rather than allegiance to a definite religious group or creed, the basis of exemption. We are not convinced by anything in the record that the registrant did not report for induction because of a compelling voice of conscience which we should regard as a religious impulse . . .

There is a distinction between a course of reasoning resulting in a conviction that a particular war is inexpedient or disastrous and a conscientious objection to participation in any war under any circumstances. The latter, and not the former, may be the basis of exemption under the Act. The former is usually a political objection, while the latter, we think, may justly be regarded as a response of the individual to an inward mentor, call it conscience or God, that is for many persons at the present time the equivalent of what has always been thought a religious impulse.84

This redefinition was pure dictum, entirely unnecessary for the disposition of the case,85 for Judge Hand was intent only upon pointing out that

83 See Waite, Section 5(g) of the Selective Service Act, As Amended by the Court, 29 Minn. L. Rev. 22 (1944); Note, 38 Ill. L. Rev. 332 (1944).
84 133 F.2d at 709.
85 See Waite, supra note 83, at 24-25. Quite clearly, Judge Hand favored the broad exemption of conscientious objectors espoused by the American Civil Liberties Union. But since this broad exemption had been clearly rejected by Congress his attempt to reconstruct the statute raises the traditional question: What right does the individual judge have to flaunt the will of the Congress (and presumably of the people) and interpret the law in a manner consonant with his personal preferences? The seriousness of this problem may be more evident from consideration of the Phryic victory which the American Civil Liberties Union wins in a decision of this type. Although the ACLU would logically be compelled to applaud the "justice" of the dictum in Kauten, the same uninhibited judicial power which allows the personal feelings of the judge to triumph over a clear decision of the majority in the legislature not only can, but historically has been a formidable instrument of political tyranny. And whatever short range gains the ACLU may establish by this departure from
even if we gave the word "religion" the broadest interpretation possible it could not be stretched to include the objections of the defendant. 86

Subsequently, however, in United States ex rel. Phillips v. Downer, 87 this same court of appeals used this dictum as the basis for its decision. The court, faced with a fact pattern that came within the dictum in Kauten, found that vague "opposition to all wars" on philosophical and humanitarian grounds characterizes a belief as "religious" rather than "political" within the meaning of the dictum in Kauten. 88 In justification of its shotgun marriage of religious, philosophical and humanitarian beliefs into the broad concept of religion, the court employed what appears to be a fallacious identification of "religion" and denominational affiliation, saying:

But if a stricter rule than was announced in the Kauten case is called for, one demanding a belief which cannot be found among the philosophers but only among religious teachers of recognized organizations, then we are substantially, or nearly back to the requirement of the Act of 1917 of membership in a well-recognized religious sect or organization whose existing creed or principles forbid its members to participate in war in any form. 89

Contrary to this reasoning, it seems both reasonable and logical to assume that had Congress intended to saddle the term "religious" in the 1940 act with a new meaning, not in accord with that which had been traditionally understood, it would have so indicated. Yet, as noted, we find no such indication in the act or its legislative history. Thus, the Second Circuit overlooked the congressional intent, perhaps purposely, and substituted its own opinion of what the exemption provision in the 1940 act should encompass, in light of the seemingly unworkable provision in the 1917 act.

When the "religious training" problem arose in the Ninth Circuit in the "government of law, not of men" concept may be quickly and easily wiped out by the simple process of changing the personnel on the Court.

86 Although it is extremely dangerous to speculate on the motives prompting Justice Hand's decision, he may have been motivated by the realization that, however logical and traditional this statutory language may seem to be, the Court must cope with the infinite variability of individual cases. Suppose, for example, a young man has received a certain amount of religious training in a fundamental sect. Then he goes to college and with the additional sophistication of a little learning he can no longer accept the teachings of his former religion. However, although his atheism consists in a negation of the logical inconsistencies in his early religious training, enough of that early training has remained for the command "thou shalt not kill," to make good sense.

87 135 F.2d 521 (2d Cir. 1943).
88 Id. at 524.
89 Ibid.
Berman v. United States,90 the court of appeals considered the dictum of Kauten and, in a lengthy opinion, rejected it. The Berman court reasoned that:

It is our opinion that the expression "by reason of religious training and belief" is plain language, and was written into the statute for the specific purpose of distinguishing between a conscientious social belief, or a sincere devotion to a high moralistic philosophy, and one based upon an individual's belief in his responsibility to an authority higher and beyond any worldly one . . . . There are those who have a philosophy of life, and who live up to it. There is evidence that this is so in regard to appellant. However, no matter how pure and admirable his standard may be, and no matter how devotedly he adheres to it, his philosophy and morals and social policy without the concept of deity cannot be said to be religion.91

Berman petitioned the Supreme Court for certiorari. In support of this petition the American Civil Liberties Union filed an amicus curiae brief arguing that the adoption of the narrow and traditional meaning of the word "religion" would exclude all those who do not acknowledge the existence of a deity. "Under this reasoning great sections of humanity would be classified as irreligious, including humanists, Buddhists, Hindus, members of Ethical Culture Societies and others attached to no formal religious organization."92 It was further contended that the court of appeals misinterpreted the congressional intent because Congress had taken into account the "fact" that in the present skeptical generation the compelling voice of conscience, whether or not it be identified with the word "God" is generally regarded as a religious impulse.93

The brief for petitioner raised the problem of the first amendment, but only by indirection. Berman argued that the lower court's decision was a "religious test" which seeks to establish orthodoxy in religious belief and therefore is a clear violation of the first amendment.94

The petition attacked the "naive anthropomorphism in religion based upon a two-story universe theory" expressed in Mr. Justice Hughes' dis-

90 156 F.2d 377 (9th Cir.), cert. denied, 329 U.S. 795 (1946).
91 Id. at 380-81.
92 Brief for the American Civil Liberties Union as Amicus Curiae, p. 12, Berman v. United States, 156 F.2d 377 (9th Cir.), cert. denied, 329 U.S. 795 (1946).
93 Ibid. This argument amounted to a paraphrasing of the reasoning of Judge Hand in Kauten.
94 Brief for Petitioner, p. 16, Berman v. United States, 329 U.S. 795 (1946). The same argument was presented in a different form when petitioner later insisted that the Circuit Court assumed the prerogative of individual conscience itself and claimed the right to legislate concerning the requirements of Berman's personal religion, and prescribed the doctrinal beliefs he must maintain in order to avoid criminal prosecution. Id. at 18.
sent in *Macintosh* and in reply to the circuit court's contention that it would be quite ridiculous to contend that the authors of the first amendment intended to include "morals or devotion to human welfare or the policy of government" within the protection afforded by that amendment, the petition stated:

"[I]t is even more "ridiculous" to imply that such concerns are beyond the pale of religion and cannot be animated by a religious impulse. It seems clear that the intent of the First Amendment was to render it forever impossible for the Congress of the United States to enact a law which would attempt to define the "true" religion, thereby working hardship on or discrimination against those who have the misfortune to dissent or believe otherwise."

However, the Supreme Court denied certiorari, leaving it up to Congress to resolve the difficulty.

**Selective Service Act of 1948**

The conflict left by the decisions in *Kauten* and *Berman* was resolved by the Congress in emphatic terms in the Selective Service Act of 1948 in which the exemption was once again based upon "religious training and belief." Congress made the scope of these terms quite clear with the explanation that:

Religious training and belief in this connection mean an individual's belief in relation to a Supreme Being involving duties superior to those arising from any human relation, but does not include essentially political, sociological or philosophical views or a merely personal moral code.

To remove any doubt about the intent of Congress, the Senate specifically

---

95 Id. at 23.
96 156 F.2d at 380-81.
97 Brief for Petitioner, p. 23, Berman v. United States, 156 F.2d 377 (9th Cir.), cert. denied, 329 U.S. 795 (1946).
98 329 U.S. 795 (1946). The conflict between the Berman and Kauten decisions was before the Supreme Court by indirection in Sicurella v. United States, 348 U.S. 385 (1955). In this case the Department of Justice had ruled that a Jehovah's Witness must be denied classification as a conscientious objector because a Witness is willing to engage in "theocratic war" and hence is not opposed to participation "in war in any form." The Court very sanely held that Congress had in mind "real shooting wars" when it referred to participation in war in any form and that the "theocratic warfare" concept of the Jehovah's Witnesses did not prevent their being included within the conscientious objector provisions of the Selective Service Act. See Taffs v. United States, 208 F.2d 329 (8th Cir. 1953), cert. denied, 347 U.S. 928 (1954).
101 Ibid.
cited Berman with approval. Therefore, with the explicit clarification in the 1948 act, the statutory construction arguments raised in Berman had to be abandoned, and the constitutional arguments which appeared by indirection in the Berman petition required elucidation.

In George v. United States the Ninth Circuit was presented with the question of whether the exemption in the 1948 act was a prohibition of the free exercise of religion, or a law in respect to the establishment of a religion. However, George believed in God and consequently did not really have standing to question the constitutionality of the "Supreme Being Clause." Yet, the court went into detail in discussing and affirming the constitutionality of the section, upholding the power of Congress to grant such an exemption as it sees fit, even though the defendant's rights were not affected by the statute as it applied to him. The court declared:

So it is evident that the definition which the Congress introduced into the 1948 Amendment comports with the spirit in which "Religion" is understood generally, and the manner in which it has been defined by the courts. It is couched in terms of the relationship of the individual to a Supreme Being, and comports with the standard as accepted understanding of the meaning of "Religion" in American society.

Political, sociological, philosophical, and ethical grounds for opposing war are so distinct from opposition induced by religious training and belief that the Congress could very well recognize the latter as a ground for exemption and refuse to sanction the former. Even if we were not dealing with the plenary power to provide for the defense of the country, such classification would meet all the accepted tests of due process.

Subsequently, in Clark v. United States, the constitutional issue was squarely before the Ninth Circuit. In that case the defendant was denied the conscientious objector exemption specifically because he did not rest his objections upon a belief in God. The court cited the George case as controlling on the constitutional issues presented in relation to

103 196 F.2d 445 (9th Cir.), cert. denied, 334 U.S. 843 (1952).
104 Id. at 452.
105 Id. at 451.
106 Id. at 451-52. In United States v. De Lime, 233 F.2d 96 (3d Cir. 1955), it was held that the administrative process of appeal was not open to the defendant because he did not come within the exception granted by the statutory language. The court found that the defendant's own uncontradicted statement that he was an agnostic demonstrated that his claim was not based on "religious training and belief."
107 236 F.2d 13 (9th Cir.), cert. denied, 352 U.S. 882 (1956).
the first amendment,\textsuperscript{108} and rejected as "specious reasoning" the argument that the clause in question violates the "no religious test" provision of article VI of the Constitution.\textsuperscript{109} Clark petitioned for certiorari, arguing that the exemption discriminates against religions that do not profess a belief in a Supreme Being and against registrants whose religion is not one expressed in orthodox terms.\textsuperscript{110} In listing the reasons why the Supreme Court should grant certiorari, the petitioner contended that an important constitutional question was involved in the case, namely, whether the "Supreme Being Clause" offends article VI and/or the first amendment. However, although faced squarely with the constitutional issue, the Supreme Court refused to grant certiorari.\textsuperscript{111}

**Effect of Torcaso**

It is now evident that the line of reasoning followed by Judge Hand in *Kauten* has been adopted by the Supreme Court as the current interpretation of the meaning of the word "religion" in the first amendment. In *Torcaso v. Watkins*\textsuperscript{112} the Supreme Court, in holding that the Maryland religious test for public office which required a declaration of belief in the existence of God was an unconstitutional invasion of appellant's freedom of belief and religion, all but explicitly declared that the "Supreme Being Clause" of the Selective Service Act is now unconstitutional. The opinion of the Court, authored by Mr. Justice Black, clearly demonstrates that the "Supreme Being Clause" is repugnant to the first amendment since it aids "all religions as against non-believers," and aids some "religions based on a belief in the existence of God as against those religions founded on different beliefs."\textsuperscript{113}

\textsuperscript{108} Id. at 24.

\textsuperscript{109} Id. at 23.

\textsuperscript{110} Brief for Petitioner, p. 4, Clark v. United States, 352 U.S. 882 (1956).

\textsuperscript{111} 352 U.S. 882 (1956).

\textsuperscript{112} 367 U.S. 488 (1961).

\textsuperscript{113} Id. at 495. The course of decisions which led the Supreme Court to the affirmative position it took in *Torcaso* began with the dictum in *Everson v. Board of Educ.*, 330 U.S. 1 (1947). The Court said:

The "establishment of religion" clause of the first amendment means at least this: Neither a state nor the Federal Government can set up a church. Neither can pass laws which aid one religion, aid all religions, or prefer one religion over another.

Id. at 15.

This dictum changed the meaning of the establishment clause of the first amendment from the meaning that clause had been given by a number of celebrated authorities. See, e.g., Cooley, *Principles of Constitutional Law* 974-76 (8th ed. 1927); Story, *Commentaries on the Constitution of the United States* § 454 (5th ed. 1891). When this
Since any attempt by a court to define or interpret the word "religion" in the first amendment must, of necessity, imply the exclusion of some opinions which a small minority may choose to call religion, the plain implication in this opinion is that any such attempt is automatically unconstitutional. Because the term "religion" may not be so defined as to exclude "non-believers" it must, of necessity, include everyone regardless of their belief or non-belief. Therefore, any attempted legislative employment of the word "religion" would be fruitless since its meaning could never be usefully defined, either by Congress or by the courts. Any definition would have to include all who "believe," even if that be a "non-belief."

An examination of appellant's brief in Torcaso, as well as the amici curiae briefs for the American Ethical Union and the American Jewish Committee, reveals an argument which has repeatedly been advanced in these cases, and which apparently influenced the Court in Torcaso, namely, that the word "religion" in the federal constitution must not be defined in such a manner as to exclude the millions of adherents of the oriental religions, such as Hinduism, Buddhism, and Taoism. If this argument was, in fact, found persuasive by the Court, the simple fact is that the Court was misled. The proponents of the above argument have confused the issue by equating all these beliefs with atheism. While it is true that the ambiguous word "atheist" has been used in religious controversies rather freely to characterize dissident points of view, the root meaning, and strict or traditional meaning of the word, refers to a person who literally denies the existence of a Supreme Being. No serious scholar of religious beliefs and practices has ever gone so far as to identify the Eastern religions with atheism, as that term is understood in western culture.

While it is true that religions such as Buddhism and Taoism do not teach a belief in a God in the same sense that is generally understood in

dictum was challenged in oral argument before the Court in Illinois ex rel. McCollum v. Board of Educ., 333 U.S. 203 (1948), Mr. Justice Black refused to allow the dictum to be questioned. The repetition of the dictum in McCollum and its elevation into constitutional principle in Torcaso have followed the traditional process of dictum being repeated until its familiar ring creates precedent and then a vague stare decisis is invoked to bridge the gap between repeated dictum and decision.


115 The Court cited this argument in its opinion. 367 U.S. at 495 n.11.

the Western cultural tradition, they most emphatically do not negate the existence of a supreme power above and beyond the human. Consequently, the narrow and historically traditional definition of "religion" which we found in Mr. Justice Hughes' dissent in *Macintosh*,¹¹⁷ a definition which was concurred in by the great liberals on the Court of that era, would exclude only the very small segment of society who are atheists and/or agnostics. The Maryland Court of Appeals in *Torcaso* stated quite clearly that "the historical record makes it clear that religious toleration ... was never thought to encompass the ungodly."¹¹⁸ Although this statement is not literally accurate, the historical evidence which has been presented so far, and which could be multiplied almost *ad infinitum*, clearly demonstrates that atheism has been *tolerated* rather than positively fostered in this country. And, as has already been pointed out, toleration is quite distinct from political recognition of full equality. As a direct consequence of the Court's decision in *Torcaso*, atheism and atheistic societies are now not only tolerated, but also given constitutional rights hitherto reserved to "religion," in the historical sense of the word. Such a validation of the atheist's claim to equal recognition and equal protection under the establishment and free exercise clauses clearly marks a significant shift in the emphasis of constitutional law.¹¹⁹

The new interpretation of the first amendment in *Torcaso* firmly establishes one of the basic tenets of the "religion" of secular humanism as the only admissible interpretation of the first amendment. This dogma is the absolute neutrality of the government, both state and national, in all matters touching upon "religion." However, the incorporation of this belief into the constitutional principles of the first amendment has seemingly created problems which admit of no solution and which for that reason had been wisely avoided by the courts in the past.

¹¹⁷ See pp. 266-67 *supra*.


¹¹⁹ An interesting argument used to bolster this grant of equal religious rights to the atheist was made by appellant in *Torcaso*. "Once the door is opened to an official orthodoxy, even if it is only that of a belief in God, the way is cleared for heresy trials." Brief for Appellant, p. 9, *Torcaso v. Watkins*, 367 U.S. 488 (1961). This somewhat dogmatic assertion seems to contain an old logical fallacy termed *ignorantio elenchii*. This country has survived for some decades without heresy trials, and during this period of history the traditional interpretation of the word "religion" has been repeatedly reaffirmed. Is there any clear and present danger of heresy trials in contemporary America? In other words, was it really necessary to enunciate a new principle of constitutional law in order to forestall the hypothetical possibility of heresy trials?
Arguments Against the Apparent Implication in *Torcaso*

There are a number of arguments which may be advanced in an attempt to circumvent the apparent implication in *Torcaso* that the "Supreme Being Clause" is unconstitutional. For example, in *George v. United States* the circuit court had reasoned that the right to exemption from combat service is a privilege which the Congress can grant or deny at will. The court there asserted that:

> It is established constitutional doctrine of long standing that exemptions of this character do not spring from the Constitution, but from the Congress. . . . This being so, there is brought into play the familiar principle that whatever the Government, State or Federal, may take away altogether, it may grant only on certain conditions. Otherwise put, whatever the Government may forbid altogether, it may condition even unreasonably.

If by this the court meant that since Congress is free to completely deny an exemption to conscientious objectors it can impose unreasonable qualifications upon the exemption, then the court seems to have overstated its position. Since the new form of the first amendment now forbids Congress from distinguishing between religious beliefs which suppose the existence of a Supreme Being and those which do not, the Congress scarcely has the power to impose a qualification in express violation of this new meaning of the first amendment. Certainly authority for the proposition that this cannot be done under the general powers of the Congress may be found in a number of cases.

On the other hand, in the factual situation in *Torcaso*, Maryland did not require an oath of belief in God for any of its other political officers, including the far more responsible position of Governor. Thus, to require such an oath from men seeking to discharge the purely ministerial functions of a notary public seems to be, on its face, an unreasonable requirement. However, the "Supreme Being Clause," as a test of sincerity in the Selective Service Act, does not appear to be so intrinsically arbitrary or unreasonable. It appears to be based on a solid and workable foundation. Congress employed this test for its objective attributes with the intention of avoiding an unrealistic, and unworkable, purely subjective test. Nevertheless, in light of *Torcaso*, it seems that only a test coming under the latter standard would be sanctioned by the Supreme Court. Had the Supreme Court in *Torcaso* confined itself to the much

---

120 195 F.2d 445 (9th Cir.), cert. denied, 334 U.S. 843 (1952).
121 Id. at 449-50.
narrower ground of "reasonableness" it would not have created the problem it must inevitably face under the Selective Service Act. Yet, despite the self-created problem, it is still conceivable that the Supreme Court will sustain the "Supreme Being Clause" as a legitimate exercise of the war power. This would certainly not be inconsistent with prior decisions of the Court.\(^\text{123}\) As the Supreme Court said in \textit{Macintosh}, the Congress

may grant or withhold the exemption as in its wisdom it sees fit . . . No other conclusion is compatible with the well-nigh limitless extent of the war powers . . . which include . . . the power . . . to compel the armed service of any citizen in the land . . . .\(^\text{124}\)

Thus, Congress can at least place reasonable restraints on the individual liberties in time of war, and the "Supreme Being Clause" might be reasonably construed as such a restraint. This test for the exemption is far from arbitrary. As has been pointed out, a less objective test would be unworkable. Since it is in the best interests of the defense of our country that true conscientious objectors be kept out of any military combat, and since it is equally important to prevent shirkers from avoiding their military duties, the present test could very possibly be upheld as a reasonable restraint under the guise of the war powers. However, the efficacy of this approach is certainly questionable. The fact that reasonable restraints may be placed upon the exercise of some constitutionally guaranteed rights during time of national emergency does not imply that these rights cease to exist absolutely. In affirming that the power to wage war is the power to wage war successfully, the Court has seemingly gone too far, and one cannot help but wonder whether it would have espoused the same extreme position after the War Crimes Trials subsequent to World War II.

Assuming for the sake of argument that the extent of the war power delineated in \textit{Korematsu v. United States}\(^\text{125}\) and \textit{Hirabayashi v. United States}\(^\text{126}\) is valid, when we take into consideration the Supreme Court's power to generate consent, is it really desirable for the Court to revalidate on principle an apparently expedient legislative infringement of first amendment rights? The Court would with one hand be rigidly safeguarding the individual liberties, here the first amendment liberties, while


\(^{124}\) 283 U.S. 605, 623 (1930).

\(^{125}\) 323 U.S. 214 (1944).

\(^{126}\) 320 U.S. 81 (1943).
it would be taking them away with the other hand. This practice of relying on governmental necessity under the veil of the war power can ultimately lead to the total destruction of those individual liberties which the Supreme Court is so vigorously striving to protect.

The Court appears to have forced itself between the horns of a dilemma. On the one hand, it can temporarily suspend, during the time of war, what it recognizes to be basic constitutional rights—an approach which, as we have seen, is as dangerous as it is illogical. On the other hand, it can frustrate the accomplishment of what Congress clearly and carefully considered to be in the best interests of the country when it enacted the present conscientious objector provisions. For, by impliedly finding the present "Supreme Being" test violative of the first amendment as an unconstitutional definition of religion, the Court has effectively invalidated the use of any objective test in the practical application of the exemption provisions.

Of course, it might be argued that Congress could avoid the entire problem by either (1) authorizing a new conscientious objector exemption requiring only a subjective inquiry into the genuineness of the claimant's objections, or (2) eliminating the conscientious objector provision altogether. The first of these alternatives, however, seems patently unworkable. Absent an extrasensory perception on the part of the Selective Service examiners, a subjective test would be incapable of detecting and thwarting an attempted avoidance of military service by those whose objection arises only out of a desire to avoid the dangers of combat. Similarly, the second alternative would defeat Congress' determination that it is both politically desirable and in the best interests of the nation's defense to exempt from military duty those who object to such for religious reasons.

CONCLUSION

The difficulties which Congress must now face if it wishes to continue the conscientious objector exemption can be seen by a glance at the spectrum of conscientious objectors. At the extremes would be the conscientious Quaker, opposed to war in any form, and able to point to the historical belief of his sect and the sincerity of his co-religionists. At the other extreme, is the ordinary young male, eager to see the world, but naturally hesitant about killing or being killed.

In between these two extremes are: (1) the denominationally affiliated person who expresses a minority viewpoint within his denomination (such as the Catholic or Methodist conscientious objector in World War II);
(2) the conscientious objector who believes that God has forbidden men to kill each other—but is not affiliated with any denomination; (3) the objector affiliated with a humanitarian organization—atheistic or agnostic—but in which the denominational opposition is based upon social or humanitarian principles; (4) the independent, educated, articulate conscientious objector whose opposition may be based on “philosophical” reasons (e.g. war is a tool of capitalism), economic reasons (e.g. war creates a false economy), political reasons (e.g. war is an inept and inefficient instrument of foreign policy), or—as will usually be the case—for mixed reasons. Then comes the final, and most difficult category—the inarticulate conscientious objector. He is opposed to participation in war—because he is. No other reasons.

Given this broad spectrum, where can Congress draw the line? Up until now the line has been drawn at the extremity of the theistic believers. However, to move the line one notch and include the denominationally affiliated humanitarians—as the American Civil Liberties Union advocated in 1940 and in 1948, clearly discriminates against those without denominational affiliation and “establishes” the denominations by giving them a sacrosanct status.

Moreover, any further attempt to classify these objections to military service will be frustrated by the simple expedient of having a sufficiently articulate defendant designate his political, sociological or economic beliefs as “religious,” on the premise that they occupy the same place in his life as the theistic beliefs occupy in the lives of people who believe in a Supreme Being.

Thus, we return once again to what seems to be the basic problem which the extreme view of the establishment clause propounded in Torcaso raises: whether any branch of the government can constitutionally define the term “religious” in the first amendment without violating that amendment. The historical evidence clearly shows that the Founding Fathers and succeeding generations of Americans, although cautious in their language, clearly understood the term “religious” as being theistic in origin, concept and development. However, this historical understanding of the term has been brushed aside as irrelevant—and in the name of greater liberty. We are thus returned to the possibility that a frustrated Congress will abolish the conscientious objector provision entirely.

Thus, the Court’s espousal of what seems to be a doctrinaire position has deprived the law of its needed flexibility, and if rigidly adhered to, will produce logically insoluble conflicts. While the “Supreme Being
Clause” may seem objectionable to what Mr. Justice Douglas called the “fastidious atheist,”127 if it does in fact constitute a government acknowledgment of the value of religions, the fact remains that it is what the people through the action of their Congress at the time of the Constitution and ever since have expressed as desirable.128

127 Zorach v. Clauson, 343 U.S. 306, 313 (1952). Among the many cases which would have to be overruled by this new interpretation of the first amendment would be Tamarkin v. United States, 260 F.2d 436 (5th Cir. 1958), cert. denied, 359 U.S. 925 (1959). In that case the circuit court found that the evidence submitted by the appellant furnished a basis in fact for the board's decision that appellant's “beliefs in vegetarianism represented 'essentially political, sociological, or philosophical views, or a merely personal moral code,' as distinguished from 'belief in a relation to a Supreme Being involving duties superior to those arising from any human relation.'” 260 F.2d at 437.

128 If the “establishment of religion” clause, now coming to the fore is to be applied with due regard to existing conditions and the spirit of the times, must not the Court adopt a more positive and forward-looking attitude than it has yet taken? Is such an attitude disclosed by emphasis upon “a wall of separation between church and state”? Do not concepts of religious liberty and the distinction between religion and a religious cultus,—i.e. a sect or organization church,—made long ago in Davis v. Beason, suggest sounder bases of interpretation? Waite, Jefferson's “Wall of Separation”: What and Where?, 33 Minn. L. Rev. 494, 519 (1949).
COMMENT
LABOR ARBITRATION AND THE 1961-1962
SUPREME COURT

LEO WEISS*

Examining in detail six of the 1961-1962 Supreme Court decisions concerning labor arbitration under section 301 of the Labor-Management Relations Act, the author analyzes the effect of these decisions in the light of the Court's previous pronouncements in this area. Mr. Weiss finds that in spite of the Court's refusal during the past term to allow federal injunctions against strikes in violation of an arbitration agreement, the attitude of the Court is still very much in favor of expanding and strengthening the role of arbitration. The author thus concludes that the 1961-1962 cases represent another logical step in the development of a consistent national policy of encouraging the peaceful settlement of labor disputes by arbitration.

INTRODUCTION

More than five years ago the Supreme Court announced in the landmark Lincoln Mills cases that federal remedies were available to enforce the arbitration provisions of collective bargaining agreements. By holding that section 301 of the Labor-Management Relations Act had created a federal right to such relief, the Court recognized the existence of a "federal common law" in this area, and thereby added a new depth and effect to the concept of a national labor policy. The federal door ajar, the Court then construed this common law to be limited only by "the range of judicial inventiveness," which in turn was to be modified by the nature of the problem facing the Court. Firmly projecting the fed-

* Attorney for the National Labor Relations Board; LL.B., University of Michigan; LL.M., Georgetown University Law Center; Member of the Bar of the State of New York.

The views expressed in this article are those of the author and do not necessarily reflect the position of the National Labor Relations Board or any of its members.


(a) Suits for violation of contracts between an employer and a labor organization representing employees in an industry affecting commerce . . . or between any such labor organization, may be brought in any district court of the United States having jurisdiction of the parties, without respect to the amount in controversy or without regard to the citizenship of the parties.

(b) . . . Any money judgment against a labor organization in a district court of the United States shall be enforceable only against the organization as an entity and against its assets, and shall not be enforceable against any individual member or his assets.

3 353 U.S. at 456-58.
eral courts and the federal substantive law into the arena of labor-man-
agement relations, the Lincoln Mills Court overcame the then-prevalent
uncertainty about the nature of section 301 jurisdiction and at the same
time established a generalized framework for the resolution of arbitration
disputes on a federal basis.

Further, in its ancillary ruling that the Norris-LaGuardia Act did not
prohibit the federal courts from compelling arbitration under a collective
bargaining agreement, the Court eliminated one difficult problem already
on the judicial horizon, thereby providing much-needed guidance for the
lower courts. In this instance, perhaps as an example of the “judicial
inventiveness” which it expected from others, the Court reasoned that
the abuses sought to be reached by this legislation did not extend to
controversies over arbitration. Rather, the statute encouraged resort to
arbitration and other peaceful means of settling labor disputes. In
reaching this conclusion Mr. Justice Douglas stated:

Though a literal reading might bring the dispute within the terms of the Act
... we see no justification in policy for restricting § 301(a) to damage suits,
leaving specific performance of a contract to arbitrate grievance disputes to
the inapposite procedural requirements of the Act. ... The Congressional
policy in favor of the enforcement of agreements to arbitrate grievance disputes
being clear, there is no reason to submit them to the requirements of § 7 of
the Norris-LaGuardia Act.

However, beyond this declaration, a ready-made judicial guideline
was not to be found in the language of Lincoln Mills. In the main, the
Court limited itself to the announcement of general principles, leaving
the lower courts, both state and federal, to struggle with their practical
application.

4 For a discussion of the problems facing the courts after the enactment of § 301, see
(1962); Note, Arbitrability Under Section 301 of the Taft-Hartley Act, 12 Syracuse L. Rev.
6 353 U.S. at 458.
7 Ibid.
8 Ibid.
9 Many legal writers have discussed the subsequent development of a substantive body of
this law following Lincoln Mills. See Gregory, Enforcement of Collective Agreements by
Arbitration, 48 Va. L. Rev. 883 (1962); Hays, The Supreme Court and Labor Law, October
Term, 1959, 60 Colum. L. Rev. 901 (1960); Weiss, Labor Arbitration in the Federal Courts,
treatment of the probable ramifications of Lincoln Mills, see Bickel & Wellington, Legislative
It was not until 1960, in the *Steelworkers* cases,\(^\text{10}\) that the Court elaborated on its views concerning the contents of this new common law and defined the broad language of *Lincoln Mills*. Utilizing a subcontracting dispute, a post-arbitration case and a refusal to arbitrate as its vehicles for judicial expression, the Court in one ambitious morning clarified the scope of the arbitrable controversy by ruling that its merits were to be decided by the arbitrator and not by the courts, regardless of the disguise in which such action might be dressed.\(^\text{11}\) Moreover, a broad arbitration clause in a collective bargaining agreement was held to include all disputes arising under the contract except for those which the parties have specifically excluded.\(^\text{12}\) The burden was thus shifted from the one seeking arbitration to the one seeking to avoid it.

In like fashion, the Court held that "management prerogatives" now meant only those rights or functions which the contract expressly reserved for exclusive determination by management.\(^\text{18}\) At the same time, it upheld the enforceability of an arbitrator's award, thereby laying to rest the contention that only orders to compel arbitration were available in the federal courts.\(^\text{14}\)

The meaning of the *Steelworkers* and *Lincoln Mills* cases cannot, however, be limited to the specific holdings described above or the many subsidiary findings and conclusions which are contained therein.\(^\text{15}\) Rather, of equivalent importance was the creation of an atmosphere in which the greatest values were placed upon the peaceful settlement of disputes through use of machinery designated by the parties for that purpose.\(^\text{16}\) To this end the litigants, the arbitrators and the courts were encouraged to


\(^\text{11}\) 363 U.S. at 568.

\(^\text{12}\) Id. at 584-85.

\(^\text{13}\) Id. at 583-84.

\(^\text{14}\) See A. L. Kornman v. Amalgamated Clothing Workers, 264 F.2d 733 (6th Cir. 1959) (dissenting opinion).

\(^\text{15}\) Many legal writers have discussed the possible ramifications of the *Steelworkers* holdings. See Gregory, supra note 11; Hays, supra note 11; Mayer, Labor Relations, 1961: The Steelworkers Cases Re-examined, 13 Lab. L.J. 213 (1962); Note, 46 Cornell L.Q. 336 (1961); Note, supra note 9.

\(^\text{16}\) One writer has described the *Steelworkers* and other § 301 decisions of the Supreme Court as reflecting "a flexible approach to the collective bargaining agreement which casts aside previous obsequiousness to the literal word as the sterility of a by-gone era." Gould, Taft-Hartley Revisited: The Contrariety of the Collective Bargaining Agreement and the Plight of the Unorganized, 13 Lab. L.J. 348, 349 (1962).
use every available means to make the arbitration process effective. The key can be found in Mr. Justice Douglas' statement for the majority:

An order to arbitrate the particular grievance should not be denied unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute. Doubts should be resolved in favor of coverage.\(^{17}\)

However, as was perhaps to be expected, while in its decisions in the *Steelworkers* cases the Supreme Court once again answered some questions, left others untouched and raised a host of new questions to be decided in future cases. And once again, the lower state and federal courts, doing as they thought best in this area, sometimes effectuated the policies announced by the Court, sometimes hindered them, and at other times merely manifested their uncertainty as to what the Court expected.\(^{18}\)

The result of this was that at the commencement of the 1961-1962 term it was evident that deep-rooted problems still remained within the framework of section 301.\(^{19}\) It was questionable whether the courts were at liberty to write a "no-strike" clause into a labor contract containing an arbitration clause;\(^{20}\) and beyond this, there remained a serious problem as to the effect of the restrictive provisions of the Norris-LaGuardia Act on the injunctive powers of federal courts.\(^{21}\) Finally, in spite of the language of the Court's earlier holdings, questions still remained as to the proper role of the state courts in the arbitral process of section 301.\(^{22}\)

Faced with these problems and with a mixed development in the lower courts, the Supreme Court finally came to grips with these issues in the 1961-1962 term in a manner that will have a strong impact on the field of labor arbitration for many years to come.

For this reason it seems appropriate, if not necessary, to examine these decisions as they arose and then to briefly analyze them as a whole to determine whether, when added to the *Lincoln Mills* and *Steelworkers* cases, they represent a realignment of the previous judicial attitude on these matters or whether they should be considered as merely another logical step in the gradual development of a consistent federal arbitration policy.

\(^{17}\) 363 U.S. at 582-83.

\(^{18}\) For a review of the cases decided during this period, see Note, Arbitrability Under Section 301 of the Taft-Hartley Act, 12 Syracuse L. Rev. 332, 333-35 (1961).


\(^{22}\) See Charles Dowd Box Co. v. Courtney, 368 U.S. 502 (1962).
The first section 301 controversy which faced the Court during the past term involved a resolution of the jurisdictional difficulties created by the broad language of Lincoln Mills. Since the Lincoln Mills Court had unequivocally stated that section 301 was "more than jurisdictional," i.e., that it authorized federal courts to fashion, from the policy of our national labor laws, a body of federal law for the enforcement of agreements within its ambit,23 it was unclear whether the substantive concepts of federal law fostered by that decision would be frustrated if state courts were allowed to exercise concurrent jurisdiction over suits within the purview of section 301(a). In Charles Dowd Box Co. v. Courtney,24 Mr. Justice Stewart finally laid this controversy to rest.

In Dowd Box, a union sued an employer in a state court for an alleged violation of a collective bargaining agreement, seeking an accounting, damages, and an injunction. The state court, rejecting the employer's main contention that section 301 deprives state courts of jurisdiction over such controversies, entered a money judgment for the union in conformity with the wage provisions of the agreement.25

Affirming the state court's rejection of federal pre-emption of this field, the Supreme Court firmly established concurrent state-federal jurisdiction of section 301 suits. In reaching this conclusion, Mr. Justice Stewart pointed out that the intent of Congress was that section 301(a) suits "may" be brought in federal district courts, not that they "must" be brought there.26 The Court then proceeded to a brief examination of the history of the enforcement of federal rights in state courts and declared:

We start with the premise that nothing in the concept of our federal system prevents state courts from enforcing rights created by federal law. Concurrent jurisdiction has been a common phenomenon in our judicial history, and exclusive federal court jurisdiction over cases arising under federal law has been the exception rather than the rule.27

To bolster this finding, a greater part of the Court's effort was devoted to a detailed examination of the legislative history of section 301. Since this history highlighted the increasing congressional concern over the inadequacy of earlier state remedies both because of the unincorporated-

26 368 U.S. at 506.
27 Id. at 507-08.
association status of most unions and because of the difficulty in bringing suits in their behalf in many of the state courts, the Court had no difficulty in declaring that the "entire tenor of the 1947 legislative history confirms that the purpose of § 301 . . . was to fill the gaps in the jurisdictional law of some of the States, not to abolish existing state court jurisdiction."

In adopting this tack, however, the Court did not fail to note the danger of a lack of uniformity among the state and federal court decisions a problem which might arise from its unequivocal stand on the concurrent jurisdiction dilemma. Recognizing this, Mr. Justice Stewart admitted that "'diversities and conflicts' may occur . . . as there evolves in this field of labor management relations that body of federal common law of which Lincoln Mills spoke." But, at the same time he pointed out that one of the traditional functions of the Court is "to resolve and accommodate such diversities and conflicts." Thus, the Court acquiesced in the inevitable diversity in the lower courts and entrusted the resolution of this problem to its own future decisions.

Although by this reasoning the Court seemed to have avoided a resolution of the problem of diversity of results in section 301 suits, a closer reading of the opinion and its rationale indicates that the end result of this holding was to reinstate the Lincoln Mills concept of a uniform federal common law with considerably more emphasis than ever before.

For, while establishing concurrent jurisdiction in the state courts, the Dowd Box Court clearly re-emphasized the holding of Lincoln Mills to the effect that all these cases were to be decided under the prevailing

---

28. Id. at 512. It should be noted that Dowd Box was not an arbitration case, but a controversy over wages, holidays and vacations. Also, the outcome resulted in direct personal benefit to the employees, thus seemingly conflicting with the "uniquely personal rights" theory of Association of Westinghouse Salaried Employees v. Westinghouse Elec. Corp., 348 U.S. 437 (1955). Finally, in December 1962, ten months after deciding Dowd Box, the Court unequivocally rejected the idea that "all suits to vindicate individual employee rights arising from a collective bargaining contract should be excluded from the coverage of § 301." Smith v. Evening News Ass'n, 31 U.S.L. Week 4041 (U.S. Dec. 10, 1962). Actually, the Supreme Court has been gradually abandoning the "uniquely personal rights" doctrine ever since Lincoln Mills.

29. 368 U.S. at 514.

30. Ibid.

federal law.32 Thus, the holding in *Dowd Box* did not authorize the state courts to decide section 301 suits within the narrow limits of state law alone. Regardless of the forum, the federal "common law" must prevail. This being so, there is little likelihood that the inclusion of the state courts within the forums available for section 301 suits will bring about any greater diversity than that which was already to be found in the federal system.

On the contrary, it would seem that the more probable result of the *Dowd Box* holding will be to decrease the extent of diversity that presently marks the law in this area. For, notwithstanding the doubt which existed concerning the states' jurisdiction over section 301 suits prior to *Dowd Box*, the fact remains that many state courts had exercised this jurisdiction, though not clearly stating their grounds therefor.33 Moreover, in deciding these cases, they at times appeared to pay no more than lip service to the *Lincoln Mills* doctrine, preferring instead to decide these cases in accordance with state law.34 By reiterating the principles laid down in *Lincoln Mills* and by again making it clear that they are to apply in state as well as federal courts, the Supreme Court in *Dowd Box* has once more strengthened the place of arbitration in the labor relations complex.

*Local 178, Retail Clerks Ass'n v. Lion Dry Goods, Inc.*

While the *Dowd Box* Court clarified an important procedural point in the area of judicial enforcement of arbitration agreements, it left untouched many other important but as yet unanswered questions that had arisen concerning section 301 of the Taft-Hartley Act. Paramount among these were the uncertainties concerning the type of labor contract necessary to confer jurisdiction on the courts under that section and

32 See 368 U.S. at 506-07. This point was made even clearer in the subsequent case of *Local 174, Teamsters Union v. Lucas Flour Co.*, supra note 31 where the Court stated that "incompatible doctrines of local law must give way to principles of federal labor law." Id. at 102.

33 Five years before *Dowd Box*, the California Supreme Court had held that § 301 did not foreclose state jurisdiction. *McCarroll v. Los Angeles County Dist. Council of Carpenters*, 49 Cal. 2d 45, 315 P.2d 322 (1957), cert. denied, 355 U.S. 932 (1958). A comprehensive discussion of state jurisdiction under § 301 may be found in *Meltzer*, supra note 31.

34 In *Local 174, Teamsters Union v. Lucas Flour Co.*, 369 U.S. 95 (1962), for example, the action was originally brought in a state court which not only held that it had jurisdiction to award damages for a strike in violation of an arbitration agreement but which also stated that in deciding the case it was not bound by principles of federal law. Id. at 102.
the status which the union must have before it can bring an action under it. However, these questions were soon to be put before the Court in *Local 178, Retail Clerks Ass'n v. Lion Dry Goods, Inc.*,\(^35\) the second of the six section 301 cases to come before it during the 1961-1962 term, where the Court was asked to decide (1) does section 301 apply to a contract which is not a collective bargaining agreement? (2) may a union sue under that section if it does not represent a majority of the employees in the bargaining unit? Liberally interpreting section 301(a)'s reference to "contracts between an employer and a labor organization representing employees in an industry," the Court answered both questions in the affirmative.

In *Lion Dry Goods*, the respondent department stores and the union, which represented only a minority of the store employees, reached an impasse in negotiations for renewal contracts. After a strike, the parties signed a statement characterized by the lower court as a "strike settlement agreement," which included, among other conditions, an agreement to submit grievances to a suitable forum for arbitration and to abide by the subsequent decision. When the company refused to abide by the arbitrator's award, the union brought suit in a federal district court pursuant to section 301(a) to compel the stores to correct the situations which precipitated the grievances. The district court held that it did not have jurisdiction over the subject matter of the dispute since (1) the contract here involved was not a collective bargaining agreement as contemplated by section 301(a), and (2) the union involved did not represent a majority of the employees of the stores.\(^36\) The Court of Appeals for the Sixth Circuit affirmed this judgment, though it was not clear whether it approved one or both grounds of the district court's holding.\(^37\) The Supreme Court granted certiorari because of the importance of the jurisdictional question presented as to the enforcement of the "national labor policy."\(^38\)

In interpreting the provisions of section 301(a), the Court was faced with a notable lack of authoritative precedent. As indicated in the Court's opinion,\(^39\) the district court had relied heavily on dictum from *Schatte v. International Alliance*\(^40\) to the effect that section 301(a) applies only to

\(^{35}\) 369 U.S. 17 (1962).


\(^{37}\) 286 F.2d 235 (6th Cir. 1960).

\(^{38}\) 369 U.S. at 18-19.

\(^{39}\) Id. at 24 n.6.

\(^{40}\) 84 F. Supp. 669, 672 (S.D. Cal. 1949).
"collective bargaining agreements." However, the Supreme Court quickly nullified the effect of the Schatte dictum by quoting an earlier Supreme Court case in which Mr. Justice Jackson had stated that a "contract in labor law is a term the implications of which must be determined from the connection in which it appears." But other than refuting the Schatte dictum, this language was of little assistance to the Court. Nor were any real guidelines to be found in the Court's earlier opinion in Lincoln Mills, perhaps because the Court was there concerned only with true collective bargaining agreements.

Thus, the Court was forced to look beyond the scant judicial precedent interpreting section 301(a) and instead place almost total reliance on the intent of Congress in enacting this legislation. In so doing, it found that the language of the section itself, viewed in the light of the lawmakers' compromises in writing the act, indicated that had Congress intended to restrict its application to collective bargaining agreements, it would have done so in explicit terms.

In arriving at this holding, the policy considerations before the Court were evidently of overriding importance. Stating that it is enough to confer jurisdiction on federal courts under section 301(a) "that this is clearly an agreement between employers and labor organizations significant to the maintenance of labor peace between them," the Court concluded that to hold otherwise would defeat the purpose of the statute by disrupting stable labor relations and consequently, interstate commerce. To justify the importance which it attributed to the strike settlement agreement in question, the Court pointed out that the sole purpose of such a contract was to avoid the economic harm which might result from a protracted strike, by restoring workers to their jobs and enabling the employer's plant to resume full production. Moreover, as the Court also noted, such an agreement affects the employees' working conditions just as any formal collective bargaining agreement would. For these reasons, the Court concluded: "If this kind of strike settlement were not enforceable under § 301(a), responsible and stable labor relations would suffer, and the attainment of the labor policy objective of

42 369 U.S. at 27.
43 Id. at 28.
44 Id. at 27.
45 Id. at 28.
46 Ibid.
minimizing disruption of interstate commerce would be made more difficult.\footnote{Id. at 27.}

With regard to the second question the Court, again adopting a legislative history-policy approach, quickly disposed of the argument that section 301(a) applies only to unions which are the exclusive bargaining agents of the employees. It noted that the language of section 301(a) is almost identical with the language of section 301(b) and that the contention that the latter subsection is applicable only to majority representatives, had already been rejected by the Court.\footnote{Id. at 29.}\footnote{Ibid.} In addition it once more argued that had Congress intended section 301(a) to apply only to majority representatives, it would have explicitly so provided.\footnote{Ibid.} Finally, reasoned the Court, requiring a federal court to determine whether a union is the majority representative would conflict with those provisions of the Taft-Hartley Act which give the NLRB exclusive jurisdiction to make such determinations.\footnote{Ibid.} Thus, it concluded, the federal courts clearly must have jurisdiction in such instances.

Considering these two facets of the Court’s decision in \textit{Lion Dry Goods} together with its earlier opinion in \textit{Dowd Box}, it becomes evident that the Court once again expanded the role which the arbitrator is to play in the resolution of labor disputes. Whereas in \textit{Dowd Box} the Court increased the forums available for the enforcement of arbitration agreements, in \textit{Lion Dry Goods} it first increased the types of contracts which could be enforced under section 301 and then it liberalized the “standing” requirements as to the status which a union must have before it can enforce an arbitration provision under that section. As to the first half of the \textit{Lion Dry Goods} opinion, however, the caveat must be made that, in holding the arbitration provision in the strike settlement agreement of that case to be enforceable, the Court stopped short of delineating the precise nature of the types of agreements covered by section 301. Thus, the enforceability of arbitration provisions contained in contracts, other than collective bargaining agreements and strike settlement agreements such as the one in \textit{Lion Dry Goods}, still remains uncertain. Nevertheless, the decision in that case seems to reflect a continuation of the same liberal interpretation of section 301 which has marked the Court’s decisions in the past.

\footnote{Id. at 27.} \footnote{Id. at 29.} \footnote{Ibid.} \footnote{Ibid.}
Local 174, Teamsters Union v. Lucas Flour Co.

The third section 301 case to come before the Supreme Court during the last term concerned one of the most hotly disputed issues in the entire arbitration area; namely, whether a strike can violate a collective bargaining agreement which does not contain a "no-strike" clause but which does contain an arbitration provision for the settlement of disputes. The courts of appeals for five circuits had considered this question before it came to the Supreme Court by way of the Washington Supreme Court. In Local 174, Teamsters Union v. Lucas Flour Co., the Supreme Court answered this question affirmatively.

In Lucas Flour a union called a strike in order to force an employer to rehire an employee who had allegedly been discharged because of unsatisfactory work. While a board of arbitration was considering the union's appeal, the employer brought a suit against the union in a Washington state court seeking damages for losses attributable to the strike instituted by the union. Distinguishing the pre-emption doctrine of San Diego Bldg. Trades Council v. Garmon, the state supreme court held that it was not deprived of jurisdiction to resolve the controversy, and further that the Labor-Management Relations Act could not "reasonably be interpreted as pre-empting state jurisdiction or as affecting it by limiting the substantive law to be applied." The suit was thus decided on the basis of state law.

The first issue presented to the Supreme Court was whether the terms of section 301 of the Labor-Management Relations Act deprived the state judicial system of jurisdiction over a suit of this nature. Adopting the rationale of Lincoln Mills and Dowd Box, the Supreme Court agreed that in this instance the state court was a proper forum for adjudication, but denied that it could use state law as the basis for its decision, since under Lincoln Mills the federal substantive law was an adjunct of section 301 and therefore must be utilized as the basis of any decision on the merits. However, since the state and federal law on the substantive matters involved in the case were not inconsistent, the Court refused to consider this as grounds for reversal.


52 369 U.S. 95 (1962).


54 57 Wash. 95, 102, 356 P.2d 1, 5 (1962).

55 369 U.S. at 103.
Having disposed of this point, the *Lucas Flour* Court went on to decide the principle question before it: "Whether as a matter of federal law, the strike which the union called was a violation of the collective bargaining contract . . . ." Pointing to the fact that by the terms of their collective bargaining agreement both parties had agreed that the dispute which gave rise to the strike was to be exclusively decided by arbitration, the Court followed the lead of the lower federal courts\(^5\) and held that it did. The Court stated simply: "To hold otherwise would obviously do violence to accepted principles of traditional contract law."\(^6\)

In support of its holding that a "no-strike" clause may be implied from a collective bargaining agreement of this nature, the Court uses little explanation or rationale. Rather, harking back to *Lincoln Mills*, a strong reliance is placed on "the basic policy of national labor legislation to promote the arbitral process as a substitute for economic warfare."\(^7\) Thus, a pervasive desire to avoid economic disruption seems, in reality, to have been the motivating factor behind the Court's interpretation of what the parties actually intended when they incorporated a broad arbitration provision within the terms of their collective bargaining agreement.

However, after adopting this approach, the Court proceeded to restrict its holding by limiting it to those instances where the dispute resulting in the strike is clearly covered by the arbitration provision of the collective bargaining agreement. It rejected out of hand the contention that *any* collective bargaining agreement is violated by a strike and limited the effect of its decision to those cases where the dispute over which the union strikes is subject to arbitration under the contract; if not, the union is free to strike.\(^8\)

In spite of the narrowness of the majority opinion in *Lucas Flour*, Mr. Justice Black had difficulty in justifying the importation of a "no-strike" clause into an agreement from which it was excluded. He argued that such a provision is so vital to both employer and union that it is inconceivable that it can be left out of a contract by inadvertence. Since no one claimed that the parties in this case had, by their conduct, implied the existence of a promise not to strike, the Court, according to Mr. Justice Black, was creating a strict rule of law that negotiation of an arbitration clause necessarily includes a "no-strike" clause. He concluded that

---

\(^5\) See cases cited note 51 supra.
\(^6\) 369 U.S. at 105.
\(^7\) Ibid.
\(^8\) Id. at 105 n.14.
while both arbitration clauses and "no-strike" clauses serve useful and worthwhile purposes and are in accord with our national labor policy, there is no warrant for writing either provision into a contract when the parties have omitted it.\textsuperscript{60} Thus, he declared, "I would . . . relegate this controversy to the forum in which it belongs—the collective bargaining table.\textsuperscript{61}

While Mr. Justice Black’s dissent seems concerned with what should be inferred from the precise terms of the contract, it must be noted that the language of the \textit{Lucas Flour} contract did, at least, provide that there would be no "work stoppage" over an issue which has \textit{been} submitted to arbitration\textsuperscript{62} and that it was undenied that the dispute in question was subject to binding and final arbitration.\textsuperscript{63} Examined in this context, the result reached in \textit{Lucas Flour} appears to be neither surprising nor unreasonable. Rather it indicates only what has been said, or at least implied, many times before, namely, where an arbitration agreement will reasonably support an interpretation which will promote its effectiveness, that will be the interpretation which the courts will favor. It seems clear that the \textit{Lucas Flour} Court’s interpretation of the contract before it was another in the line of judicial decisions promoting the effectiveness of an arbitration agreement.

\textit{Drake Bakeries, Inc. v. Local 50, American Bakery Workers Atkinson v. Sinclair Ref. Co.}

The vital importance of carefully drawn contract language is illustrated by the opposite results reached by the Court in \textit{Drake Bakeries, Inc. v. Local 50, American Bakery Workers}\textsuperscript{64} and \textit{Atkinson v. Sinclair Ref. Co.},\textsuperscript{65} the next two section 301 cases to come before it last term. In \textit{Drake}, the employer, who was normally closed on Saturday, scheduled work for the Saturdays following Christmas and New Year’s (which fell on Fridays) and instead gave the employees the prior Thursdays off. The union protested, claiming that its contract prohibited unilateral change of the normal work schedule, and most of the employees did not report for work. The employer sued the union for damages in a federal court, alleging violation of the "no-strike" clause in the collective bargaining

\begin{footnotes}
\item[60] \textit{Id.} at 110.
\item[61] Ibid.
\item[62] \textit{Id.} at 96.
\item[63] \textit{Id.} at 105 n.12.
\item[64] 370 U.S. 254 (1962).
\item[65] 370 U.S. 238 (1962).
\end{footnotes}
agreement, and bypassing the procedure established by the contract, although the arbitration clause was broadly drawn so as to cover "any act or conduct or relation between the parties."

Moving for a stay of the action pending arbitration, the union denied there had been a strike, denied it had instigated a strike, denied that the employees were obligated to work on the disputed Saturday, and claimed that the employer had violated the contract by scheduling such work. Both the district court and the Second Circuit accepted the union's contention that the dispute was arbitrable and should not be litigated until the arbitrator handed down his award. The Supreme Court affirmed.

Mr. Justice White pointed out that the contract's language was clear and that it unquestionably covered the controversy. He rejected the employer's argument that violation of the "no-strike" clause was such a fundamental breach of the agreement that it justified him in refusing arbitration. Instead, he thought it more likely that so vital a part of the contract would be excluded from arbitration only by specific agreement of the parties. Since such an agreement did not exist here, the employer then urged that it be implied from the inherent nature of labor contracts and "no-strike" clauses. This the Court also refused to do.

Justifying the Court's decision, Mr. Justice White emphasized that it gives effect both to the arbitration clause and the "no-strike" clause. The arbitrator may now decide whether there actually was a strike and if the union was responsible; if so he may award damages. Consequently, the employer loses no remedy that he might otherwise have. Should the Court have held the other way, however, only the "no-strike" clause would have been made effective, and the arbitration provision would have been eliminated. No reason seems to exist for such a result. Rather, the exact opposite is in accord with the national labor policy of encouraging arbitration of as many disputes as possible.

A short but vigorous dissent by Mr. Justice Harlan argued that courts are as capable as arbitrators to decide whether there has been a strike in breach of contract and the appropriate damages. An arbitrator's expertise is more likely to be in the field of employee grievances. Since the arbitrator's award is not self-executing, the employer will have to go to

66 294 F.2d 399 (2d Cir. 1961).
67 370 U.S. at 261.
68 Id. at 266.
69 Id. at 267.
court eventually to enforce it and this decision deprives him of the most direct route.

While in the *Drake Bakeries* case, the Court relied on the contract's broad arbitration language, in *Atkinson*, where the contract language was narrow, the Court held that a stay pending arbitration was not warranted.70

There the employer had docked three men a total of $2.19, in retaliation for which the entire plant stopped work for two days. Suing the union in a federal court for damages resulting from the work stoppage, the employer was met with the argument that the dispute should be arbitrated and that the court action should await the outcome of that arbitration. The union also claimed that it had filed a number of grievances involving issues identical to those involved in the court action.

This last contention was rejected by the Supreme Court, as it could visualize a number of different ways in which the outcome of the grievances might have no effect on the outcome of the court action.71 More important, however, it held that the employer had no right under the contract to initiate arbitration over his own complaints and that this procedure was restricted to complaints of employees.72 Since he had no adequate remedy in arbitration, it was proper for the employer to bring an action in the district court and there was no justification for staying that action.

In analyzing the effect of *Drake Bakeries* and *Atkinson*, it is necessary to refer back to the Court's previous holding in *Lucas Flour*, for these two later decisions appear, at least, to modify the force of the earlier one. In *Lucas Flour* the employer was allowed to bring a court action for damages caused by the union strike, but in *Drake Bakeries*, where the arbitration provision appeared no broader than that in *Lucas Flour*,73 the Court held that if the union moved within a reasonable time to submit the question of its striking to arbitration, the court action must be stayed and the issue of damages must be decided by the arbitrator. Thus, as to the issue of damages, *Drake Bakeries* appears to give the union its choice of forums, *i.e.*, the court or the arbitrator. Of course this will not be the case if the arbitration provision is of the narrow type seen in *Atkinson*. However, even conceding this limitation, the fact remains that added

---

70 370 U.S. 238 (1962).
71 Id. at 243-45.
72 Id. at 241-42.
73 Compare the arbitration provision in *Lucas Flour*, 369 U.S. at 96, with that in *Drake Bakeries*, 370 U.S. at 259 n.4.
importance has been attributed to the arbitration agreement; for, just as Lucas Flour authorized a damage action to discourage violations of the arbitration agreement in the form of strikes, Drake Bakeries has gone on to place the granting of this relief within the power and jurisdiction of the arbitrator.74

**Sinclair Ref. Co. v. Atkinson**

Climaxing the Court's 1962 decisions concerning section 301 was Sinclair Ref. Co. v. Atkinson,75 another aspect of the case we have just been examining. There the vital question of whether the Norris-LaGuardia Act76 still prevented federal courts from issuing injunctions against strikes in violation of a collective bargaining agreement was also answered by the Court in the affirmative.

In Sinclair the employer had been plagued by repeated work stoppages, slowdowns and short strikes over a period of nineteen months, all caused by controversies over matters which were subject to the grievance and arbitration provisions contained in the union contract. Claiming that there was no adequate remedy at law for the damage caused by the union's conduct and that the union was violating its "no-strike" clause, the employer sought an injunction in the United States District Court. Its refusal to grant the injunction was upheld by the Seventh Circuit and was consistent with decisions in two other circuits.77 The Tenth Circuit, however, had ruled that Norris-LaGuardia did not bar an injunction under such circumstances.78

In its decision, the Supreme Court first stated that all the disputes over which work had been halted were labor disputes within the meaning of

74 The Court in Atkinson also gave burial to another potentially explosive problem when it held that § 301 absolves union members from liability for the misconduct of the union even though a union can act only through its individual officers and agents. The Court emphasized that:

[The legislative] policy cannot be evaded or truncated by the simple device of suing union agents or members, whether in contract or tort, or both, in a separate count or in a separate action for damages for violation of a collective bargaining contract for which damages the union itself is liable.

370 U.S. at 249.

75 370 U.S. 195 (1962).


77 Sinclair v. Atkinson, 290 F.2d 312 (7th Cir. 1961), aff'd, 370 U.S. 195 (1962); A. H. Bull S.S. Co. v. Seafarer's Union, 250 F.2d 236 (2d Cir. 1957); W. L. Mead, Inc. v. Local 25, Teamsters Union, 217 F.2d 6 (1st Cir. 1954).

Norris-LaGuardia. This meant that federal courts could not issue injunctions in such cases unless section 301 repealed the anti-injunction provisions in connection with breaches of collective bargaining contracts. However, an analysis of the language of section 301, a review of those portions of Taft-Hartley which specifically repealed portions of Norris-LaGuardia, and an examination of the legislative history of section 301, convinced the Court that Congress had no such intention.\textsuperscript{79}

The Court similarly rejected the idea that Norris-LaGuardia was not intended to apply to disputes over breach of contract since its policy statement included language encouraging “liberty of contract.” Rather, the Court held that the act was aimed precisely at preventing all enjoining of strikes by the federal courts and the fact that such strikes arose out of breaches of contract was irrelevant. This is to be distinguished from the problem which arises when a federal court issues an order compelling arbitration. Refusal to arbitrate was not contemplated by Congress as within the evils sought to be remedied by Norris-LaGuardia. \textit{Lincoln Mills}, therefore, could order arbitration without going afoul of the anti-injunction statute.\textsuperscript{80}

Another argument rejected by the Court was that Congress intended that both Norris-LaGuardia and section 301 be “accommodated” to each other by a court’s determination whether, in any particular case, public policy required that an injunction should issue. This, and the contention that injunctions are indispensable in making the arbitration process effective, were declared by the court to be arguments which may be addressed to Congress but not to the courts. As a matter of policy, Congress could do such things; it could even repeal the anti-injunction provisions entirely if it thought that an employer should have injunctive relief available to him. Such a power, however, had never been given to the courts.

Moreover, the Court noted that the existing law does not completely destroy the employer’s remedies. He may still sue for damages, or he may obtain an order compelling the union to arbitrate. But he is not entitled to enjoy the benefits of an injunction, for “Congress was not willing to insure that enjoyment . . . at the cost of putting the federal courts back into the business of enjoining strikes and other related peaceful union activities.”\textsuperscript{81}

\textsuperscript{79} 370 U.S. at 199, 203-06.
\textsuperscript{80} A thorough discussion of the relative merits of arbitral versus judicial enforcement of no-strike clauses and a persuasive argument that the courts are the proper forum for such enforcement can be found in Stewart, No-Strike Clauses in the Federal Courts, 59 Mich. L. Rev. 674 (1961).
\textsuperscript{81} 370 U.S. at 214.
Mr. Justice Brennan was joined by Justices Douglas and Harlan in a strong dissent. He argued that it was possible to accommodate both the Norris-LaGuardia Act and section 301 of the Taft-Hartley Act, that both were applicable to the case at bar, and that it was "our duty . . . to seek out that accommodation of the two which will give the fullest possible effect to the central purposes of both." 82

This is what the Court has done, according to the dissenters, in the Railway Labor Act 83 and in case of enforcement of the agreement to arbitrate under section 301. 84 In both instances, Norris-LaGuardia might have stood in the way of the issuance of court decrees, but the Supreme Court found that there were compelling reasons to allow injunctions. That kind of logic, they argued, is even more applicable in the instant situation because the union has actually signed a voluntary agreement not to strike. Further, the fact is that enforcement of an arbitration clause is considerably weakened by unavailability of an injunction against a strike pending arbitration. At the same time, the union suffers no substantial harm because by giving up its strike weapon it has gained a sufficient alternative remedy—arbitration enforceable in the courts. This, according to the dissenters, was not the kind of situation which induced Congress to enact Norris-LaGuardia. 85

What effect the instant decision will have on state court actions is also questioned by the dissent. If the state courts must follow it, then section 301 has deprived employers of a remedy which they once had—the state court injunction. But section 301 was designed to increase the remedies available to the parties, not decrease them. Yet, if the state courts need not follow this case, then there will never develop that uniform body of federal law concerning collective bargaining agreements which was contemplated by Lincoln Mills, Dowd Box and Lucas Flour. And while such uniformity might be advanced by the availability of removal from state to federal courts, the language of the removal statute is such as to cast grave doubt on whether it may be used in this fashion. 86

82 Id. at 216.
84 See note 6 supra and accompanying text.
85 370 U.S. at 222-24.
86 In his dissent in Sinclair Ref. Co. v. Atkinson, 370 U.S. 195 (1962), Mr. Justice Brennan predicted that such a solution would lead unions to seek removal from state to federal courts, a factor which would militate in favor of uniformity. But he doubted that removal would be allowed and his doubt is well-grounded since the statute allows removal only in cases "of which the district courts of the United States have original jurisdiction." 28 U.S.C. § 1441 (1958). Because Norris-LaGuardia deprives the district courts of juris-
As the dissent in *Sinclair* indicates, of the six important section 301 cases which came before the Supreme Court during its October 1961 term, only the last raises serious questions concerning a change in the Court's attitude towards the role of arbitration in the federal labor relations scheme. Certainly the Court's thinking in *Sinclair* seemed to deviate from what it was in *Drake Bakeries* where it emphasized that the submission of an issue to arbitration deprived neither party of its legal rights since these rights could be as effectively protected by arbitration as they could by litigation. Indeed, a similar argument might have been advanced in *Sinclair* by arguing that the rights which the union sought to protect by means of a strike could have been just as adequately protected without weakening the force of the arbitration agreement had the union submitted its dispute to the arbitrator instead of striking. By refusing to allow an injunction against a strike in violation of an arbitration agreement the Court has thus seemingly wavered in its previously unequivocal support of an effective arbitration process.87

**The Meaning of the 1961-1962 Cases**

What conclusions may be drawn from the Supreme Court's pronouncements concerning section 301 during the past term? Has the Court departed from *Lincoln Mills* and *Steelworkers* or has it remained consistent, merely filling in some details where the picture was blurred, thereby giving unions and management new knowledge and certainty to help them in their dealings with each other?

It seems quite clear, first of all, that the Court has no intention of substantially departing from the earlier cases. In *Dowd Box*, *Drake Bakeries* and *Lucas Flour* it has re-emphasized its reliance on the *Lincoln Mills* doctrine and its determination to put the power of the federal judiciary behind the enforcement of arbitration agreements. In *Lucas Flour* it also insisted that the parties abide by the contracts they have made—not a revolutionary doctrine, certainly, but one which some employers and unions have honored more in the breach than in the observance.

In *Dowd Box*, the Court strengthened the arbitration clause by making it enforceable in state as well as federal courts. With one stroke, the Court tremendously increased the number of forums where such issues

---

87 See 370 U.S. at 225, 227.
may be litigated. At the same time, the Court signified its refusal to abandon its supervisory function over every court which tries such an action, thereby guaranteeing that the law in this area will develop in a consistent and uniform manner. Litigants can thus be certain that whether they take their controversy to a state or a federal court and regardless of the state in which their case happens to arise, the judgment will be based on the same substantive principles.

The Court in *Drake Bakeries* also resisted efforts to water down section 301 by limiting it to certain kinds of contracts and certain kinds of unions. The statute says: "Suits for violation of contract between an employer and a labor organization . . ." and the Court rejected the attempts to limit the meaning of that clear language. It now appears that whenever a breach of contract suit is brought between a union and an employer, section 301 will be applied. It seems equally likely that other efforts to restrict the types of agreements or types of parties covered by the section will be met with disfavor. Unions and employers entering into contracts with each other may be certain that many forums, good law and a strong statute are all available to insure that they perform as provided.

Making the parties perform as promised might be called the keystone of the entire structure. An employer cannot avoid the arbitration which he agreed to use in settlement of his disputes with the union, even if the union breaches the "no-strike" clause of the contract. The union is not free to strike at will, even in the absence of a "no-strike" clause, if it has already agreed to arbitrate its disputes. A union must abide by its contract just as an employer must abide by his. Once the parties agree in advance to the peaceful settlement of their controversies by arbitration, the Supreme Court will not let them back out, regardless of the excuse they present. However, if the parties do not provide arbitration for the settlement of their controversies, the Court will not impose it on them. Thus, as in *Atkinson*, when a contract provides only that employee grievances are to be arbitrated without providing any means by which the employer can process his complaints to arbitration, the normal means of settling contract disputes (the courts) will be made available to the employer.

As the dissenting opinions in some of the cases show, this is sometimes considered to be strong medicine. But every public policy pronouncement in the field of labor relations for the last thirty years, whether by Congress or the President of the United States or the Supreme Court,

has emphasized that the peaceful settlement of labor disputes, especially settlement by arbitration, is vital to the welfare of our nation and to be preferred over “economic warfare.” If it is strong medicine, it is being used to improve the health of the nation’s economy. If the parties don’t like the taste of it, they needn’t put the prescription into their contracts. But the only way in which the courts can serve the public policy thus announced is to see to it that parties who agree to arbitrate, do so. About this there can be no legitimate complaint.

However, having thus extolled the virtues of arbitration in resolving labor disputes, having outlined a broad area within which section 301 would be given free rein and having overcome every legal roadblock thrown up by resourceful counsel in trying to reverse the trend, the Supreme Court suddenly announced the first serious obstacle to effective enforcement of the arbitration clause. It denied employers use of the anti-strike injunction.

The shock is genuine. To many it seems incongruous for the Court to insist that parties must obey the arbitration provisions of their collective bargaining agreements, while at the same time depriving them of the most effective instrument for compelling such obedience. Directing a union to arbitrate when it knows that a strike cannot be prohibited invites evasion of the obligation to settle disputes peacefully. In spite of this, the Court’s decision in *Sinclair* should have come as no surprise.

After all, the same result commended itself to the First, Second and Seventh Circuits with only the Tenth Circuit holding to the contrary.89 Twelve different jurists on the three courts of appeals, including such distinguished names as Judge Learned Hand, Judges Clark, Frank, Lumbard, and Magruder, had held that an anti-strike injunction could not be issued consistently with Norris-LaGuardia. Five Justices of the Supreme Court agreed. It can hardly be said, therefore, that the *Sinclair* decision was so outrageous as to upset all properly functioning legal minds.

On the other hand, had Mr. Justice Brennan been able to pick up two more votes for reversal, this too would have come within the area of reasonable expectancy. For the arguments in support of Justice Brennan’s view are substantial and respectable ones.

The majority’s opinion is a traditional analysis, starting with the importance ascribed to the Norris-LaGuardia Act by Congress at its passage, proceeding through a history of congressional reluctance to modify

89 See notes 77 & 78 supra and accompanying text.
that statute, and arriving finally at the failure of Congress to expressly amend it in the respect here under analysis while enacting section 301 of the Taft-Hartley Act. Under such an approach no weight is given to the social and practical effects which the decision may have on the labor relations picture, such considerations being relegated exclusively to Congress.

It is Mr. Justice Brennan’s opinion which is replete with public policy arguments. Here we find the questions about the impact which the decision will have on relations between unions and employers. Here we find also the curious proposition that Norris-LaGuardia and section 301 co-exist peacefully, with the Court deciding in each case whether the nation’s public policy requires one or the other statute to be paramount in that case only.

The dissent argues in terms of policies and purposes, while the majority argues in terms of the legal effects of the congressional enactments. Mr. Justice Brennan shapes his view of the case by examining the social and practical effects which he foresees, while Mr. Justice Black refuses to pursue anything which does not shed light on congressional willingness to amend or repeal Norris-LaGuardia.

This wide difference in approach is underlined by the fact that Mr. Justice Douglas joined Mr. Justice Brennan in dissent. Mr. Justice Douglas is probably the best friend that section 301 has on the Court. He is the author of the six Lincoln Mills and Steelworkers decisions and he was in the majority in all of the 1962 cases except Sinclair.90 He has insisted that labor arbitration is to be encouraged by the courts, that the parties are to be held to their arbitration bargain, and that the Lincoln Mills interpretation of section 301 embodies the most desirable kind of public policy because it substitutes peaceful settlement of disputes for “economic warfare.” Because he has been hostile to every effort which would weaken the effectiveness of section 301, he has been frequently and severely criticized by those who do not favor the broad scope he has imparted to it. Finding Mr. Justice Douglas on the side of the dissent in Sinclair, therefore, suggests that he thinks the case is a backward step on the road taken by the Supreme Court since Lincoln Mills. Certainly Mr. Justice Brennan thinks so.

Now that the federal courts are definitely out of the injunction picture,

90 That Mr. Justice Black holds a more restricted view of § 301 than does Mr. Justice Douglas is shown by his majority opinion in Sinclair, in which Mr. Justice Douglas dissented, and Mr. Justice Black’s dissent in Lucas Flour, in which Mr. Justice Douglas was in the majority.
the most troublesome question seems to be whether a state court remains free, while applying section 301, to issue an injunction which could not be issued by a federal court because of *Sinclair*.

The argument has been made that Norris-LaGuardia expresses a facet of the national labor policy which has been imposed on both federal and state courts by section 301. Just as a state court may not refuse to order labor arbitration when a federal court would do so, because this would violate national labor policy, it is argued that a state court may not issue an anti-strike injunction when the federal courts would be forbidden to do so, because this would likewise violate national labor policy.\(^{91}\) Acceptance of this contention would mean that no court in the United States could enjoin a strike while enforcing section 301.

However, the argument does not seem persuasive. Norris-LaGuardia has never been considered anything but a withdrawal from the federal courts of a portion of their equity powers. Its language,\(^{92}\) its legislative history, the abuses at which it was aimed and thirty years of judicial application all support this theory. While the act undoubtedly forms part of our national labor policy, it does so only to the extent of prohibiting *federal* courts from issuing injunctions in labor disputes. To rule otherwise, would deprive employers of state remedies which had been available to them before passage of section 301 and would frustrate its purpose, which was to increase, not decrease, the remedies available for breach of a collective bargaining agreement.

Refusal by the Supreme Court to apply the Norris-LaGuardia Act to state courts would continue to make anti-strike injunctions available, but only in those states where the courts are free to grant them. In those jurisdictions where a similar statute prohibits their issuance, the remedies would be the same as those available in the federal courts. Of course, an employer who is satisfied with a judgment for damages or an order to arbitrate can still obtain these in either the federal or state courts.

Mr. Justice Brennan's criticism of this result is that denying federal injunctions while permitting state injunctions will destroy the uniformity of decision which he deems desirable when applying section 301. Yet his fears may not be well-founded. As Mr. Justice Stewart pointed out in the *Dowd Box* case:

> It is implicit in the choice Congress made that "diversities and conflicts" may

\(^{91}\) See Isaacson, supra note 86, at 919.

occur, no less among the courts of the eleven federal circuits, than among the courts of the several States, as there evolves in this field of labor-management relations that body of federal common law of which Lincoln Mills spoke. But this not necessarily unhealthy prospect is no more than the usual consequence of the historic acceptance of concurrent state and federal jurisdiction over cases arising under federal law. To resolve and accommodate such diversities and conflicts is one of the traditional functions of this Court.93

Nor is there anything peculiar about a federally-created right or remedy being available only in a state court. We are once again indebted to Mr. Justice Stewart's Dowd Box opinion for pointing out that a civil action based on the Constitution, a federal statute or treaty, may be brought only in a state court unless the amount in controversy exceeds $10,000 or Congress has expressly removed the jurisdictional amount.94

There seem to be good reasons, therefore, to persuade the Supreme Court to uphold the power of the states to enjoin strikes in violation of a collective bargaining agreement and thus to sweeten the bitter taste left in some mouths by Sinclair.95

CONCLUSION

Accepting Sinclair as a sign that section 301 is vulnerable and that the Court is open to arguments which would impose limitations upon it, we must nevertheless fit the case into its proper context. It has not opened any floodgates. Since Lincoln Mills, in 1957, the Court has consistently encouraged resort to arbitration and 1962 did not see a reversal of that trend. The Norris-LaGuardia Act still has tremendous emotional appeal and Sinclair has left it intact, while reminding us that other useful remedies are available to substitute for the anti-strike injunction. Perhaps an order to arbitrate or a judgment for money damages is not as effective, but it certainly retains some coercive powers. As the other 1962 cases showed, arbitration is still high on the Supreme Court's scale of values, and it would be a mistake to look upon Sinclair as an abandonment of that principle.

94 Id. at 508 n.4.
95 Of course, many questions remain as to the full effect of the Court's decision in Sinclair. See Summers, Role of Supreme Court in Labor Relations, 50 L.R.R.M. 94, 101-02 (1962). Professor Summers asks whether a federal court may specifically enforce an arbitration award which directs a union to end a strike in violation of its contract. See also Meyer, Enforcement of Arbitrator's Labor Injunctions in the Federal Courts, 7 How. L.J. 17 (1961). Professor Summers also asks whether a union may be found in contempt for striking in the face of a court order to arbitrate or a court's confirmation of an arbitrator's award. Such questions are not answered by Sinclair, but we may expect their arrival on the Supreme Court's docket in due course. See also Isaacson, supra note 86.
NOTES

FEDERAL PRE-TRIAL PRACTICE: A STUDY OF MODIFICATION AND SANCTIONS

Introduction

The adoption of the Federal Rules of Civil Procedure was in part a recognition of the fact that the admitted advantages of the common law adversary system were attended by grave defects. Conspicuous among the latter was the frequency with which the litigant with the better case on the merits failed to prevail because of surprise at the trial; even more prominent, perhaps, were the nonsuits following upon even slight variations from the pleadings. The pre-trial process set up by Federal Rule 16 was to eradicate these defects by displacing the pleadings from the dominant position they had occupied in common law pleading. By delaying formulation of the issues until a pre-trial conference, held after the pleadings had been entered and after the parties had presumably become thoroughly familiar with all aspects of the case through the deposition-discovery process, the framers of the Rules sought to eliminate surprise at trial, as well as the needless nonsuits of the common law, and to abolish forever the sporting theory of justice from the federal courts.

Such, in any event, was the theory. However, pre-trial was rather slow in developing in many respects; and only in the last few years has it become possible to determine just how far this theory has become a reality. For only recently have the courts, in their opinions and decisions, begun to reveal a tendency toward viewing pre-trial as a stage of the legal process having a more or less definite place in an integrated system.

This development in the judicial attitude toward the pre-trial process is best manifested in two areas: modification of the pre-trial order under Rule 16, and the creation of sanctions to enforce the basic rules of pre-trial practice. In each, the function of pre-trial as a device to preserve the advantages of the common law system while avoiding its defects clearly appears. Thus, in regard to modification, the central problem is to do away with the rigid formalism of the pleadings while preserving the specificity needed to prevent chaos at trial. And in the area of sanctions, the cases show a continuing effort on the part of the courts to find sanctions which will insure the adherence of the parties to the practical requirements of pre-trial practice, but which will avoid the tendency of the common law to punish a litigant for his counsel's...
negligences and oversights by depriving him of his right to be heard on the merits.

It is in these two closely interwoven areas that one can best detect the constant evolution of the pre-trial process as a vital part of the federal system of litigation. For these reasons, this note will concentrate on these two problematic areas in an effort to explicate some of the nascent concepts of federal pre-trial practice.

**Modification of the Pre-Trial Order**

Rule 16 of the Federal Rules of Civil Procedure\(^1\) specifically states that the pre-trial order, once entered, "controls the subsequent course of the action, unless modified at the trial to prevent manifest injustice." However, it is readily apparent that in the concrete circumstances of individual cases, the "manifest injustice" test is at best a nebulous criterion. Like the term "due process," "manifest injustice" is incapable of precise definition and can be given meaning only on a case-by-case basis. This is best illustrated by the fact that in the twenty-five years since the adoption of the Federal Rules, virtually the only effort to give any real normative value to the "manifest injustice" criterion remains that of Judge Holtzoff in *McCarthy v. Lerner Stores Corp.*,\(^2\) when he stated:

If counsel waits until the trial, he is bound by the pretrial order, unless the trial court relieves him of the pretrial order to prevent manifest injustice. Of course, it is contemplated that this will be done only in exceptional cases, as otherwise the adverse party may be taken by surprise and in a proper case may become entitled to a continuance and possibly a mistrial, if the case is tried before a jury.\(^3\)

Other courts have made almost no attempt to assign any settled meaning to the term—and, indeed, it is doubtful whether such an approach would be feasible or even possible. The tendency seems rather to be to emphasize certain factors which, in the particular factual situations of individual cases, have struck the courts as amounting to "manifest injustice."

Even this more cautious approach, however, has generated no little confusion; for there are some factors of seeming importance which the

---

\(^1\) Fed. R. Civ. P. 16 provides in pertinent part as follows:

The court shall make an order which recites the action taken at the [pre-trial] conference, the amendments allowed to the pleadings, and the agreements made by the parties as to any of the matters considered, and which limits the issues for trial to those not disposed of by admissions or agreements of counsel; and such order when entered controls the subsequent course of the action, unless modified at the trial to prevent manifest injustice.


\(^3\) Id. at 31.
courts have apparently afforded scant weight as regards the question of modification. Thus, although the "manifest injustice" criterion would seem, by the express words of Rule 16, to become applicable only "at the trial," the courts have generally assumed that Rule 16 applies as soon as the pre-trial order is entered. 4 Again, since stress has often been laid on the peculiar value of the pre-trial conference as a vehicle for securing time-saving stipulations, 5 it might be thought that modification would be granted more freely with regard to stipulations than with regard to such things as lists of witnesses, in the interest of making the parties more amenable to entering into such stipulations at pre-trial. However, this consideration has found small favor with the courts, 6 and the nature of the modification sought apparently has little bearing on whether such modification will be granted. 7

Nevertheless, it is believed that the factors which influence the courts in their determination of whether modification of the pre-trial order should be allowed can be divided generally into two broad categories: (1) the courts' attitudes toward the pre-trial process, their view of its nature and the place it occupies in the system of federal procedure; and (2) the conduct of the parties at trial. However, even in making this distinction


It is only in rare instances that amendments are permitted after the case is certified from the pre-trial calendar to the ready-for-trial calendar. . . . [T]he judges let it be understood generally that the pre-trial session is the time at which amendments should be made and the trial judges adhere to a reasonably rigid rule concerning amendments after the case has left the pre-trial calendar.


it must be pointed out that any attempt to isolate these factors runs the risk of being to some extent misleading—that is, it must not be thought that any single factor is necessarily decisive. For what does or does not strike a court as "manifest injustice" must depend, in the last analysis, upon the circumstances of the particular case, and the court which has stressed one factor in allowing or denying modification in one case may stress a completely different factor in allowing or denying it in another.

CONSIDERATIONS OF POLICY

The Relationship Between the Pre-Trial Order and the Pleadings

In discussing the possible policy considerations which govern the courts' attitudes toward amendment of the pre-trial order, the initial question which arises concerns the particular relationship to be attributed to the pre-trial order and the pleadings. In the period immediately following adoption of the Federal Rules, the view was expressed that it was not the intention of the framers of Rule 16 that the pre-trial order should supplant the pleadings. This view, if accepted, has important ramifications in relation to the problem of modification of the pre-trial order: for if the converse position is taken—that the validity of the pleadings ceases once the pre-trial order has been entered—then seemingly Rule 15, dealing with amendment of the pleadings, is no longer to be considered in determining whether or not to allow the modification. It would follow that the liberal amendment policies of Rule 15 have little or no application to modification of the pre-trial order, which must be controlled exclusively by the stricter "manifest injustice" test of Rule 16.

The first question concerning the practical effect of this relationship arises when the court is faced at trial with the problem of whether or not to direct a modification of the pre-trial order, that is, in those situations when an express motion to amend the pre-trial order is made, or when the evidence sought to be introduced is objected to on the ground that it deviates from the pre-trial order. Rule 15(a) provides in sub-

---

8 See Commentary, The Pre-Trial Order, 4 Fed. Rules Serv. 16.3, at 906 (1941). Rule 16 also states that one of the matters to be considered at the pre-trial conference is "the necessity or desirability of amendments to the pleadings" thereby suggesting that the importance of the pleadings does not cease with the entry of the pre-trial order.


10 In this latter situation, the question may also arise concerning the relationship between Rule 16 and the "amendment to meet objections" provision of Rule 15(b). This problem arises most frequently where it is asserted that by failing to seek a continuance the party
stance that leave to amend the pleadings "shall be freely granted when justice so requires"; and it might, perhaps, be argued that a similarly liberal standard should be applied with regard to express modification of the pre-trial order.

Admittedly, it is somewhat difficult to justify this approach in the face of the wording of the rules; for the "manifest injustice" language of Rule 16 seems to completely exclude the "when justice so requires" criterion of Rule 15(a). However, at least one court has adopted the view that, when the problem of express modification of the pre-trial order arises, Rule 16 is to be applied in the "spirit" of Rule 15(a);\(^\text{12}\) and another court in a similar situation has gone so far as to virtually ignore Rule 16 and to apply Rule 15(a) in its stead.\(^\text{13}\)

Although it would thus seem that the relationship between Rules 16 and 15(a) has had considerable influence upon the courts in their determination of whether to direct a modification of the pre-trial order, the full practical effect of this approach is, nevertheless, somewhat uncertain. The explanation of this uncertainty might be that while many courts may in fact apply the liberal approach of Rule 15(a) to situations involving express modification of the pre-trial order, they generally neglect to verbalize their conception of the relationship between Rules 16 and 15(a) and proceed, as it were, under the guise of Rule 16 alone.\(^\text{14}\)

In any event, the practical effect of the courts' views of the relationship between the pre-trial order and pleadings becomes more apparent when there arises the problem of whether the pre-trial order may be \textit{implies} \textit{ly} modified to conform to evidence introduced at trial without objection. Under Rules 15(b)\(^\text{15}\) and 54(c),\(^\text{16}\) if evidence entitled one of the pleadings is waived his right to claim surprise and consequently may not argue that modification of the pre-trial order was erroneously permitted. See note 60 infra.

\(^\text{11}\) Fed. R. Civ. P. 15(a) provides in pertinent part as follows:
A party may amend his pleading once as a matter of course at any time before a responsive pleading is served or, if that pleading is one to which no responsive pleading is permitted and the action has not been placed upon the trial calendar, he may so amend it at any time within 20 days after it is served. Otherwise a party may amend his pleadings only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires.

\(^\text{12}\) Maryland Cas. Co. v. Rickenbaker, 146 F.2d 751, 753 (4th Cir. 1944); cf. Smith Contracting Corp. v. Trojan Constr. Co., 192 F.2d 234, 236 (10th Cir. 1951).

\(^\text{13}\) McDowell v. Orr Felt & Blanket Co., 146 F.2d 136 (6th Cir. 1944).


\(^\text{15}\) Fed. R. Civ. P. 15(b) provides in part:
When issues not raised by the pleadings are tried by express or implied consent of the
the parties to relief is introduced without objection, that relief should be granted even though the evidence is outside the issues raised by the pleadings. Although no motion to amend the pleadings is made, the pleadings are regarded as impliedly amended to conform to the evidence.

In spite of this, in cases where a pre-trial order has been entered, some courts, adopting the view that the pre-trial order supplants the pleadings, have refused to permit the implied modification of the pre-trial order to conform to the evidence, even when that evidence is introduced without objection. Their rationale seems to be that since Rule 16, unlike Rule 15(b), says nothing about implied amendment or modification, there can be no modification of the pre-trial order unless a specific motion to this effect is made. Exemplifying this point of view, the Supreme Court of New Jersey, in interpreting a state procedural rule virtually identical to Federal Rule 16, has stated: “Modification may be had at the trial to prevent manifest injustice, but the modification should be by direction and not by indirection.” And in McCarthy v. Lerner Stores Corp., Judge Holtzoff expressed the view of certain federal courts, stating: “It is the Court’s view that if counsel desires to inject an issue not raised at pretrial, application should be made to amend the pretrial order and to

parties, they shall be treated in all respects as if they had been raised in the pleadings. Such amendment of the pleadings as may be necessary to cause them to conform to the evidence or to raise these issues may be made upon motion of any party at any time, even after judgment; but failure so to amend does not affect the result on the trial of these issues.

Fed. R. Civ. P. 54(c) provides in pertinent part: “Except as to a party against whom a judgment is entered by default, every final judgment shall grant the relief to which the party in whose favor it is rendered is entitled, even if the party has not demanded such relief in his pleadings.”

In Ringling Bros.-Barlum & Bailey Combined Shows v. Olvera, 119 F.2d 584 (9th Cir. 1951), the pre-trial order contained a stipulation that the contract underlying the action had been made in Florida. In affirming a judgment for the plaintiff, the court of appeals noted: “At the trial there was evidence from which it could be inferred that the contract was executed in Texas, but the order was not modified and we hold the stipulation is binding.” Id. at 586. Contra, Mayfield v. First Nat’l Bank, 137 F.2d 1013 (6th Cir. 1943).

See, e.g., McCarthy v. Lerner Stores Corp., 9 F.R.D. 31 (D.D.C. 1949). But see Rosden v. Leuthold, 107 U.S. App. D.C. 89, 274 F.2d 747 (1960). This rationale, while seemingly implicit in the cases, has rarely been verbalized, the courts usually contenting themselves with the bare statement that a motion is needed before the pre-trial order may be amended. A typical statement is that of Mr. Justice Reed, dissenting in Johnson v. Geffen, 111 U.S. App. D.C. 1, 6, 294 F.2d 197, 202 (1960), where he stated, “a failure to object to evidence surely does not enlarge the scope of the pretrial order when no motion to amend or enlarge is made.”

include that issue in the pretrial order." Thus, under this view it is unnecessary to apply the "manifest injustice" test at all unless and until an express motion to amend the pre-trial order is made.

In opposition to this construction of Rule 16 is the position of those courts which consider the pre-trial order as not supplanting the pleadings, but rather as restating them in a combined and more definite form. Under this interpretation these courts have construed the criterion of Rule 16 not independently from but rather in the light of the standards and policies enumerated in Rule 15(b). Hence, these courts continue to apply the liberal amendment criteria of Rule 15(b) to modification of the pre-trial order.21

Thus, in Bucky v. Sebo,22 when a trial court had decided a patent infringement case on the basis of infringement-estoppel and unfair competition, although neither of these issues was contained in the pre-trial order, the court of appeals saw nothing objectionable in such action. It stated:

Since the pre-trial order was not expressly "modified at the trial," pursuant to Rule 16, it is arguable that neither of those issues was open. But as plaintiffs' counsel during the trial made at least a brief reference to the issue of estoppel re infringement, and as defendants' counsel did not then object or ask [for] an adjournment, we think that the trial judge was at liberty to consider that issue, for we read Rule 16 in the light of Rule 15(b) . . .23

The Bucky court did not go on to make clear whether it was merely reading Rule 16 in the light of Rule 15(b) such that retroactive amendment will be allowed if "manifest injustice" so requires, or whether it was really incorporating the language of Rule 15(b) into Rule 16, thereby making implied modification of the pre-trial order mandatory in such situations. However, the latter interpretation would seem to be the more plausible. For while this position might seem somewhat at variance with the Bucky court's use of the phrase "in the light of," it is the one favored by the courts, whether they explicitly apply the implied amendment provi-

---


22 Supra note 21.

23 Id. at 305. (Emphasis added.)
sions of Rule 15(b) or reach the same result without expressing their reliance on this rule. Further it will be noted that this approach is not subject to the objection raised to a similar incorporation of Rule 15(a) into Rule 16; for there is nothing in the "manifest injustice" language of Rule 16 which would bar application of the retroactive amendment provisions of Rule 15(b) to modification of the pre-trial order.

Supporting the above interpretation some courts appear quite clearly to hold that Rule 15(b) applies whenever evidence which is outside of the pre-trial order is introduced at trial without objection. Admittedly, one court, in a similar situation, seemed to require an additional showing that the introduction of such evidence had not resulted in surprise to the opposing party, thereby possibly effecting a combination of the implied amendment provisions of Rule 15(b) with the "manifest injustice" test of Rule 16. However, in so suggesting, the same court also held that lack of surprise was more or less conclusively shown by a failure to object to the evidence in question when it was introduced at trial. Thus, in an indirect fashion, it arrived at the same result reached by those courts which directly apply the implied amendment language of Rule 15(b).

In the final analysis it is of course unimportant what rationale is adopted. What is important is the avoidance of a strict and literal interpretation of Rule 16 which might lead to a result not in conformity with the facts of the case as disclosed at trial; for it seems axiomatic to say that a party should not lightly be deprived of his right to have his case decided on the merits because of the error of his counsel at pre-trial, particularly in situations where those errors may be readily corrected on trial without prejudice to either party or substantial inconvenience to the court.

Moreover, liberal standards for allowing implied modification are seemingly contemplated by the Federal Rules themselves. If the plead-

25 See Mayfield v. First Nat'l Bank, 137 F.2d 1013, 1016-17 (6th Cir. 1943); Harris v. Harris, 90 U.S. App. D.C. 239, 196 F.2d 46 (1942).
28 Id. at 92, 274 F.2d at 750.
29 Of course, there can be no implied modification where the evidence introduced bears on issues concededly within the scope of the pre-trial order, as well as on issues allegedly outside of it, for in such a situation failure to object does not indicate tacit consent to trial of the new issues. See First Fed. Sav. & Loan Ass'n v. United States, 295 F.2d 481, 482 (9th Cir. 1961).
ings may be subsequently amended to conform to the evidence and the pre-trial order may not be, the result would be that the liberal amendment policies of Rule 15(b) would be of practical value only in those cases in which there is no pre-trial order.30 A similar result would logically follow with regard to Rule 54(c)—in spite of the fact that there is absolutely nothing in the language of that rule to indicate that it was to apply only in those cases where there was no pre-trial order. The result of the strict modification position would be that in the interest of securing the manifest benefits of pre-trial, the liberal amendment policies of Rules 15(b) and 54(c) would be relegated to a purely ancillary place in the process of federal litigation. Such, it seems, could not have been the intention of the framers of the Federal Rules.

Construction of the Pre-Trial Order

The differences in basic policy considerations which divide the courts on the question of implied modification are perhaps even more clearly illustrated in those cases dealing with construction of the pre-trial order. The main issue in these cases is whether the pre-trial order should be given a "liberal" as opposed to a "strict" construction in determining whether or not a certain issue not specifically set forth in the order is included within its general scope—a problem which in turn raises the question of precisely how much specificity should be demanded of the parties in their pre-trial statements. It is possible to frame a pre-trial statement or stipulation which, though stated in terms specific enough to at least suggest a definite issue, is sufficiently general so that the issue is not squarely presented. If this issue is then asserted at trial, the question becomes one of construction as to whether it is contained in the generalities of the pre-trial order or whether modification under Rule 16 is necessary.

In support of a liberal amendment policy towards the construction of the order as well as towards its implied modification, resort might be had to the familiar argument that the Federal Rules envision "notice pleading"; that is, the pleadings serve to inform the respective parties of the nature of the action and the defenses to be raised only in the most general way.31 However, this theory also presupposes that by means of discovery and the pre-trial processes each party will become familiar with the particularities of the other's case and the rationale upon which it rests,

31 See, e.g., Dioguardi v. Durning, 139 F.2d 774 (2d Cir. 1944).
and the issues will then be simplified for the purposes of trial. A necessary corollary of this theory would seem to require that counsel present their case with specificity at pre-trial, and that the pre-trial order set forth the issues to be tried in reasonably precise terms. This would then lead to the conclusion that where a party seeks over objection to inject at trial an issue not clearly raised at pre-trial, either the pre-trial order should be modified or the issue should be barred.

Giving effect to this view, some courts do require that, absent modification, an issue be rather clearly presented by the pre-trial order before it may be raised at trial. One leading case in this regard is *Walker v. West Coast Fast Freight, Inc.*, wherein plaintiff attempted unsuccessfully to assert damages at trial for difficulties in childbirth allegedly caused by the accident being litigated. Plaintiff there argued on appeal that since her pre-trial statement alleged injuries which included "a severe tearing, twisting, and warranting of the tendons, muscles, ligaments, bones, nerves, and soft tissue of her . . . pelvic area, right hip, and leg," and inasmuch as defendant's counsel had subsequently discovered that plaintiff was pregnant, defendant should have anticipated that plaintiff would suffer some difficulty in childbearing and claim damages therefor.

However, the court of appeals held that this issue was not presented by the pre-trial order and hence could not be raised at trial unless a motion for modification were made. Although the court recognized that defendant's counsel "might well have concluded that it was more probable than not" that plaintiff would experience difficulties in childbirth for which she would seek damages, it ruled that this was not enough, stating:

> [T]his would have placed upon him the burden of preparing for a contention which might never arise and which would not be hard to overlook. It seems inconsistent with the purpose of clarification and simplification of issues to place upon a party the burden of connecting subsequently-discovered facts with allegations buried in the pre-trial order and acting upon consequences which might come about.

---

32 In *Metropolis Bending Co. v. Brandwen*, 8 F.R.D. 296, 297 (M.D. Pa. 1948), the court stated:

> To the pleadings is assigned the task of general notice giving, whereas narrowing and clarifying the basic issues between the parties, ascertaining the facts or information as to the existence or whereabouts of facts relative to those issues is the role of the deposition-discovery process aided by the pre-trial hearing.


33 See, e.g., *Miller v. Brazel*, 300 F.2d 283, 287 (10th Cir. 1962).

34 233 F.2d 939 (9th Cir. 1956).

35 Id. at 941. (All italicized in original.)

36 Id. at 942.

37 Ibid.
In contrast with this view there are other cases indicating a propensity on the part of some courts to give the pre-trial order a more liberal reading by concluding that an issue allegedly raised for the first time at trial was impliedly contained in or necessarily suggested by the pre-trial order, thereby completely avoiding the thorny problem of modification. Thus, in Conlon v. Tennant, the plaintiff was able to successfully assert on appeal that the trial court had erred in refusing to instruct on the issue of last clear chance merely because this issue was never raised until plaintiff requested such an instruction at the close of trial. In reversing, the appellate court held that the assertion in plaintiff's pre-trial statement that the defendant was negligent in circumstances where he “knew or should have known that the female plaintiff was oblivious to the impending danger” raised the issue of last clear chance with sufficient clarity so that the defendant should have been prepared to meet it at trial.

Perhaps, the extreme instance of the tendency of some courts to avoid the whole question of modification in this manner was seen in Johnson v. Geffen, where the court of appeals in reversing a directed verdict for the defendant again obviated all necessity of considering the question of modification, by holding that an issue not specifically set out in the pre-trial order was nevertheless fairly presented therein. In doing so it went on to announce as a general rule of construction that “upon motion for a directed verdict the plaintiff's pre-trial statement should be read in the light most favorable to him.”

It will be noted that the Johnson and Conlon decisions stand midway between the two basic positions previously noted—the one requiring an express motion to modify the pre-trial order, and the other permitting implied modification by utilizing the liberal amendment policies of Rule 15(b). Clearly no objection can be made to the refusal of Johnson and Conlon to hold the parties strictly to the terms of the pre-trial order merely because no attempt was made to modify the order at trial. But what is objectionable in these cases is the rationale upon which the decisions rest

39 Id. at 142, 289 F.2d at 883.
41 Id. at 3, 294 F.2d at 200. This view seems to equate interpretation of the pre-trial statement with interpretation of the evidence. It is suggested that the better position is that of Mr. Justice Reed in dissent: “The question is of law, of the correct, not the most favorable, interpretation of a document prepared by counsel in the course of litigation, and approved by the court.” Id. at 6, 294 F.2d at 202.
the principle that whenever the pre-trial order can be read as impliedly containing an issue, all question of modification with regard to that issue becomes moot. For while there is strong support for applying the liberal amendment policies of Rule 15(b) to modification under Rule 16, there is considerably less support for an equally liberal construction of the pre-trial order in order to avoid all need for modification. Indeed, such decisions can only tend to weaken the binding force of the pre-trial order by not requiring of it the specificity needed to provide a clear guide for the parties and the court at trial.

In evaluating the relative merits of the positions espoused by the Walker and Johnson courts it would appear that the Johnson and Conlon decisions ignore the fact that, while the Federal Rules endorse notice pleading, they do not envision “notice pre-trial.” There can be no doubt that the very nature of the pleadings under the Federal Rules requires that the issues be framed with some clarity in the pre-trial order if chaos is not to ensue at trial.\(^{42}\) Indeed, one court has gone so far as to vacate a judgment on the ground that the pre-trial order did not present the issues to be tried with sufficient precision.\(^{43}\) There must come a time, in the process of federal litigation, when specificity is required—when the issues are crystallized and squarely presented for trial. If such specificity is not attained at the pre-trial conference, one may wonder when and if ever it is to be achieved. The answer of Johnson and Conlon—the only remaining alternative—is that the courts must “wait until the trial is in progress before . . . [they] can ascertain what particular facts are in issue and what legal theories are relied upon by the parties.”\(^{44}\)

\textit{Conflict in Philosophies of Pre-Trial}

Before one can justifiably conclude that there is an irreconcilable split of opinion in this regard among the federal courts, it must also be borne


\(^{43}\) Plastino v. Mills, 236 F.2d 32 (9th Cir. 1956). Noting that the pre-trial order contained the words, “and the pleadings now pass out of the case,” the court observed that “the pleadings might pass out here unmourned, but the trouble is that the pre-trial order is so badly drawn that it would have been far better to have proceeded to trial on the pleadings.” Id. at 33-34. See also Calvin v. West Coast Power Co., 5 Fed. Rules Serv. 16.33, Case 1 (D. Ore. Nov. 24, 1941).

\(^{44}\) Padovani v. Bruchhausen, 293 F.2d 546, 552 (2d Cir. 1961) (separate opinion).
in mind that judicial policy toward modification of the pre-trial order is not governed solely by the courts' various views on the relationship between the pre-trial order and the pleadings and the theoretical desirability of reading Rule 16 in the light of the liberal policies of Rule 15. Another factor of equal, and perhaps greater, importance which must be borne in mind is the more practical consideration which might be termed the courts' "philosophy of pre-trial," i.e., their concept as to how best to practically utilize pre-trial procedure to achieve what they variously conceive to be its purpose. Thus, some courts are prone to permit amendment of the pre-trial order because they feel that unless such modification is rather freely permitted, counsel will be unwilling to enter into pre-trial agreements and hence needless litigation, unnecessary complexity, expense, and loss of time will result.

Illustrative of this view is Smith Contracting Corp. v. Trojan Constr. Co.46 There, the trial court refused to permit the defendant's modification of the pre-trial order to assert a counterclaim on the ground that the counterclaim would raise issues of fact not presented by the order. The Court of Appeals for the Tenth Circuit reversed, reasoning that requiring a "rigid adherence" to pre-trial conference agreements would tend to discourage cooperation of counsel and impair their "willingness to agree at the pretrial conference as to the real and substantial issues to be presented."47 Such a result, hinted the court of appeals, would emasculate pre-trial procedure.

However, a diametrically opposed approach was enunciated by the Court of Appeals for the Third Circuit in Payne v. S.S. Nabob,47 a personal injury admiralty action. In his opening statement at trial, libellant raised the issue of improper loading of the vessel involved. The trial court sustained an objection to this as outside of the scope of the pre-trial order, since libellant's pre-trial memorandum, incorporated therein, had stated that he was relying solely upon the faulty condition of a winch to prove his cause of action.

In affirming, the court of appeals rejected libellant's contention that the trial court had abused its discretion. While referring obliquely to surprise and the delay between the entry of the pre-trial order and the trial,48 the appellate court based its decision on the necessity of enforcing

45 192 F.2d 234 (10th Cir. 1951).
46 Id. at 236. See Laird v. Air Carrier Engine Serv., Inc., 263 F.2d 948, 954 (5th Cir. 1959).
47 302 F.2d 803 (3d Cir. 1962).
48 Five and a half months had elapsed between entry of the pre-trial order and the trial, during which time libellant had made no attempt to modify the pre-trial order. Id. at 807.
pre-trial procedure "very strictly" in order to insure that such procedure should continue to function properly.\textsuperscript{49} The court emphasized the fact that pre-trial procedure had become a vital element of litigation and a routine part of judicial procedure in the Eastern District of Pennsylvania, which had given enormous relief to a badly clogged trial list. For the trial court to have permitted amendment of the pre-trial order or for it to have granted a continuance, felt the Third Circuit, would have amounted to "repudiating the whole pre-trial theory and system as understood and followed in the Eastern District."\textsuperscript{50}

At first glance, in comparing these two results it might seem that the position of the Tenth Circuit is something of an anomaly in that it holds amendment of the pre-trial order should be freely permitted so as to encourage pre-trial agreements which are not to be binding upon the parties. However, it must be noted that the value which is stressed—the need for encouraging a willingness to stipulate on the part of counsel or the need for rigid enforcement of the pre-trial procedures—will logically depend largely on the state of pre-trial procedure in the jurisdiction in question.\textsuperscript{51} That is, in the Eastern District of Pennsylvania pre-trial is, said the Third Circuit in \textit{Payne}, "routine"—a "vital element of litigation."\textsuperscript{52} Under such circumstances, where pre-trial procedure has crystallized and become an intrinsic element of the judicial process, a more or less rigid adherence to its rules is more likely. Where, however, pre-trial practice is in a rather inchoate state, its acceptance is facilitated by a more liberal attitude on the part of the courts towards modification of the pre-trial order. While such considerations might appear too mundane to influence judicial interpretation, such factors cannot be ignored in any attempt to reconcile what seems to be an irreconcilable conflict among the federal courts.


\textsuperscript{50} 302 F.2d at 807.

\textsuperscript{51} In King v. Edward Hines Lumber Co., 68 F. Supp. 1019 (D. Ore. 1946), the court stated: "No matter what the circumstances were the fact admitted of record binds the parties . . . . No matter what the legal rights of the client were, the attorney in a civil case can destroy them all by admissions made in the record." Id. at 1012. It will be noted that Oregon, like the Eastern District of Pennsylvania, is a jurisdiction in which pre-trial is rather well-established. See Montgomery Ward & Co. v. Northern Pac. Terminal Co., 17 F.R.D. 52 (D. Ore. 1954) (action against 57 common carriers wherein the pre-trial order covered 1420 pages).

\textsuperscript{52} 302 F.2d at 807.
FACTUAL CONSIDERATIONS

Besides the question of the relationship between Rules 15 and 16 and the problem of construing the pre-trial order, it remains to determine just what circumstances will persuade a court to find "manifest injustice" in a particular case. The necessity for this inquiry will arise out of one of two situations: (1) where a party, over objection, seeks to introduce evidence obviously outside the scope of the pre-trial order; and (2) where after the close of the evidence a party seeks to have the court instruct the jury on an issue which was neither mentioned in the pre-trial order nor clearly raised by the evidence introduced at trial, thus precluding any application of the implied amendment provisions of Rule 15(b).

Of these two situations, it would seem that the former presents the courts with the greater problems; for in many of these cases the modification sought will not only require the presentation of additional evidence on new issues of fact but the undertaking of additional discovery as well, making the dangers of prejudicing one of the parties by allowing or denying the motion considerably greater. Nonetheless, for the most part it seems that the same basic considerations influence the courts regardless of whether the case before them is of the first or second type.

The Effect of Modification upon the Opposing Party

Among the many factual considerations which the courts will weigh in determining whether modification of the pre-trial order is required "to prevent manifest injustice," the two most important are (1) the danger of surprise to the party opposing modification, and (2) the degree of diligence exercised by the party seeking modification both before and after the need for modification arose. Of these two the more important would appear to be the presence or absence of surprise. Frequently it has been asserted that one of the prime purposes of the pre-trial process is to eliminate surprise at trial. Indeed, some cases tend to stress this element to the extent of allowing a party to introduce evidence on an issue outside of those presented by the pre-trial order, merely upon a showing that the opposing party is not surprised thereby.

54 See, e.g., Walker v. West Coast Fast Freight, Inc., 233 F.2d 939, 941 (9th Cir. 1956).
One of the most important elements in an appellate court's determination of whether a party was surprised by the trial court's allowance of a deviation from the pre-trial order is the conduct of that party at the trial. Thus, where he conducted an extensive and searching cross-examination on the evidence introduced below, he may not claim that its introduction resulted in surprise. And counsel could not claim surprise where photographs not referred to by the pre-trial order were nonetheless introduced in evidence, when he later used these photographs to strengthen his own argument to the jury.

Further, some courts seem to make it a requirement that before a party may assert that he was surprised by a modification of the pre-trial order he must have sought a continuance. In those cases the theory is, perhaps, that by failing to request a continuance counsel showed that he was prepared to litigate the issue allegedly outside of the scope of the pre-trial order, and cannot thereafter assert surprise. Applying this reason-

56 Virtually all of the opinions in this area are by appellate courts, thus making it somewhat difficult to say with certainty precisely which factual considerations motivate trial courts in granting or denying modification. This is the more difficult because the "manifest injustice" language of Rule 16 is not mandatory, unlike the retroactive amendment provisions of Rule 15(b), thus enabling appellate courts to dispose of modification cases largely on the ground that the trial court has not abused its discretion in granting or denying modification of the pre-trial order in a given instance. See Globe Cereal Mills v. Scribner, 240 F.2d 330, 335 (10th Cir. 1956); Texas & Pac. Ry. v. Buckles, 232 F.2d 257 (5th Cir. 1956); Cherney v. Holmes, 185 F.2d 718, 722 (7th Cir. 1950); cf. Payne v. S.S. Nabob, 302 F.2d 803, 807 (3d Cir. 1962); Phoenix Mut. Life Ins. Co. v. Flynn, 83 U.S. App. D.C. 381, 382, 171 F.2d 982, 983 (1948).

57 Millers' Nat'l Ins. Co. v. Wichita Flour Mills Co., 257 F.2d 93 (10th Cir. 1958).

58 Cherney v. Holmes, 185 F.2d 718, 722 (7th Cir. 1950).


60 Some courts apparently regard this situation, where evidence is objected to as outside the scope of the pre-trial order, as a proper one for the "amendment to meet objections" provision of Fed. R. Civ. P. 15(b), which reads as follows: If evidence is objected to at the trial on the ground that it is not within the issues made by the pleadings, the court may allow the pleadings to be amended and shall do so freely when the presentation of the merits of the action will be subserved thereby and the objected party fails to satisfy the court that the admission of such evidence would prejudice him in maintaining his action or defense upon the merits. The court may grant a continuance to enable the objecting party to meet such evidence.

See Sens v. Baltimore & O.R.R., 149 F. Supp. 442-43 (W.D. Pa. 1957); Firemen's Ins. Co. v. Show, supra note 59, at 530. Failure to request a continuance has also been viewed as a test of surprise in a pure 15(b) situation, where there was no pre-trial order. See, e.g., Rabenovets v. Crossland, 78 U.S. App. D.C. 54, 137 F.2d 675 (1943). However, assuming that Rule 16 should be read in the light of the above-quoted language of Rule 15(b), this
ing in *Meadow Gold Prods. Co. v. Wright*, the Court of Appeals for the District of Columbia Circuit, in affirming the trial court's modification of the pre-trial order, held that by failing to object to or seek a continuance upon the injection of the issue outside of the scope of the pre-trial order, the appellant had thereby waived any claim of surprise or prejudice which he might otherwise have asserted on appeal.

Notwithstanding the apparent logic of this approach, it would seem that by making failure to request a continuance a more or less decisive test of lack of surprise, these courts are tending toward the imposition of a rigid standard where none can logically be utilized. The difficulty with this view is that by the time of trial, discovery is over; and even assuming that counsel is able to conduct additional discovery in order to meet the new issue, the time which elapses between pre-trial and trial is often considerable—witnesses forget, evidence may no longer be available, and it may be that even with a continuance counsel may be unable to secure the once-available evidence needed to meet the new issue and thus may be prejudiced by its introduction. Therefore, while failure to request a continuance may in a given case indicate lack of surprise, such failure cannot logically be elevated to the status of a hard-and-fast test. Recognizing this, some courts do not require a motion for a continuance where counsel would not be aided by the additional time and the granting of a continuance would be a "paper formality."

The reasoning of the preceding line of cases seems to adopt the view that, all other things being equal, modification of the pre-trial order should be permitted where this will not result in surprise to the adversary, and denied where it would. Some courts have recognized, however, that the mere presence or absence of surprise is not the all-important test and have adopted the position that whether modification should be

would not justify the employment of failure to request a continuance as the test of surprise, for Rule 15(b) clearly indicates that continuance is merely one remedy which the court may utilize to protect the objecting party. Moreover, the amendment-to-meet-objections portion of Rule 15(b) is discretionary, unlike the implied amendment portions of that rule. See Fidelity & Deposit Co. v. Drout, 157 F.2d 912, 913 (2d Cir. 1946). Thus, the better view is that failure to request a continuance is significant only where it is clear that the objecting party did not need the continuance to meet the evidence objected to and for that reason deliberately chose not to request it. See Sens v. Baltimore & O.R.R., supra at 442-43.

64 Laird v. Air Carrier Engine Serv., Inc., 263 F.2d 948, 952 (5th Cir. 1959).
permitted must be governed largely by the ability of the court to impose adequate safeguards for the protection of the opposing party. Thus, in Laird v. Air Carrier Engine Serv., Inc.\(^65\) the court permitted the defendant to repudiate a stipulation when the trial was nearly a third over, on the basis of newly discovered facts. On appeal, the Fifth Circuit did not challenge the trial court's decision to permit modification of the pre-trial order, but nonetheless reversed, stating:

The Court does have the right . . . to relieve counsel of stipulations to prevent manifest injustice. . . . But the Court is responsible for seeing that suitable protective terms or conditions are imposed to prevent substantial and real harm to the adversary. What these terms or conditions might be no one can forecast. In one case it might be a continuance. In others it might be the making of a new stipulation to permit the receipt in evidence of data or material or other statements now relevant and trustworthy, but lacking in some technical admissibility. Whatever form it takes, the protection must be as full as needed to assure that the authorized change does not subject the adversary to insuperable and irretrievable harm.\(^66\)

Similarly, other courts have held or indicated that in a proper case, the party opposing modification may be entitled to an opportunity to consult his witnesses,\(^67\) a continuance or reopening and recall of witnesses at the expense of the surprising litigant,\(^68\) a mistrial,\(^69\) further discovery,\(^70\) or to have his adversary post a bond.\(^71\)

It is apparent that in treating surprise as the determining factor in considering whether or not modification of the pre-trial order should be allowed, the courts are applying a negative test of "manifest injustice" rather than a positive one. In spite of the language of Rule 16, these courts are in effect reading the provision that modification of the pre-trial order shall be permitted to prevent "manifest injustice" to mean that such modification shall be allowed if to allow it would not result in "manifest injustice." This results necessarily in what might be termed a one-sided test of "manifest injustice"—that is, only the effect of allowing the modification upon the party opposing it is considered.

\(^{65}\) Supra note 64.


\(^{67}\) Millers’ Nat’l Ins. Co. v. Wichita Flour Mills Co., 257 F.2d 93, 98 (10th Cir. 1958).


This approach, however, is not necessarily subject to criticism. It amounts to nothing more than reading Rule 16 in the light of the liberal standards set forth in the language of Rule 15. It would seem eminently reasonable that the effect of modification upon the opposing party should be examined with special concern in ascertaining the presence or absence of "manifest injustice." However, it is submitted that some courts have erred in trying to make this determination by the application of rather rigid tests such as failure to seek a continuance. While this approach has the merit of making it possible to apply the "manifest injustice" criterion of Rule 16 with some certainty, it nevertheless ignores the fact that whether modification of the pre-trial order should be permitted must depend, in the last analysis, upon the totality of the facts and circumstances of each individual case and not merely upon the presence of surprise as indicated by a failure to seek a continuance. To be preferred, it is suggested, is the approach which stresses the power of the courts to impose, in each individual case, whatever conditions may be necessary to protect the party opposing modification, rather than the formulation of hard-and-fast tests.

Conduct of the Party Seeking Modification

While the courts have clearly stressed the effect of the proposed modification upon the party opposing it, the cases indicate some confusion as to precisely what weight is to be given the conduct of the party seeking such modification. A strong argument can be made that this factor cannot simply be ignored; for the ideal of the pre-trial conference is, as the court in *McCarthy v. Lerner Stores Corp.* 72 has stated, that "at the pre-trial counsel are [to be] as thoroughly familiar with the case . . . as they will be at the trial." 73 If this ideal is to be achieved, it would seem that when a modification of the pre-trial order is requested the conduct of the party seeking it should be closely scrutinized, to insure that it was not his lack of preparation at pre-trial which made the modification necessary. Further, the very language of Rule 16 supports this view; for the phrase "unless modified . . . to prevent manifest injustice" suggests that the burden should be on the party seeking modification to show affirmatively that manifest injustice would result unless such modification were granted.

The courts apparently feel constrained to pay at least some deference

73 Id. at 31.
to this line of argument; for they have generally indicated that the conduct of the party seeking modification is an important factor to be considered. Their approach seems to be a sort of variation on the "clean hands" doctrine; one seeking modification of the pre-trial order must show that he is equitably entitled to it\textsuperscript{74}—that the need for modification did not arise through any fault of his. Thus, modification cannot be allowed where a party waits until trial is over to attempt to repudiate a stipulation contained in the pre-trial order.\textsuperscript{75} Nor should modification be permitted where a party seeks to completely change the theory of his case after all of the evidence is in, at the time for requesting instructions.\textsuperscript{78}

From a review of the cases, however, it appears that except in rather flagrant cases\textsuperscript{77} such as those mentioned above, the courts in fact treat the conduct of the party seeking modification as among the less important of the factors to be considered under Rule 16. Although the courts often employ language indicating that the conduct of such a party is of vital importance, the language frequently does not mirror the actuality. Thus, in \textit{Meadow Gold Prods. Co. v. Wright},\textsuperscript{78} the Court of Appeals for the District of Columbia Circuit stated: "the courts are not to be lenient with counsel who fail to reveal the theory of their case until all of the evidence is closed."\textsuperscript{79} However, the fact is that the court \textit{has} been lenient with such counsel; thus, even in \textit{Meadow Gold}, by emphasizing waiver of surprise, the court decided that it would have been error to refuse an instruction on last clear chance, even though the trial judge as well as opposing

\textsuperscript{74} This equitable approach is clearly indicated in Wood v. National Farmers Union, 114 F. Supp. 514, 521 (D. Colo. 1953), wherein the court stated: "It is not unfair to hold defendant's counsel to his admissions ... in the pre-trial conference ... for the reason that as the record of the trial ... will show, defendant's counsel ... insisted that plaintiff was bound by his admissions and stipulations in the same conference."


\textsuperscript{76} Miller v. Brazel, 300 F.2d 283 (10th Cir. 1956). One case has held that defendant would not be permitted to admit a point on trial, where the admission should have been made at the pre-trial conference and was not only because defendant's attorney had not then studied his case closely. The court reasoned that to permit the admission would surprise plaintiff by throwing him "out of his stride" in presenting his case. Byers v. Clark & Wilson Lumber Co., 27 F. Supp. 302 (D. Ore. 1939).

\textsuperscript{77} Modification clearly will not be permitted where the court derives the impression that it was the intention of the party neglecting to seek modification to thereby surprise his opponent on trial. Cf. Burton v. Weyerhauser Timber Co., 4 Fed. Rules Serv. 16.32, Case 2 (D. Ore. Feb. 1, 1941).


\textsuperscript{79} Id. at 35, 278 F.2d at 869.
counsel expressed his surprise at the requested instruction. And a similar result was reached in Conlon v. Tennant, by holding that the issue of last clear chance was impliedly contained in the plaintiff's pre-trial statement. Similarly, although it has sometimes been indicated that a long, unexplained delay in seeking modification of the pre-trial order should weigh rather heavily against such modification, the courts have in practice exhibited a willingness to accept rather dubious "explanations" or to ignore the delay entirely in permitting modification even during trial.

This confusion in the cases, it is suggested, results from the fact that while the courts still cling to the ideal enunciated in McCarthy, they are unwilling to enforce it. For with acceptance of the idea that the Federal Rules contemplate liberal modification of the pre-trial order, the fact that counsel has been guilty of some failure to inform himself or to promptly seek a modification is not an adequate reason for needlessly imposing the harsh penalty of refusal of modification. Certainly, this strict approach would be inconsistent with the view of those courts which place the emphasis upon the power of the courts to impose conditions on modification which will adequately protect both parties, rather than upon the application of rigid, somewhat artificial tests.

The basic conflict here is between two considerations, each one significant. On the one hand, by the time of trial the parties have had the benefit of all the federal pre-trial and discovery devices, and there should be no excuse—except in an exceptional case—for delay in seeking modification or for raising new issues or seeking to call new witnesses on trial. But conversely, a party should not be deprived of his cause of action, of his right to a trial on the merits, unless he can only be permitted such a trial at the expense of irretrievably prejudicing his adversary. And, so far as the conduct of the party seeking modification is concerned, the latter consideration apparently far outweighs the former.

But in the last analysis it must be borne in mind that Rule 16 cannot be read in isolation from the other Federal Rules, for together they are the practical guides that delimit a system of litigation. Consequently,

---

83 See, e.g., Cherney v. Holmes, 185 F.2d 718 (7th Cir. 1950).
the courts' attitudes toward the problem of modification of the pre-trial order must necessarily be influenced, at least in part, by the manner in which they regard the system of federal litigation as a whole. Further, while the courts have in fact formed certain varying views as to the nature of the pre-trial order, its relation to the pleadings and its place in the process of litigation, these views have no meaning existing abstractly, but are important only insofar as they influence the decisions of actual cases; and here they must inevitably be tempered or even outweighed by other considerations of a factual nature. In this regard, while the courts have stressed such considerations as surprise and failure to exercise due diligence in seeking modification as factors to be given some weight under Rule 16, this is not to say that situations might not arise in which different considerations, hitherto unemphasized, will greatly influence the decision. For, as emphasized previously, it is only in the particular factual situations of the individual cases that a court can properly weigh all those myriad factors that may go to make up "manifest injustice."

SANCTIONS

While the question of when to allow modification of the pre-trial order relates to the nature of the order and its role in the scheme of pre-trial practice, a corollary problem relates to the very formation of the pre-trial order and presents itself in the question of how to compel the parties in a case to abide by the ground rules of pre-trial procedure. Careless observation of such rules often results in requests for the modification of the pre-trial order and all the problems attendant upon such a request. Thus, if the courts are to prevent unnecessary problems of modification from arising, their more immediate problem is to determine what measures may be taken to insure the cooperation of counsel while the pre-trial procedure is in progress.

Rule 16 provides no sanctions to insure the smooth operation of the pre-trial conference. Yet, it is quite clear that some method of compelling obedience to the requests and demands of the pre-trial judge or examiner is essential if the system is to be effective. This was best exemplified by the failure and abandonment of the compulsory pre-trial conference in Montgomery County, Pennsylvania, which has been mainly attributed to the lack of effective sanctions.\(^{85}\) Recognizing this, the district

courts, in their discretion, have adopted various sanctions to insure cooperation of counsel before the entry of the pre-trial order. Among these, the most common have been the assessment of costs and fees, the entry of preclusion orders, and dismissals or default judgments.

In accordance with the rulemaking power vested in the district courts by Rule 83, many district courts have included in their local rules detailed steps for the administration and enforcement of pre-trial practice. Although there is a notable lack of uniformity in the treatment given by such rules to the question of when the various sanctions may be imposed, the most common disposition of this matter is to charge the application and measure of sanctions to the discretion of the court and the demand of the circumstances. Thus, these rules provide great latitude in specifying the type of misconduct which warrants the exercise of this discretion. A number of courts grant a general license to penalize when there is a failure of counsel to appear at the pre-trial hearing. Other district courts allow the general imposition of sanctions in the case of a failure to stipulate not made in good faith, failure to file a memorandum, failure to participate in or prepare for the pre-trial conference and for refusal to cooperate in the preparation of the pre-trial order.

In addition to these penalties which fall upon the parties, the Eastern District of Pennsylvania also directs that an attorney may be punished as the court shall deem just. In regard to the application of these sanctions, at least four districts specifically provide for an ex parte pre-trial hearing to enter an appropriate order.

The most common and least drastic of the above-mentioned sanctions

---

86 Fed. R. Civ. P. 83 provides:

Each district court by action of a majority of the judges thereof may from time to time make and amend rules governing its practice not inconsistent with these rules. In all cases not provided for by rule, the district courts may regulate their practice in any manner not inconsistent with these rules.

87 In some instances the judge is granted such discretion upon the failure of a party to comply with any pre-trial rule. E.g., W.D. Ark. R. 9(e); S.D. Cal. R. 31; D. Conn. R. 10(g); E.D.N.C. Civ. R. 7P; M.D.N.C.R. 22(p); W.D. Pa. R. 5(II)H.

88 E.g., D. Conn. R. 10(g); D. Md. R. 15(a); D. Mass. R. 11(b); E.D. Wash. R. 8; W.D. Wash. R. 40.

89 D.D.C.R. 12(1).

90 S.D.N.Y. Calendar R. 13(b)(2).

91 D. Del. R. 11B; accord, D. Conn. R. 10(g) (upon failure to participate).

92 E.D. Pa. 12(c); accord, S.D. Cal. R. 31.

93 D. Del. R. 11B (ex parte or otherwise, after notice; upon failure to appear, participate, prepare, or cooperate); M.D.N.C.R. 22(a) (upon failure to appear); W.D. Okla. R. 16(b) (upon failure of either party or counsel to appear); W.D. Pa. R. 5(II)(H) (upon failure to comply with the pre-trial rules).
is the assessment of costs and fees. In *Matheny v. Porter*, a failure to comply with a court order to furnish certain information was suggested to be sufficient to justify the assessment of the costs necessitated by the refusal, and possibly all the costs up to that point. Similarly, the courts have also imposed indirect fines upon successful litigants for variance from the pre-trial order by refusing to impose, as costs, upon the losing party the expense of witnesses and exhibits or illustrations which were outside the scope of the issues approved at pre-trial. These routine costs, however, are relatively mild penalties involving nominal monetary sanctions. For this reason they rarely give rise to significant legal problems.

**PRECLUSION ORDERS**

More difficult problems are presented by the second and more stringent of the sanctions within the power of the district courts, that is, the entry of preclusion orders. Under various local court rules, such orders have been authorized to preclude the use of a defense in whole or in part.

94 Fed. R. Civ. P. 54(d) provides in part: "Except when express provision therefor is made either in a statute of the United States or in these rules, costs shall be allowed as of course to the prevailing party unless the court otherwise directs . . . ." Under the local rules of district courts, such sanctions have been authorized upon failure to prepare for pre-trial hearing, S.D.N.Y. Calendar R. 16 (reasonable costs on attorneys); E.D. Pa. Standing Order (Feb. 8, 1960), appear at such a hearing, e.g., D. Conn. R. 10(g); S.D.N.Y. Calendar R. 16; E.D. Pa. Standing Order (Feb. 8, 1960), participate therein, e.g., D. Conn. R. 10(g); E.D. Pa. Standing Order (Feb. 8, 1960), or comply with a pre-trial rule or order, e.g., S.D. Cal. R. 31; D. Conn. R. 10(g).

95 158 F.2d 478 (10th Cir. 1946).

96 Ibid. (dictum).


98 Walker v. West Coast Fast Freight, Inc., 233 F.2d 939 (9th Cir. 1956). The close relationship between discovery sanctions and pre-trial preclusion orders appears clearly in two areas. First, the entry of the preclusion order as a sanction is substantially similar to the penalties authorized by Federal Rule 37 for a refusal to cooperate in discovery, and the reasoning employed by the courts in imposing the two sanctions is almost the same. The second area of similarity is the analogous considerations applied by the court both in denying a preclusion order and in granting a motion to limit discovery, the so-called "protection order," under Federal Rules 30(b), 31(d), 33, and 34. It is suggested that in this respect the courts are once more applying discovery rules at pre-trial, although this is not verbalized in the decisions. Compare Syracuse Broadcasting Corp. v. Newhouse, 271 F.2d 910, 916 (2d Cir. 1959) with Glick v. McKesson & Robbins, Inc., 10 F.R.D. 477 (D. Mo. 1950) and Compagnie Continentale D'Importation v. Pacific Argen. Braz. Line, Inc., 1 F.R.D. 388 (S.D.N.Y. 1940).

pleadings, and evidence, including witnesses and exhibits; and, in at least one instance, failure to appear at a pre-trial conference without adequate excuse has been construed as a waiver of the right to trial by jury. Some of these rules limit the area of discretion somewhat by designating infractions for which sanctions can be imposed. Among the more commonly listed instances are counsel’s failure to comply with a local pre-trial rule, to prepare for trial or the pre-trial conference, to appear at the conference or participate therein, to make full disclosure of evidence, or to reveal witnesses, exhibits or points of proof.

In analyzing the propriety and effect of preclusion orders, it must be noted initially that when unnecessary and irrelevant matter is eliminated in order to narrow the issues for trial, no serious legal problems exist. It is only when an integral portion of a party’s case, or the evidence necessary to prove such an integral portion, is challenged by a motion to preclude that the court is faced with the difficult task of judging whether the entry of such an order is justified. In this regard, it makes little difference whether the order is directed at a contention per se or at evidence necessary to prove that contention; for in both instances the courts apply approximately identical standards in their determination.

Also to be noted is the fact that in these more problematic situations, the entry of a preclusion order has substantially the same effect as a refusal to allow modification of the pre-trial order; for in terms of effect it makes no difference whether the court excludes evidence or a theory at trial because it does not appear in the pre-trial statement or because of counsel’s failure to abide by some pre-trial rule. Thus, it is both reasonable and probable that many of the factors which influence the court

100 E.D. Wis. R. 12.
101 E.D.N.C. Civ. R. 7P; M.D.N.C.R. 22(p); W.D. Pa. R. 5(II)G.
102 E.D.N.C. Civ. R. 7Q, 7R; M.D.N.C.R. 22(q); W.D. Okla. R. 16(b).
104 E.D.N.C. Civ. R. 7P, 7R (without good cause shown); M.D.N.C.R. 22(q); W.D. Okla. R. 16(b).
108 W.D. Pa. R. 5(II)G (unless (1) not discoverable at pre-trial, (2) impeaching matter, or (3) privileged matter).
109 E.D.N.C. Civ. R. 7Q (willful failure to reveal exhibits and points of proposed proof); M.D.N.C.R. 22(q) (willful failure to reveal witnesses or exhibits).
in regard to the question of modification will also influence them in regard to the question of the appropriateness of a preclusion order. However, the fact that this latter question will generally arise at an earlier stage of litigation than the former would also indicate that the courts will be even more reluctant to enter a preclusion order before trial than they are to deny modification during trial.

In determining whether a preclusion order is appropriate, the courts have looked to various factors to guide their decisions. Although it is not always clear that each court has considered all the facets of the case in a particular instance, nevertheless, it can be reasonably assumed that all relevant factors are, or at least should be, weighed.

There are several general considerations. Foremost among these is the realization that the preclusion order is a drastic sanction and should be employed only to the extent necessary to attain the desired purpose—an entirely just disposition of the case in a speedy and efficient manner.110 The need to limit and define issues is tempered with the desire to preserve, whenever possible, litigation on the merits.111 For this reason courts are naturally reluctant to enter an order which would result in a default judgment or dismissal without adequate cause.112 Furthermore, the courts bear in mind their "overriding responsibility to see that justice is done between litigants before the court."113 In most cases, they accomplish this by examining the prejudice which would result to both the litigants upon the withholding or granting of the preclusion order.114

If a meritorious claim or defense is presented, a preclusion order for purely technical procedural reasons is generally avoided by the courts. Thus, in *Gamble v. Pope & Talbot, Inc.*,115 even though defendant's pre-trial memorandum was filed ten months late, a motion to strike, which would have resulted in a default on the issue of liability and pre-

110 Syracuse Broadcasting Corp. v. Newhouse, 271 F.2d 910, 915 (2d Cir. 1959); Matheny v. Porter, 158 F.2d 478 (10th Cir. 1946).
112 Padovani v. Bruchhausen, 293 F.2d 546 (2d Cir. 1961); Syracuse Broadcasting Corp. v. Newhouse, 271 F.2d 910 (2d Cir. 1959); Gamble v. Pope & Talbot, Inc., supra note 111.
115 Supra note 114; accord, Padovani v. Bruchhausen, supra note 114.
cluded evidence in reduction of damages, was denied where plaintiff showed no substantial prejudice. In other instances, the availability of alternative sanctions, which are adequate and effective, but not as harsh, has deterred the court from entering a preclusion order.116 Thus, where costs are considered a sufficient penalty, the courts have refused to impose more drastic remedies.117

When certain factors are present, a more liberal standard of compliance with pre-trial procedure is generally applied. If the controversy involves serious injuries or a substantial sum of money, the courts are less likely to impair, even slightly, either party's case.118 Similarly, inadequate compliance which has arisen because of a lack of precision or clarity in the court order demanding compliance, has been viewed as the fault of the trial court rather than of the party,119 and when a case is extremely complex, burdensome or difficult adherence to the court orders and rules should seldom be demanded.120

The conduct of the attorney is often scrutinized to determine whether pre-trial is being pursued in good faith. In so doing, a court's desire to obtain cooperation through the imposition of sanctions is often balanced by the requirement that counsel must show a sufficiently consummacious attitude before he is deemed to have breached his duty to cooperate.121 Whether or not adequate opportunity to comply has been given weighs heavily in this determination.122 The court thus closely examines the degree of neglect that has occasioned the consideration of a sanction and is often wary of punishing the client when the error or dereliction is that of his attorney.123

As the above indicates, it appears that substantial compliance to the court's orders is all that is required to deter the entry of a preclusion

118 Ibid.
120 Syracuse Broadcasting Corp. v. Newhouse, 271 F.2d 910, 915 (2d Cir. 1959).
121 Padovani v. Bruchhausen, 293 F.2d 546, 548 (2d Cir. 1961), where the court stated: "[T]here has here been not so much outright default on counsel's part as a debatably inadequate compliance . . . ." Ibid.
order. At least such was the position of the Second Circuit in two of the *Syracuse Broadcasting Corp.* cases, when in considering the appropriateness of sanctions for failure to comply with a pre-trial order to disclose requested information in a so-called "big case," that court adopted a test under which substantial compliance with the court order was sufficient to deter the entry of a preclusion order. However, as to the propriety of a preclusion order for noncompliance with a court order to disclose, the *Syracuse* court also felt that if information relating to a certain issue was peculiarly within one party's knowledge, and that party failed to comply with an order to produce such information, an order precluding him from introducing evidence on that issue would have been manifestly justified. But, the court pointed out that since no special knowledge existed in that case and since the information was equally accessible to each party, it was error to preclude the opposing party from introducing such evidence as he was able to on that point, even though he may have failed to comply with the disclosure order.

In *Padovani v. Bruchhausen*, the Second Circuit considered another special problem of the "big case" when it was presented with a situation where a comprehensive preclusion order was entered after several detailed pre-trial statements had been rejected as insufficient. In setting aside the preclusion order, which was so broad that it destroyed plaintiff's case, the *Padovani* court pointed out that if the courts are permitted to *force* parties by successive repleadings to limit their case beyond the issues presented in the pleadings, to plead legal theories and to disclose witnesses, there is a distinct danger that pre-trial will become so particularized that it will fall prey to the shortcomings of special pleading. On the other hand, Judge Dawson's separate opinion points out that the antithesis, "notice pleading," is equally fraught with difficulties.

---

125 271 F.2d at 916.
126 293 F.2d 546 (2d Cir. 1961).
127 Id. at 548-49.
128 Id. at 551-52 (separate opinion). In still another protracted case, however, this same circuit held that a writ of mandamus does not lie to vacate a preliminary court order defining the issues, where although the parties' proposed issues were substantially identical, no formal agreement acceptable to both could be reached. Life Music, Inc. v. Edelstein, 309 F.2d 242 (2d Cir. 1962) (per curiam). The district court in this case distinguished *Padovani* on the ground that "ours is not a situation where the court is 'clubbing the parties into admissions they do not willingly make . . . ." Life Music, Inc. v. Broadcast Music, Inc., 31 F.R.D. 3, 22 (S.D.N.Y. 1962).
This controversy as to the proper role of pre-trial in the “big case” indicates once more the underlying policy problem which confronts the courts: whether to require strict compliance with pre-trial rules in order to enforce the pre-trial procedure or liberally to effectuate the overall policy of the Federal Rules of Civil Procedure. The courts must have the power to control pre-trial procedure if it is to be effective, but it is evident that this power must be kept within reasonable bounds. It is suggested that an awareness and balancing of the factors discussed will enable the courts to achieve both goals, at least in the area of preclusion orders.

DISMISSAL AND DEFAULT

Since it has been seen that the courts are reluctant to enter a preclusion order which would make it impossible for a party to prove his case, it is only natural that the judiciary has generally shown even greater reluctance to impose the necessarily fatal sanctions of dismissal or default. Perhaps the most compelling deterrent to the entry of such an order is the feeling that such a harsh penalty would be unjust in most cases. Nevertheless, the availability of these sanctions plays an important part in the orderly administration of pre-trial procedure in the federal courts; for, if the possibility of these penalties exists, cooperation in pre-trial practice can be established and maintained under the mere threat of drastic penalty with only rare cases of imposition. Moreover, recent developments in the Supreme Court indicate that the threat is not an idle one. However, in considering what conduct is so reprehensible as to warrant this harsh penalty, the courts must balance in this critical area,

129 Illustrative of this division in the courts are the contrasting views on the question of whether a party can be forced to disclose trial witnesses at pre-trial. The weight of authority, although not the better rule, is that a party cannot be forced to make this disclosure. Padovani v. Bruchhausen, 293 F.2d 546, 549-50 (2d Cir. 1960); 2A Barron & Holtzoff, Federal Practice and Procedure § 650, at 90-93 (Rules ed. 1961); 4 Moore, Federal Practice ¶ 26.19, at 1077-81 (2d ed. 1950). On the other hand, it has been argued that Rules 16 and 26(b) give the court the power to require, even to the point of forcing, disclosure of witnesses, Goldberg v. Ann Vien, Inc., 29 F.R.D. 6 (N.D. Ga. 1961). In Mitchell v. Madden, 1 Fed. Rules Serv. 2d 33.533, Case 3 (W.D. La. Oct. 14, 1958), an order was granted requiring the Secretary of Labor to disclose all witnesses under local pre-trial rules 2 and 2(a) of the Western District of Louisiana and in the “interest of justice.”


in particular, the value of an efficient pre-trial system against the justice or injustice which the imposition of such a sanction will work.

Rule 41(b) of the Federal Rules of Civil Procedure specifically authorizes that "for failure . . . to prosecute or comply with these [federal] rules or any order of court, a defendant may move for dismissal . . . ."132 Since the words "defendant may move" are merely permissive, it has been held that the courts, acting on their own initiative, may clear their calendars of cases which are dormant because of inaction or dilatoriness.133 Generally, the authority of the district courts to dismiss sua sponte has been held to be an inherent power, stemming not from any rule or statute, but from the necessity of the courts to manage their own affairs so as to have an orderly and expeditious disposition of cases.134

Various local court rules expressly place dismissal and/or default within the pre-trial judges' discretion. And in many instances matters of dismissal which would ordinarily be considered at a hearing on a special motion before or after pre-trial are dispensed with at the pre-trial conference.135 Thus, for example, courts are empowered to dismiss at pre-

132 Fed. R. Civ. P. 41(b) further provides that "unless the court in its order for dismissal otherwise specifies, a dismissal under this subdivision . . . , other than a dismissal for lack of jurisdiction or for improper venue, operates as an adjudication on the merits."


135 Rule 56 of the Federal Rules of Civil Procedure, providing for summary judgment, is compulsory in its nature and supplements the discretionary pre-trial system of Rule 16. Even though issues of material fact exist, Rule 56(d) directs the court, where practicable on a motion for summary judgment, to enter an order settling the uncontroverted issues and specifying the controverted issues remaining for trial. Woods v. Mertes, 9 F.R.D. 318 (D. Del. 1949). By this use of 56(d), some of the objectives of pre-trial can be obtained outside of the confines of Rule 16. As in the case of a pre-trial order, the order under 56(d) is subject to modification and revision at trial upon a proper showing. Coffman v. Federal Laboratories, Inc., 171 F.2d 94 (3d Cir. 1948), cert. denied, 336 U.S. 913 (1949); E. I. du Pont De Nemours & Co. v. United States Camo Corp., 19 F.R.D. 495 (W.D. Mo. 1956). Thus, Rule 56(d) can be used to simplify issues, but the pre-trial conference, where available, would seem to be the more appropriate method. Yonkers Contracting Co. v. Maine Turnpike Authority, 24 F.R.D 205, 229 (D. Me. 1958); United States v. Copacabana, Inc., 17 F.R.D. 297 (S.D.N.Y. 1955); Krause v. George K. Garrett Co., 5 F.R.D. 385 (D. Del. 1946). Also, if no genuine issue exists, the pre-trial conference can be used to grant summary judgment. Associated Beverages Co. v. P. Ballantine & Sons, 287 F.2d 261 (5th Cir. 1961); Lynch v. Call, 261 F.2d 130 (10th Cir. 1958); Klein v. Belle Alkali Co., 22 F.2d 658 (4th Cir. 1926); Berger v. Brannan, 172 F.2d 241 (10th Cir.), cert. denied, 337 U.S. 941 (1949); Berry v. Spokane, P. & S. Ry., 2 F.R.D. 483 (D. Ore. 1942).
trial for lack of proper service or jurisdiction, want of prosecution, or failure to state a cause of action.

Other grants of power are more directly related to pre-trial proceedings. Some courts may act as in non-appearance for final trial, when a party fails or refuses to appear at the pre-trial conference. Dismissal has also been authorized for failure to comply with any pre-trial rule or order, failure to file a pre-trial statement, or prepare for or participate in the pre-trial conference.

In approaching the question of dismissal, the reluctance of the courts to impose harsh sanctions is balanced with a consideration of the degree of recalcitrance and lack of cooperation. In making this determination, the courts consider factors very similar to those discussed in connection with preclusion orders. Thus, as in the case of the preclusion order, the allegation of a substantial loss, a serious injury or a meritorious defense, the availability of appropriate alternative penalties, or the extreme complexity of a case will often cause the courts to be more lenient in the degree of compliance to the rules and orders of the court which they require. However, the possibility of prejudice to the cooperating non-negligent party, if the dismissal is not granted, is also given weight.

As a general rule with regard to dismissals, it can be assumed, as it was by the court in Gamble v. Pope & Talbot, Inc., that since Rule 16

137 E.g., N.D. Ind. R. 10, 12.
139 E.g., D.D.C.R. 12(b); S.D. Ind. R. 17; W.D. Mo. R. 20(d); S.D.N.Y. Calendar R. 16(b); M.D.N.C.R. 22(o); E.D. Pa. Standing Order (Feb. 8, 1960); E.D. Wash. R. 8; W.D. Wash. R. 40.
140 E.g., E.D.N.C. Civ. R. 7P; M.D.N.C.R. 22(p); W.D. Pa. R. 5(II)H.
141 D.D.C.R. 12(b).
142 E.g., S.D.N.Y. Calendar R. 16(b); E.D. Pa. Standing Order (Feb. 8, 1960).
146 As the Court in Link v. Wabash R.R., 370 U.S. 626 (1962) stated: "[K]eeping this suit alive merely because plaintiff should not be penalized for the omissions of his own attorney would be visiting the sins of plaintiff's lawyer upon the defendant." Id. at 634 n.10.
permits modification of the pre-trial order even during the actual trial to prevent "manifest injustice," "manifest injustice" should not be endorsed in the form of a dismissal at an earlier stage of the litigation.\textsuperscript{148} Thus, a showing of excusable neglect, or good and sufficient reason for the failure to comply or cooperate, will normally be sufficient to avoid the entry of a dismissal or default.\textsuperscript{149} However, in cases of flagrant refusal to comply with a court order or rule, or where the court feels that a non-complying party has been shown "utmost lenience," dismissal is justified and has been entered.\textsuperscript{150} In taking into account the opportunity that has been given the party to comply, the courts have looked to the length of time the case has been pending and the advance notice that has been given, as well as the number of notices to comply.\textsuperscript{151} However, in connection with this last factor, the Supreme Court, in \textit{Link v. Wabash R.R.},\textsuperscript{152} has cast doubt upon the weight which it should be given as it stated that in most cases neither advance notice of the possibility of dismissal nor an opportunity for an adversary hearing are necessary before a dismissal for failure to prosecute can be entered at pre-trial.\textsuperscript{153} As a generalization, it can be said that when a court feels that fair and reasonable opportunity to comply has been afforded, it will be less reluctant to enter a dismissal or default.

In most cases, the courts in reaching their determination, will look at the record as a whole, considering all the circumstances, rather than an isolated instance of non-compliance. In \textit{Link}, for example, the Court considered the entire history of the case, especially previous delays, in justifying their dismissal.\textsuperscript{154} Thus, the Supreme Court never reached the question of whether dismissal is warranted for a failure to appear at the pre-trial conference alone, but decided only that in light of all the

\begin{itemize}
  \item \textsuperscript{148} Id. at 764-65.
  \item \textsuperscript{149} See Fed. R. Civ. P. 60(b).
  \item \textsuperscript{150} Package Mach. Co. v. Hayssen Mfg. Co., 266 F.2d 56 (7th Cir. 1959), affirming 164 F. Supp. 904 (E.D. Wis. 1958).
  \item \textsuperscript{151} Janousek v. Wells, 303 F.2d 118 (8th Cir. 1962) (pending four years; plaintiff impeding progress by every maneuver and obstacle possible); Package Mach. Co. v. Hayssen Mfg. Co., supra note 150 (pending three years; every fair and reasonable opportunity to comply).
  \item \textsuperscript{152} 370 U.S. 626 (1962).
  \item \textsuperscript{153} Id. at 632. It should be noted, however, that failure to seek relief from such a judgment under Rule 60(b) led the Court to minimize any claim of excusable neglect on appeal. Ibid.
  \item \textsuperscript{154} See 370 U.S. 626 passim (1962); accord, Sandee Mfg. Co. v. Rohm & Haas Co., 298 F.2d 41 (7th Cir. 1962).
\end{itemize}
attendant circumstances, the failure of plaintiff's counsel to attend the pre-trial hearing was indicative of a failure to prosecute, justifying dismissal. By so doing the Court refused to follow the approach of the court of appeals in that case which apparently based its affirmance of the dismissal solely upon counsel's failure to appear at the pre-trial conference without adequate excuse.

Even though the Supreme Court decided Link ostensibly on the narrow ground stated above, the decision must nevertheless be considered as the strongest caveat yet pronounced in the entire area of pre-trial sanctions. The facts of the case are subject to varying interpretations and would seem to provide enough of the factors necessary to persuade a court to impose lesser penalties than dismissal. Notwithstanding this, the Supreme Court affirmed the dismissal. Unless the Court intends or chooses to limit its decision in the future, it must be construed as strengthening and fully endorsing the imposition of sanctions at pre-trial, even in their most extreme form. Apparently only the most extenuating and mitigating excuse for any neglect would amount to good and sufficient reason for the appellate court reversing the trial court's determination of what sanction is appropriate.

THE PROBLEM OF PUNISHING THE CLIENT

Underlying this entire matter of sanctions and, perhaps, determinative of many of the unanswered questions in this area is the significant and controversial problem of whether the client should be punished for the shortcomings of his attorney. In this regard, judicial thinking has traditionally considered the attorney and client as a single entity for most purposes, but when a grave penalty is inflicted upon an innocent client as a result of his attorney's conduct, the validity of this mode of thought is rightly subject to serious inquiry.

155 370 U.S. at 635 & n.12.
156 See 291 F.2d 542 (7th Cir. 1961), aff'd, 370 U.S. 626 (1962).
157 The dissents in the court of appeals and the Supreme Court cast considerable doubt on the Supreme Court's holding on the facts. Counsel had phoned the court and opponent on the scheduled day of pre-trial hearing and the previous day to explain his inability to attend. Furthermore, much of the six years' delay was seemingly attributable to the court and defendant railroad's counsel. The dissent has an extremely persuasive argument that neither dismissal for failure to appear without adequate excuse nor dismissal for failure to prosecute was justified. See 370 U.S. 626, 636 (1962) (Black, J., dissenting); 291 F.2d 542, 547 (7th Cir. 1961) (dissenting opinion). The Supreme Court has denied a petition for rehearing and reargument in the Link case. Link v. Wabash R.R., 371 U.S. 873 (1962) (memorandum decision).
Normally, the justification for visiting the sins of the attorney upon his client is stated in agency terms—the client has freely selected a lawyer and cannot avoid the consequences of the actions of his lawyer-agent.\textsuperscript{168} According to this line of reasoning, the client is bound by the acts of his representative and if the conduct of the lawyer falls below acceptable standards, the client's remedy is a malpractice suit, not the repudiation of the agency relationship.\textsuperscript{159} To do otherwise, it is contended, would be to visit the sins of a party's attorney upon the opposing party.\textsuperscript{160}

However, such reasoning has not gone uncriticized. One judge has termed it "as unrealistic as imposing a penalty on a passenger because the railroad train on which he rides is late because of the dereliction of the operating crew."\textsuperscript{161} Indeed, unless the litigant's conduct has been extremely vexatious, it is difficult to see how requiring the opposing party to try his case on the merits works any great injustice. Further, the client seeking to redress his injury by way of a malpractice suit is faced with a difficult task. Not only must he prove that but for the attorney's negligence he would not have lost the suit, but he has also to prove the damages which resulted from such negligence.\textsuperscript{162} Therefore, the client is given a remedy which requires that he prove two cases in one, and the burden of proof is on him in both instances.\textsuperscript{163}

Furthermore, the mechanical application of this agency theory does seem to ignore some of the realities of the lawyer-client relationship. In selecting legal counsel, the layman has very few methods of checking upon his competency. When a person is licensed by a state to practice law, it is presumed that he has a certain degree of skill, integrity and knowledge. Even if it can be assumed that the general public is aware that in reality there are good and bad lawyers, it is often difficult for the unskilled layman to determine which lawyer is best qualified to

\textsuperscript{159} Id. at 634 n.10.
\textsuperscript{160} Ibid.
\textsuperscript{161} Gamble v. Pope & Talbot, Inc., 307 F.2d 729, 734 (3d Cir. 1962) (dissenting opinion).
handle his case. Nonetheless, clients are forced to make a choice and may be suddenly apprised of the fact that a valuable claim has vanished because of the mistake of their counsel. For these reasons Justice Black suggests that the better rule would be that a client should never be punished for the conduct of his attorney unless he is first notified that such a threat hangs over his head.\textsuperscript{164} According to Justice Black, this is the least that should be required if we are to incorporate the "basic constitutional requirements of fairness into the administration of justice."\textsuperscript{165} Yet, in spite of these arguments, the attorney-client agency theory is presently the law.\textsuperscript{166}

A seemingly easy answer to the problem would be to impose sanctions directly on the attorney. Since a high degree of cooperation between the bench and bar, not between the bench and parties, is the essence of an effective pre-trial system, the imposition of penalties upon the lawyer, who was responsible for the infraction of the rules, seems to be quite logical. Moreover, penalizing the negligent attorney rather than the blameless client would more effectively promote the attorney's full compliance with the ground rules for administering the pre-trial system.

However, short of the Supreme Court's suggestion that the attorney may be indirectly fined by means of a malpractice suit, the prevailing law in this area severely limits the district courts' ability to impose a fine directly upon counsel for failure to comply with the pre-trial rules.\textsuperscript{167} At present two rather limited statutory penalties exist. The first is a


\textsuperscript{165} Ibid.

\textsuperscript{166} Ibid. at 633-34.

\textsuperscript{167} See Gamble v. Pope & Talbot, Inc., 307 F.2d 729 (3d Cir. 1962). But see Bardin v. Mondon, 298 F.2d 235 (2d Cir. 1961), wherein the Second Circuit stated:

[Appellants have suffered from the sins of their counsel, sins of which they probably knew nothing at all. Although a litigant is ordinarily bound by the mistakes of his counsel, in this instance, we think it would serve a better purpose to require counsel himself to pay for the inconvenience caused by his own dilatory conduct.

As a result, we hold that the case ought to be remanded with instructions that it be dismissed without prejudice for failure to comply with an order of the court . . . on condition that [counsel] . . . pay all trial costs taxed to [his client] . . . , and for having so multiplied the proceedings as to increase costs unreasonably, that he pay an additional $100. in costs . . . . If payment is not made as directed, the action will be dismissed with prejudice.

Id. at 238. (Footnotes omitted.) The case appears to be in direct conflict with the Gamble decision. The "additional $100" would be a fine prohibited by the Gamble court, if payable to the government, and a windfall if payable to his client, since the client has already received "all trial costs." In addition, it should be noted that if the attorney fails to comply with the court's order, the case is dismissed with prejudice and apparently, the client must once more rely on the remedies of a malpractice suit, with all its attendant difficulties.
federal statutory provision that "any attorney . . . who so multiplies the proceedings in any case so as to increase costs unreasonably and vexatiously may be required by the court to satisfy personally such excess costs." This, however, is judicially limited by the fact that only excess costs can be imposed and that such expenses are payable only to a party litigant. Therefore, the United States, as sovereign, cannot impose a fine in the form of a fee, above and beyond costs.

A second source of disciplinary power for the district courts is the federal contempt statute. However, since the statute imposes fines only for specified conduct and since it has been held that the procedural protections of Rule 42 of the Federal Rules of Criminal Procedure must be provided, the contempt statute supplies a rather limited power to the courts. Aside from these two statutory sanctions, it has been held that nothing in the Federal Rules permits sanctions in the form of penalties to be levied upon a lawyer in a civil litigation, on the grounds that fining an attorney without a finding of contempt and the procedural safeguards of Criminal Rule 42 would violate the fifth amendment. Furthermore, it has been contended that such "basic disciplinary innovations" are not within the power of the various district courts under Rule 83, in that they require a uniform approach and the consideration of the Supreme Court's advisory committee.

In opposition to the above, it has been argued by some that such a fine is within the discretionary rulemaking power granted the district courts by Rule 83 and is necessary to the effective acceleration of litigation

---

170 Ibid. But, the United States can collect excess costs under 28 U.S.C. § 1927 (1958) when it is a party-litigant.
A court of the United States shall have power to punish by fine or imprisonment, at its discretion, such contempt of its authority, and none other, as—
(1) Misbehavior of any person in its presence or so near thereto as to obstruct the administration of justice;
(3) Disobedience or resistance to its lawful writ, process, order, rule, decree, or command.
Subsection (2) of this section has been held inapplicable to attorneys. Cammer v. United States, 350 U.S. 399 (1956).
174 Ibid.
175 Id. at 731-32.
through pre-trial procedure. The supporters of such a view have pointed out that demanding uniformity in the application of sanctions would render Rule 83 meaningless, since docket conditions, varying greatly from forum to forum, require that each district court be able to adapt its procedure and practice to local needs. Moreover, since the Supreme Court has approved dismissal of a party’s case, a much more drastic sanction, for failure to comply with pre-trial procedure, a fine upon counsel cannot be said to be too harsh a penalty. Similarly, it might be argued that the imposition of a fine upon counsel does not carry “the criminal hallmark,” but rather, unless an abuse of discretion has occurred, it carries the deserved label of “uncooperative.” Finally any alleged abuse of discretion could be reviewed and, if necessary, corrected by the appellate courts.

In short, the argument for imposing fines upon counsel at the trial court’s discretion seems sufficiently reasonable to warrant that courts, or, if necessary, Congress, investigate the possibility of expanding the rather limited present scope of the district courts’ powers in this area.

CONCLUSION

Only in recent years have the courts come clearly to grips with the problem of attempting to place pre-trial within the integrated system of practice envisioned by the Federal Rules. Consequently, there remains a notable lack of definition in many areas. Much of the uncertainty surrounding modification of the pre-trial order, for example, results from the fact that the courts have not yet reached any settled view of the relationship between the pre-trial order and the pleadings. Similarly, in attempting to evolve the sanctions necessary to enforce the basic rules of pre-trial practice and ensure the cooperation of the parties, the courts have not agreed on where the balance should be struck between the desire to promote litigation on the merits and the necessity for strong sanctions, including dismissal, needed to make pre-trial effective.

In spite of this confusion, however, a study of the cases indicates much progress. The more recent decisions indicate a trend away from the application of artificial tests of “manifest injustice” and the utilization of sanctions of minimum punitive value, toward a realization that only the thoughtful exercise of judicial discretion can do justice in the particular

176 Id. at 733-37 (dissenting opinion).
177 Id. at 735 (dissenting opinion); see Bardin v. Mondon, 298 F.2d 235, 237 & n.4 (2d Cir. 1961).
factual situations of individual cases. Hence, the better decisions have emphasized the power of the courts to impose adequate safeguards to protect both parties in granting modification of the pre-trial order. Also, in enforcing the rules of pre-trial practice the courts have increasingly recognized that in certain situations meaningful sanctions must be imposed if the pre-trial procedure is to succeed while at the same time indicating a realization that it is unconscionable to penalize the blameless client for the negligence of his attorney if another method of enforcement can feasibly be utilized. It thus appears that the courts are well-started on their dual tasks of making the indefinite criteria of Rule 16 meaningful standards for decision and developing those sanctions needed to make pre-trial practice a vital part of the process of federal litigation.

MARIO ESCUDERO
JOHN J. KENNY
HARRY PELTZ, JR.

RELIEF FOR COLLAPSIBLE CORPORATIONS
UNDER SUBSECTION (e)

INTRODUCTION

Rarely has a provision of the federal tax law evinced as much criticism as has the statute governing collapsible corporations. Since its inception in 1950, legal scholars have denounced it as grossly complex, poorly drafted and incapable of fulfilling its purpose. Although the statute is extremely complex and produces many inequitable results, its enactment was, nevertheless, necessary to preclude the conversion of ordinary income into capital gains under the aegis of incorporation. Furthermore,


2 "[T]he collapsible corporation is a device whereby one or more individuals attempt to convert the profits from their participation in a project from income taxable at ordinary income rates to long term capital gains taxable only at a rate of 25 percent." S. Rep. No. 2375, 81st Cong., 2d Sess. 88 (1950); H.R. Rep. No. 2319, 81st Cong., 2d Sess. 96 (1950). Thus, the purpose of this 1950 Amendment (now Int. Rev. Code of 1954, § 341) was to prevent individuals from using a temporary corporation to convert ordinary income into capital gain. See S. Rep. No. 2375, supra, at 88; H.R. Rep. No. 2319, supra, at 96.
the immediacy of the need for legislation dictated the atmosphere in which the statute was drafted and further compounded the difficulty of formulating statutory solutions to many of the problems inherent in the concept of a collapsible corporation—a concept indigenous to the closely held corporation.

Several amendments to the original statute became necessary because of the hiatus which existed, i.e., the 1950 statute failed to embrace some industries which were converting ordinary income into capital gains through the corporate device. Such piecemeal drafting of a statute regulating a corporate problem as involved as this was bound to create problems of interpretation and application. This is best reflected by the conflict existing in circuit courts today and the fact that the courts are still in the process of deciphering the language of the statute.

Subsection (e), the most recent amendment to section 341, was enacted to mitigate the hardships of the collapsible corporation provisions. The purpose of this note will be to trace briefly the history of the collapsible corporation and to analyze in detail this new subsection in an effort to determine which, if any, of the rigors of section 341 have been ameliorated.

BACKGROUND

Prior to 1950, the Internal Revenue Service was not equipped, either statutorily or judicially, to cope with the corporate device which taxpayers were utilizing to avoid ordinary income tax rates. Although


4 See H.R. Rep. No. 2319, supra note 2, at 96-99; S. Rep. No. 2375, supra note 2, at 88-91. At first, the corporate scheme was used principally by the motion picture industry. The main participants in the production of a movie would incorporate and accept stock in the corporation in lieu of compensation. When the movie was substantially completed but prior to the realization by the corporation of income attributable to the movie, the shareholders would either sell their stock or liquidate the corporation. Upon a liquidation, the corporation would distribute to the shareholders an interest in the movie proportionate to the ownership of stock. The basis of the interest received by the shareholder would be his proportionate share of the fair market value (based on expected earning) of the movie at the time of liquidation. The difference between the basis of the shareholder’s stock and the basis of the shareholder’s interest would only be taxed as capital gains and the shareholder would amortize this amount against his proportionate share of the net receipts from the
various means had been employed to prevent the enjoyment of capital gains rates on profits which should have been ordinary income,\(^5\) none of these had proved successful and finally the Service acquiesced in a case involving a classic example of a collapsible corporation.\(^6\) Realizing that the only method of eliminating this nemesis was through legislation, Congress was eventually prevailed upon and section 117(m),\(^7\) the first statutory attack on collapsible corporations, was added to the Internal Revenue Code of 1939.

exhibition of the movie. The shareholder would not receive ordinary income unless the net receipts from the movie exceeded the fair market value as computed at the time of liquidation. If the shareholders chose to sell their stock instead of liquidating, the gain on the sale of stock would be subject to capital gains rates. Thus, in either case the shareholders would realize only capital gains rates on profits which should have been ordinary income.

Other offenders in this particular corporate scheme were real estate dealers who could manage capital gains rates on ordinary income in much the same way as the motion picture people.

\(^5\) The Internal Revenue Service attempted many arguments to combat these transactions. There were three major arguments relied on. First, the commissioner argued that the corporate entity was a sham and that the gain should be taxed as ordinary income to the individuals. However, the courts consistently rejected this argument on the grounds that the factors surrounding the entity were indigenous to a corporation, that the entity was engaged in the normal corporate activities, and that a corporation does not lose its identity merely because it is organized for a single purpose. See Herbert v. Riddell, 103 F. Supp. 369, 374-75 (S.D. Cal. 1952). Secondly, the argument was advanced that the corporation was guilty of an anticipatory assignment of income and this transaction was invalid because the one who earns the income is obliged to pay the tax thereon. United States v. Joliet & Chicago R.R., 315 U.S. 44 (1942); Lucas v. Earl, 281 U.S. 111 (1930). It was held, however, that the principle governing anticipatory assignments was inapplicable for the reason that the corporation was dissolved by liquidation prior to the time when the income was earned and, therefore, the income resulting from the original corporate activity was not attributable to the corporation since it was no longer in existence. See Herbert v. Riddell, supra, at 384-85; Pat O'Brien, 25 T.C. 376, 384 (1955), acquiesced in part, 1957-1 Cum. Bull. 6, 9 n.14. The third theory advanced by the government was the doctrine espoused in Commissioner v. Court Holding Co., 324 U.S. 331 (1945) which held that a corporation could not perform all the preliminary matters relating to a sale of the assets and then dissolve, thus giving the benefit of the contract of sale to its shareholders. This theory was rejected on the ground that the corporation was not engaged in negotiating a sale, but only in dissolving the corporation and liquidating the corporate assets. See Pat O'Brien, supra.

\(^6\) Pat O'Brien, supra note 5. Briefly, in this case the shareholders liquidated the corporation surrendering their stock. They reported capital gains on the difference between the basis of their stock and the fair market value of the interest in the property received. The Tax Court held in favor of the taxpayer.

It should be noted that the money received in excess of the projected value of the movie at the time of distribution was taxable as ordinary income. Id at 385.

\(^7\) Int. Rev. Code of 1939, § 117(m), added by ch. 994, § 212, 64 Stat. 934 (1950).
Section 117(m) deemed a corporation collapsible when it had been "formed or availed of principally for the manufacture, construction, or production of property" with a view to the disposition of stock by, or a distribution of the assets to, the shareholders prior to the "realization . . . of a substantial part of the net income to be derived from such property . . ." 8 If the corporation came within this definition, the effect was to disallow the shareholders capital gains consequences and to treat all gain realized as ordinary income. 9 However, the complexity of the statute, the difficulty of interpretation, and the inclusion of a subjective test brought practically insoluble problems to the courts and resulted in basic differences of opinion. 10


9 This was accomplished by subsection (1) of section 117(m) which provided that "gain from the sale or exchange . . . of stock of a collapsible corporation . . . shall be considered as gain from the sale or exchange of property which is not a capital asset." Int. Rev. Code of 1939, § 117(m)(1), added by ch. 994, § 212, 64 Stat. 934 (1950).

10 The phrase "with a view to" requires a subjective analysis in order to determine the intent of the shareholder of the corporation. See Int. Rev. Code of 1954, § 341(b)(1). However, this requirement is satisfied when the collapsing of the corporation is contemplated by those persons who are in a position to determine the policies of the corporation, either because they own a majority of the voting stock or otherwise. Treas. Reg. § 1.341-2(a)(2) (1955). Furthermore, the regulations provide that the "requisite view" exists even if it was only contemplated as a "recognized possibility." Ibid. Most Courts follow this regulation. See e.g., Sidney v. Commissioner, 273 F.2d 928, 931 (2d Cir. 1960); August v. Commissioner, 267 F.2d 829, 833-34 (3d Cir. 1959); Burge v. Commissioner, 253 F.2d 765, 770 (4th Cir. 1958). Thus, the arm of the statute is all embracing.

However, the courts are not in accord as to when the "view" must exist. A literal and sweeping interpretation has been taken by the Second and Fourth Circuits which held that as long as the requisite view actually occurs prior to the realization by the corporation of a substantial part of its potential income from the property, the requirement is satisfied. See Glickman v. Commissioner, 256 F.2d 108, 111 (2d Cir. 1958) (dictum); Burge v. Commissioner, supra, at 769 (dictum). Under such an interpretation the "view" may exist either at the inception of incorporation or during or after the production, manufacture, or construction of the property. Contra, Treas. Reg. § 1.341-2(a)(3) (1955) wherein it is provided that the "requisite view" must exist either prior to or during the course of the production of the property in question and not after production. The Tax Court as well as several circuit courts agree with the regulation. See Jacobson v. Commissioner, 281 F.2d 703 (3d Cir. 1960); Payne v. Commissioner, 268 F.2d 617, 621-22 (5th Cir. 1959) (dictum); Maxwell Temkin, 35 T.C. 848 (1961). Although this conflict exists among the circuits, it is mitigated to a large extent since, as indicated, most circuits are in harmony with the "recognized possibility" test.

A problem arose in construing the intention of Congress as to what part of the clause "principally" should modify i.e., either "manufacture, production, construction" or "view to sale or exchange." A modification of the latter would greatly simplify the taxpayer's burden of proof. However, such an interpretation would stifle the usefulness of the statute.
Although the statute as originally drafted thwarted many attempts to convert ordinary income into capital gains, the exclusion of any type of purchased property, as distinguished from property “manufactured, constructed or produced,” left open a loophole of major proportions. A corporation would purchase property which would, by its nature, increase in value with age (whiskey, for example). After the shareholders had held their stock for more than six months they would dispose of it, realizing a substantial gain because the assets were certain to appreciate in value. This gain was taxed at capital gains rates.\(^{11}\) In an effort to preclude this practice, section 117(m) was amended in 1951 to include property purchased as stock in trade.\(^{12}\) With respect to this newly included property, however, the difficulty of determining collapsibility remained unchanged.

The 1954 revision of the Internal Revenue Code introduced several new provisions into the collapsible corporation section. From the Senate report, it appears that Congress was disturbed because the statute failed

---

One writer has suggested that “principally” should modify “with a view to.” See Schlesinger, supra note 1, at 898. However, judicial decisions have generally held that “principally” modifies the phrase “for the manufacture, production, or construction of property.” In Weil v. Commissioner, 252 F.2d 805 (2d Cir. 1958), the court stated that “the corporation may be treated as collapsible if ‘manufacture, construction, or production’ was a principal corporate activity even if the ‘view to’ collapse was not the principal corporate objective when the corporation was formed or availed of . . . .” Id. at 806. See Mintz v. Commissioner, 284 F.2d 554, 558 (2d Cir. 1960); Burge v. Commissioner, supra at 768.

Diverse interpretation problems have also arisen in regard to the phrase “before the realization . . . of a substantial part of the taxable income . . . .” \(\text{§}\) 341(b)(1)(A). The regulation interpretation is that a corporation is collapsible if, prior to the sale of the stock by the shareholders, there remains a substantial part of net income yet to be realized from the property. Treas. Reg. \(\text{§}\) 1.34-5(b)(5) (1955). (Emphasis added.) Compare Commissioner v. Kelley, 293 F.2d 904 (5th Cir. 1961), with Abbott v. Commissioner, 258 F.2d 537 (3d Cir. 1958), for dissimilar interpretations of “substantial part.” See Leverson v. United States, 157 F. Supp. 244 (N.D. Ala. 1957) (holding a more than 50% realization at the corporate level meets the “substantial realization” test) and Commissioner v. Kelley, 293 F.2d 904 (5th Cir. 1961) (holding that 30% was sufficient). See also G. A. Heft, 34 T.C. 86 (1960), aff’d, 294 F.2d 795 (5th Cir. 1961) (realization of only 17% is insufficient).


\(^{12}\) To cover this loophole Congress added a phrase to the definition of a collapsible corporation. Since this 1951 amendment, “a corporation formed or availed of principally . . . for the purchase of property which (in the hands of the corporation) is stock in trade, or inventory, or property held by taxpayer primarily for sale to customers in the ordinary course of his trade or business is deemed a collapsible corporation. Int. Rev. Code of 1939, ch. 994, \(\text{§}\) 212, 64 Stat. 934 (1950), as amended, 65 Stat. 502 (1951).
to cover all collapsible corporations. In an effort to tighten up the collapsible corporation statute, Congress enacted section 341 which contained a larger category of purchased assets than the 1951 Amendment, introduced a presumption of collapsibility in certain instances, and increased the number of shareholders affected by the section by expanding its coverage to include all more-than-five-per cent shareholders. The 1954 revision completed the attack on collapsible corporations; however, it was soon discovered that the entire statute was so severe that it could not adequately accomplish its objectives.

Three exceptions limiting the applicability of the collapsible corporation provision had been written into the 1950 statute in its original form, but these exceptions were extremely problematical and the extent

---


14 Int. Rev. Code of 1954, §§ 341(b)(3)(C), (D). The amendment added to the group of purchased assets which may give rise to collapsibility (1) certain “unrealized receivables or fees,” and (2) all section 1231(b) assets, except such assets used in the manufacture, production, or sale of stock in trade or property held primarily for sale in the ordinary course of business. Ibid.

15 Int. Rev. Code of 1954, § 341(c). This section established a presumption of collapsibility if at the time of sale or exchange of stock by shareholder or distribution (pursuant to § 341(a)) by corporation, the fair market value of the corporation’s § 341 assets (defined in § 341(b)(3)) was (1) 50% or more of the fair market value of corporation’s total assets (total assets for this section excluded cash, obligations which were capital assets in hands of the corporation, and stock in any other corporation), and (2) 120% or more of the adjusted basis of such § 341 assets.


17 Section 117(m)(3) had provided that this section should not apply to any shareholder unless he “(i) owned . . . more than 10 per centum in value of the outstanding stock of the corporation, or (ii) owned stock which was considered as owned at such time by another shareholder who then owned . . . more than 10 per centum in value of the outstanding stock of the corporation; . . .” secondly, it did not apply unless “more than 70 per centum of such gain is attributable to the property . . . manufactured, constructed, or produced; . . .” and thirdly, it did not apply to “gain realized after the expiration of three years following the completion of such manufacture, construction or production.” Int. Rev. Code of 1939, ch. 994, § 212, 64 Stat. 935 (1950).

18 The three year limitations necessitated a determination as to when construction was completed. Court decisions indicate that a project was completed only after the last detail has been attended to, which, in the case of an apartment house, may mean that it will be partially occupied before construction is deemed complete. See Glickman v. Commissioner, 256 F.2d 108 (2d Cir. 1958) (everything finished but the landscaping and minor building work). This interpretation severely restricts the limitation written into the statute.

A second problem arose out of the fact that a corporation was only considered col-
to which they were workable limitations on the vast scope of the statute is questionable. A more effective attempt to alleviate the stringencies of the collapsible corporation provisions occurred in 1958 with the addition of subsection (e) to section 341. The need for this change arose out of the fact that the original statute and its earlier amendments had been so loosely drafted that judicial interpretations were completely subverting the basic purpose for its enactment. Occasions arose when a literal reading of the statute resulted in the imposition of ordinary income rates on income from a transaction that would have been entitled to capital gains rates had the individual not chosen the corporate form.

This was effectively illustrated by one side of a recent conflict between the Second and Fifth Circuits concerning the proper interpretation of the pre-1958 collapsible corporation provisions. In each of two cases, one brought before the Fifth Circuit and the other brought before the Second, the taxpayer contended, among other things, that the collapsible corporation provisions should not apply because their gain would have been taxed at capital gains rates had the transactions been consummated on an individual level. Although a denial of this contention would be collapsible when more than 70% of the shareholder's gain was attributable to the collapsible property of the corporation, i.e., property manufactured, produced, or constructed. The Federal Housing Authority had established the practice of guaranteeing mortgage loan funds in an amount in excess of the actual construction. Upon distribution of this excess, the taxpayers would contend that this excess was not gain attributable to collapsible property and would attempt to circumvent the statute in this manner. However, in Glickman v. Commissioner, supra at 111, the court said that "as to the cash distribution the Tax Court correctly held that all of it was directly attributable to the constructed property, since it was paid out of the funds advanced to Mott on the F.H.A. mortgage." The same theory was espoused in Burge v. Commissioner, 253 F.2d 765, 769-70 (4th Cir. 1958).

21 Braunstein v. Commissioner, supra note 20. In this case the taxpayers formed two corporations for the purpose of building apartment house complexes. The Federal Housing Administration guaranteed mortgage funds in excess of the construction costs. Following completion of construction the taxpayers sold their stock in both corporations and received cash distributions in an amount equal to the excess mortgage funds. The entire gain was reported as capital gains. However, the Commissioner contended that the corporations were collapsible under section 117(m) of the Internal Revenue Code of 1939 and, therefore, the gain should be treated as ordinary income.
22 United States v. Ivey, 294 F.2d 799 (5th Cir. 1961), rehearing denied, 303 F.2d 109 (1962). In this case the taxpayers began construction on an apartment house. When the construction was three-fourths complete the taxpayers sold their stock and reported their gain as capital gains. Once again the Commissioner argued that the corporation was collapsible, this time under section 341 of the Internal Revenue Code of 1954.
trary to the avowed purpose of the statute and work as a penalty on individuals who incorporated. The Second Circuit held against the taxpayer; for unfortunately, the language of section 341 and its predecessor (section 117(m) of the Internal Revenue Code of 1939) encompassed a myriad of corporations which were not in the immediate intended path of the statute but which were caught up in the broad sweep of the collapsible corporation provisions. Recognizing these facts, the Fifth Circuit found for the taxpayer and declared that “when language is so broad that a literal construction would in certain cases make nonsense of the statute in light of purposes of the legislation, it is reasonable to make sense of the statute by not applying it when the mischief at which it is aimed is absent.

On the other hand, the Second Circuit maintained that “although the courts must often interpret sections of the Internal Revenue Code in light of their purposes in order to carry out Congressional intent ... when this would require the courts to extensively rewrite clear statutory language, the task of revision should be left to Congress.” Regardless of which circuit is more justified in its approach, it is exactly these inopportune results portended by the Second Circuit’s decision that Congress has attempted to obviate with the enactment of subsection (e).

**Subsection (e)**

As has been seen, application of section 341 to corporations produced such bizarre results that it soon became evident that legislative relief was necessary. Subsection (e) became the legislators’ solution to the rigors

---

23 Included in the statement of legislative intent as reasons for the enactment of subsection (e) are:

(1) “provisions of the present law ... are so broad that in a number of situations they may have exactly the opposite effect from that intended—instead of preventing the conversion of ordinary income into capital gain, they may instead convert what would otherwise be capital gain into ordinary income”; (2) “applicability of the provisions of present law ... depends upon the subjective intent of the parties”; (3) “the entire gain of the shareholder is taxed at ordinary income tax rates, notwithstanding the fact that had the shareholder not employed the corporate entity a large part of his gain might have been taxed at capital gains rates”; and (4) “provisions of present law frequently impede or prevent legitimate business transactions.”


24 Ibid.

25 United States v. Ivey, 294 F.2d 799, 803 (5th Cir. 1961).


27 “[T]he collapsible corporation provisions of present law ... both by their terms and as interpreted, are so broad that in a number of situations they may have exactly the opposite effect from that intended—instead of preventing the conversion of ordinary income
of that section.\textsuperscript{28} As was noted previously, the original collapsible corporation provisions contained the phrase "with a view to" which necessitated a determination of the shareholders' states of mind.\textsuperscript{29} With subsection (e), an attempt was made to obviate the need for such a subjective analysis by setting up objective standards for determining whether a corporation would be entitled to relief from the sanctions imposed on a collapsible corporation.\textsuperscript{30} At the same time subsection (e) was designed to prevent the conversion of what would ordinarily be capital gains into ordinary income under section 341. Also, since the wrath of section 341 was indiscriminately bestowed on every shareholder and there existed no reason to penalize a person who held stock in a corporation purely for purposes of investment, subsection (e) was designed to immunize the investor from ordinary income rates in certain situations while imposing them on dealers. However, as will be seen, the relief in this regard is not complete, although much has been done to save the investor when there exists no logical reason to deprive him of deserved capital gains rates.

Although subsection (e) is a relief measure, it was not intended to provide complete relief, and, as a result it is only applicable to a limited number of corporate and shareholder transactions.\textsuperscript{31} Assuming that a shareholder meets the numerous and stringent qualifications necessary to come within the subsection, he may sell or exchange his stock and

\textsuperscript{28} Subsection (e) of § 341 was added to the Internal Revenue Code of 1954 by § 20(a) of the Technical Amendments Act of 1958. Section 20(b) of this act provided that the provisions of subsection (e) were to become effective for taxable years beginning January 1, 1958; and subsection (e)'s provisions were to apply only to transactions (sales, exchanges, and distributions) which occur after September 2, 1958. Technical Amendments Act of 1958 §§ 20(a), (b), 72 Stat. 1606, 26 U.S.C. § 341(e) 1958. Although subsection (e) was included in a technical amendments act, it was definitely not a mere procedural change in the existing collapsible corporation law, but an important substantive alteration. However, authors generally agree that the complexity of subsection (e) will present many new problems in the collapsible corporation area. See Anthoine, Federal Tax Legislation of 1958: The Corporate Election and Collapsible Amendment, 58 Colum. L. Rev. 1146, 1175-76 (1958); Axelrad, Collapsible Partnerships, 12 U. So. Cal. 1960 Tax Inst. 269, 375; Bitker, The Tax Treatment of Collapsible Corporations, 13 Vand. L. Rev. 129, 142 (1959); Boland, Collapsible Corporations Under the 1958 Amendments, 17 Tax L. Rev. 203, 209 (1962); Modrall, Collapsible Corporations and Subsection (e), 37 Taxes 895 (1959).

\textsuperscript{29} See supra note 10.


\textsuperscript{31} Int. Rev. Code of 1954, § 341(e)(1)-(4) [hereinafter all section references will be to the Internal Revenue Code of 1954, unless otherwise indicated].
realize only capital gains on income that would have been ordinary income prior to 1958. As will be seen, the shareholders may also qualify for relief in a section 337 liquidation once the corporation has qualified.32 Also, with respect to the corporation, no gain or loss will be recognized to the corporation on a complete liquidation pursuant to either section 33333 (elective nonrecognition on a liquidation within one month) or section 33734 (nonrecognition if the liquidation is completed within twelve months). However, as in the case of a sale or exchange of stock by the shareholder, several requirements must be complied with before the corporate liquidations will qualify to enjoy the benefits of subsection (e).

The new subsection, because of its narrow availability, excludes many legitimate business transactions from the relief which it affords.35 On the corporate level, partial liquidations are exempted from the subsection, as are distributions to shareholders, if the value of the property received is in excess of the shareholder’s basis for his stock.36 The rationale for the exclusion of the latter is that the basis of the property to the recipient would be the fair market value of the property at the time of the distribution which would allow the shareholder a stepped-up basis taxable only at capital gains rates. Since the underlying purpose of the collapsible corporation provisions is to disallow capital gains treatment on gain which should be taxable as ordinary income, this purpose could be effectively undermined by distributing highly appreciated property and obtaining a stepped-up basis. Also, at the shareholder level, a sale or exchange of stock to the corporation by a shareholder is explicitly excluded from subsection (e).37 Any gain from such a sale would, by the workings of section 341(a), be considered ordinary income since subsection (e) fails to grant relief.

The necessity of seeking relief in subsection (e) obviously does not arise unless the corporation in question is proven collapsible. Of course, a successful application of subsection (e) can render harmless a determination as to collapsibility since the penalties of the collapsible provisions would not be imposed on the corporation or the shareholders regardless

32 Section 341(e)(2).
33 Section 341(e)(3).
34 Section 341(e)(4).
36 Therefore these two transactions remain subject to § 341(a)(2), (3). The tax effect of this is ordinary income rates on the gain. All other transactions are, unless expressly included, excluded from subsection (e).
37 Subsection (e) “shall not apply to any sale or exchange of stock to the issuing corporation . . . .” § 341(e)(1).
of collapsibility. However, section 341(e)(11) provides that a corporation's failure to qualify for the benefits of subsection (e) shall not be taken into account in determining whether or not a corporation is collapsible. As a result, even though the original statute and subsection (e) are integrated into a single statute, they function independently and must be applied separately.

At this juncture, a brief analysis of the criteria which must be met in order to qualify for the relief of subsection (e) seems advisable. Throughout subsection (e) the formula\(^{38}\) used is the net unrealized appreciation\(^{39}\) on "subsection (e) assets"\(^{40}\) (numerator) over the net worth of the corporation\(^{41}\) (denominator). If the computation in the above formula exceeds fifteen per cent, the corporation and all of its shareholders have failed to qualify and must pay ordinary income tax rates on any gain realized. On the other hand, if the net unrealized appreciation does not exceed fifteen per cent of the net worth, the corporation has qualified and the same formula is then applied to the shareholders on an individual basis to determine the tax status of their gain.

It should also be noted that neither the collapsible provisions of the original statute nor the tests of subsection (e) need be applied to a shareholder who never owned more than five per cent in value of the outstanding stock of the corporation.\(^{42}\) Such a shareholder is completely free of the hardships of the collapsible corporation provisions.

**Subsection (e) Assets**

Only the net unrealized appreciation on the "subsection (e) assets" of the corporation as defined in subsection (e)(5)(A), is included in the numerator of the formula delineated above. The statute divides these assets into four categories. The first\(^{43}\) of these consists of any assets,

---

38 Hereinafter, this formula will be referred to as the "fifteen per cent test."
39 Section 341(e)(6)(A)(i), (ii). The net unrealized appreciation is the amount by which the unrealized appreciation ((B)(i), (ii) fair market value over the adjusted basis) exceeds the unrealized depreciation ((C)(i), (ii) adjusted basis over the fair market value).
40 Section 341(e)(5)(A)(i)-(iii), explained in detail infra, pp. 356-61.
41 Sections 341(e)(7)(A)(i), (ii), (B). Net worth equals the fair market value of all the assets, plus the amount of any distributions in complete liquidation made by the corporation, minus all its liabilities.
42 Section 341(d)(1). Hereinafter, mention of shareholders presupposes that the reference does not apply to any person who has not at any time owned more than 5% of the value of the outstanding stock of the corporation.
43 Section 341(e)(5)(A)(i).
except section 1231(b) assets (without regard to the holding period),\textsuperscript{44} which would be ordinary income assets in the hands of the corporation, \textit{i.e.}, assets the sale of which would produce ordinary income, not capital gains, to the corporation. Also included as corporate “subsection (e) assets” in the first category are assets which if sold by a shareholder owning more than twenty per cent in value\textsuperscript{45} of the outstanding stock of the corporation, either directly or constructively,\textsuperscript{46} would result in ordinary

\textsuperscript{44} Section 1231(b) provides:

For purpose of this section—

(1) General Rule. The term “property used in the trade or business” means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 167, held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not—

(A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year,

(B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or

(C) a copyright, a literary, musical, or artistic composition, or similar property, held by a taxpayer described in paragraph (3) of section 1221.

However, § 341(e)(9) provides that for the purposes of subsection (e), § 1231(b) assets are such \textit{without} regard to any holding period.

\textsuperscript{45} Hereinafter, all reference to a more-than-5\%, more-than-5\%-but-not-more-than-20\%, and more-than-20\% shareholder is in regard to the fair market value of the outstanding stock of the corporation.

\textsuperscript{46} According to § 341(e)(10), the ownership of stock for purposes of subsection (e) is ascertained in the manner prescribed in § 341(d). Under § 341(d), the amount of stock which a person is deemed to constructively own is determined generally by applying the constructive ownership provisions of § 544(a) (relating to personal holding companies) which states that all persons shall be deemed to be in constructive ownership of all stock owned by brothers and sisters of half or whole blood, spouses, ancestors and lineal descendants. However, § 341(d) further expands the family of a stockholder to include “the spouses of that individual’s brothers and sisters (whether by the whole or half blood) and the spouses of that individual’s lineal descendants.” The rules of attribution are especially important in determining whether a stockholder owns 5\% or less of the outstanding value of stock (if so, the shareholder is free from collapsible corporation restrictions), or more-than-20\% of the outstanding value of the stock. A shareholder, who is a dealer and via the constructive ownership rules of subsection (e)(10) owns more-than-20\% of the corporate stock, can “taint” the whole corporation by adding corporate assets which would be ordinary income assets in his hands to the total subsection (e) assets of the corporation. The broad ownership provisions of the 1958 collapsible corporate amendment will further hinder the workings of the statute in that every time a shareholder sells stock or whenever the corporation liquidates, every shareholders’ family (as expanded by a § 341(d)), corporate, partnership, and trust interests will have to be examined to determine the total ownership of stock imputable to the shareholder. This may lead to the ironic result that a more-than-20\% shareholder may cause the corporation to fail to qualify for the benefits of subsection (e) because a distant member of his family, e.g., brother-in-law, is a dealer in a corporate asset. The brother-in-law dealer will be deemed, under the constructive ownership provisions, to own the stock of the actual shareholder, and as he now is a more-than-20\% shareholder-dealer, any
income to him.\textsuperscript{47} This transaction is viewed as if the more-than-twenty-per cent shareholder had sold all the assets of the corporation at one time to one person.\textsuperscript{48} In other words, if the shareholder who owns more than twenty per cent of the stock of the corporation is a dealer in any property (exclusive of 1231(b) assets) which is an asset of the corporation, this asset will be deemed a corporate “subsection (e) asset” and any unrealized appreciation on it will be added to the numerator for purposes of the “fifteen per cent test.”

Assume, for example, that a corporation’s sole asset is an apartment house with an adjusted basis to the corporation of $1000 and a fair market value of $1500, the net unrealized appreciation being $500. If on a sale by the corporation the $500 gain would be taxed as capital gains to the corporation, and not as ordinary income, the apartment house is not a “subsection (e) asset” unless a more-than-twenty-per cent shareholder would be subject to ordinary income rates on gain from the sale of the apartment house as an individual. Thus, if the asset is not an ordinary income asset of the corporation and there is not a more-than-twenty-per cent shareholder who is a dealer in such assets, the asset is not a “subsection (e) asset” and the net unrealized appreciation of $500 does not become a portion of the numerator for purposes of the computation.

Included in the second category\textsuperscript{49} of “subsection (e) assets” are section 1231(b) assets without regard to the holding period, if there is a net unrealized depreciation on all such assets. Irrespective of the existence corporate asset which would be an “ordinary income asset” in the brother-in-law’s hands may be included in the “subsection (e) assets.” The unrealized appreciation of this new “subsection (e) asset” may sufficiently increase the numerator (unrealized appreciation of all “subsection (e) assets”) to an extent that the corporation will now fail to meet the “fifteen per cent test”—all because a non-shareholder brother-in-law was a dealer.

Also, under the constructive ownership rules of subsection (e), if a shareholder is found to own more than 20 per cent of the value of the outstanding stock, he cannot sell his stock to certain “related persons,” as defined in subsection (e)(8), if he wishes to qualify for benefits of subsection (e). § 341(e)(1). Likewise, the corporation under a § 337 liquidation does not receive the benefit of nonrecognition of gain or loss on sale of depreciable property to “related persons” of a more-than-20% equity owner. § 341(e)(4). Subsection (e) defines “related persons” as any individual shareholder’s spouse, ancestors, lineal descendants and any corporation controlled by such shareholder. § 341(e)(8)(A)(i), (ii).

\textsuperscript{47} However, in ascertaining which are “subsection (e) assets” under a § 333 liquidation as provided for by § 341(e)(3), it is stated in § 341(e)(5)(B) that a more-than-5% shareholder will be the norm.

\textsuperscript{48} Section 341(e)(5)(A).

\textsuperscript{49} Section 341(e)(5)(A)(ii).
of a more-than-twenty-per cent shareholder, the full amount of the net unrealized depreciation on such 1231(b) assets is used to offset the net unrealized appreciation on other “subsection (e) assets” in determining the figure to be used as the numerator.\textsuperscript{50} However, and this is the third class of “subsection (e) assets,”\textsuperscript{51} if there is a net unrealized appreciation on all 1231(b) assets, the entire unrealized appreciation is not necessarily included in the numerator, but only the amount of the net unrealized appreciation, if any, on the section 1231(b) assets which would have produced ordinary income had they been sold by a more-than-twenty-per cent shareholder, \textit{i.e.}, a dealer in those particular section 1231(b) assets.\textsuperscript{52} As can be seen, the second and third categories of “subsection (e) assets” are mutually exclusive since it is impossible to have both an overall net unrealized appreciation and an overall net unrealized depreciation on the same group of assets with the result that, if a corporation has any section 1231(b) assets at all, they will only fit into one of the two categories of 1231(b) assets.

The fourth classification of assets as corporate “subsection (e) assets” is obviously a direct attack on the industry which was initially responsible for the collapsible corporation—the moving picture industry.\textsuperscript{53} Thus, the statute includes within this fourth category all property “which consists of a copyright, a literary, musical, or artistic composition, or similar property, or any interest in any such property, if the property was created in whole or in part by the personal efforts of any individual who owns more than five per cent in value of the stock of the corporation,”\textsuperscript{54} If any of the corporate property falls within this category, the net unrealized appreciation on such property increases the numerator by that amount. It should be noted that a whole or part creator has been substituted for a dealer (as is the case in the other classes of “subsection (e) assets”) and that the percentage requirement of ownership of stock in the corporation by the shareholder has been reduced from twenty to five per cent. Reduc-

\textsuperscript{50} Thus, if a corporation has two § 1231(b) assets, one which has an unrealized depreciation of $250 and the other which has an unrealized appreciation of $100, the net unrealized depreciation, $150, on the § 1231(b) assets would be used to offset any unrealized appreciation on other subsection (e) assets.

\textsuperscript{51} Section 341(e)(5)(A)(iii).

\textsuperscript{52} Assume there is a total net unrealized appreciation on all 1231(b) assets of the corporation of $1000, but the net unrealized appreciation on § 1231(b) assets which are ordinary income assets in the hands of a more-than-20% shareholder is only $400. Only the $400 is included in the numerator, not the $1000.

\textsuperscript{53} See supra note 4.

\textsuperscript{54} Section 341(e)(5)(A)(iii).
tion of the stock ownership percentage to such a low figure effectively prevents a producer, director, actor, or anyone closely connected with the production from accepting stock in the corporation in lieu of compensation.55 Also, since subsection (e) disallows all distributions in liquidation of depreciable or amortizable property,56 the scheme which was utilized by the motion picture industry prior to 1950 to obtain a stepped-up basis on such property57 has been effectively thwarted.

Although it is readily understandable why these severe restrictions58 were placed on the movie industry (realizing, of course, that other industries will be similarly affected under this category), in enacting them Congress seems to have disregarded the primary purpose of subsection (e), i.e., to prevent conversion of profits which would ordinarily be treated as capital gains into ordinary income.59 As an example of how this provision can abort the avowed legislative intent, consider the consequences when the shareholder-part creator only holds six per cent of the outstanding stock of the corporation. The effect is this: the numerator is increased by the full amount of the net unrealized appreciation on, say, a motion picture, which may make it very difficult for the corporation to qualify under the “fifteen per cent test.” Assuming the corporation fails to qualify, the shareholders must pay ordinary income rates on the gain realized upon disposition of their stock or liquidation of the corporation. This means that innocent investors owning ninety-four per cent of the corpora-

---

55 However, since shareholders owning less than 5% of the value of the outstanding stock of the corporation are exempt from the rigors of § 341, it is possible for an individual to receive 5% or less of the stock of the corporation as compensation and realize only capital gains on the increment in value of the stock. This method of tax avoidance would have limited use because it is doubtful that a small amount of stock (the original value of which would be taxed at ordinary income rates as compensation) would adequately compensate the creator.

56 Section 341(e)(4)(C).

57 The stepped-up basis stems from the fact that the distributee’s basis would then be the fair market value of the property at the time of distribution and not the corporation’s adjusted basis. § 301(d)(1). The real effect is that the receipts from the property would be offset against the depreciation expense, thereby resulting in a minimum amount of taxable ordinary income from this asset.

58 Section 1221(3) restricts individual taxpayers by precluding them from obtaining capital gains upon the sale of “a copyright, a literary, musical, artistic composition, or similar property” which they produced through their own efforts. Section 341 disallowed the use of a corporate device to avoid the adverse tax effects of § 1221(3). Because of the numerous conditions imposed by subsection (e) before relief will be granted, the taxpayer’s position has not been improved to any real extent.

tion, although entitled to capital gains, must now pay tax at the ordinary income rates. What makes the result even more illogical is that the tax consequences to the shareholders are the same even if the six per cent shareholder-part creator received a salary commensurate with his contribution to the production of the movie. The penal nature of this particular provision seems unnecessarily discriminatory when one considers that dealer-shareholders in other types of collapsible corporations have less difficulty obtaining relief under subsection (e).

_Fifteen Per Cent Test_

Satisfaction of the "fifteen per cent test" is determinative of the relief given under subsection (e). In order to qualify, the net unrealized appreciation on all corporate "subsection (e) assets" must not exceed fifteen per cent of the net worth of the corporation. If it does, no shareholder will be allowed capital gains treatment on the gain recognized; if it does not, the test must be reapplied to each shareholder since, under the provisions of subsection (e), there may be variations as to the "subsection (e) assets" used to determine the percentage figure for the individual shareholder.\(^{60}\) with the result that some shareholders may pay only capital gains rates while others may be subject to ordinary income rates. The formula for computing the per cent is as follows:

\[
\frac{\text{Net Unrealized Appreciation of Subsection (e) Assets}}{\text{Net Worth of the Corporation}} = \text{Per cent.}
\]

The net unrealized appreciation on "subsection (e) assets" equals the amount by which unrealized appreciation on "subsection (e) assets" exceeds the unrealized depreciation on "subsection (e) assets."\(^{61}\) Unrealized appreciation is equal to the excess of the fair market value of the asset over its adjusted basis,\(^{62}\) and, conversely, the unrealized depreciation.

---

\(^{60}\) A shareholder-dealer who owns more than 5% but not more than 20% in value of the outstanding stock of the corporation and a more-than-20% shareholder who, although not an actual dealer, may, for purposes of subsection (e), be a hypothetical dealer, may be charged with additional subsection (e) assets on an individual basis. § 341(e)(1)(B), (C); § 341(e)(2)(B), (C). The hypothetical dealer will be explained in detail infra, pp. 371-75.

\(^{61}\) Section 341(e)(6)(A)(i), (ii). However, when determining the unrealized appreciation on certain subsection (e) assets, the gain on which would produce both ordinary income and capital gains, e.g., § 306 stock, discount bonds under § 1232 and emergency facilities under § 1238, only that amount of the unrealized appreciation which is equal to the ordinary-income gain will be included in the total unrealized appreciation of subsection (e) assets. § 341(e)(6)(D).

\(^{62}\) Section 341(e)(6)(B)(i), (ii).
is equal to the excess of the adjusted basis over the fair market value. If the unrealized appreciation is larger than the unrealized depreciation then the numerator is the difference (net unrealized appreciation). However, if the converse is true, the numerator would be a minus figure. The test must then be applied to each shareholder to determine if there is enough unrealized appreciation on other assets which are “subsection (e) assets” only as to him, to not only absorb the negative numerator, but also to end up with net unrealized appreciation large enough to prevent qualification under the “fifteen per cent test.”

The denominator in the formula, i.e., the net worth of the corporation, is equivalent to the sum of the fair market value of all the assets of the corporation (not limited to the fair market value of “subsection (e) assets”) plus the value of any property which has been distributed by the corporation in complete liquidation, less the sum of all the liabilities of the corporation. As a precautionary measure to prevent tax avoidance, the legislators provided that “the net worth of a corporation as of any day shall not take into account any increase in net worth during the one-year period” immediately preceding such day “to the extent attributable to any amount received by it for stock, or as a contribution to capital or as paid-in surplus, if it appears that there was not a bona fide business purpose for the transaction . . . .” This provision precludes the shareholders from pouring capital into the corporation in an effort to increase net worth and correspondingly decrease the per cent to satisfy the “fifteen per cent test.” However, limiting the effect of this provision to one year seems unwise since such wording in a tax statute could give rise to a conclusive presumption that any increase in capital one year and one day prior to date of the computation of net worth was for a bona fide business purpose. Thus, by a literal reading of the statute, the

63 Section 341(e) (6) (C) (i), (ii).
64 Section 341(e) (7) (A) (i). The fair market value of the assets held by the corporation must be ascertained in order to determine both the net worth and the unrealized appreciation on “subsection (e) assets.” However, as to the proper method for determining the “fair market value”, subsection (e) and the regulations under § 341(c) are silent. It would seem that the sales price should be determinative of the “fair market value,” since that is the price a buyer would pay for the asset, and thus the amount the corporation would realize.
65 Section 341(e) (7) (A) (ii).
66 Section 341(e) (7) (B).
67 Section 341(e) (7).
68 An exception was provided by § 341(d) (3) for gains not realized by a shareholder until more than three years after completion of the “collapsible” property. It would seem
shareholders could flood the capital account of the corporation one year and one day before liquidation of the corporation or disposition of their stock and not be called upon to defend the validity of the transaction. Also, upon incorporation the shareholders could overinvest in the corporation and practically assure qualification under the "fifteen per cent test."

To guard against the possibility of disqualification by the "fifteen per cent test," a corporation should also issue preferred stock instead of bonds, absent an overriding policy consideration. Bonds, since they are treated as a debt of the corporation, would increase liabilities and thereby decrease net worth, whereas preferred stock is considered capital and an increase in capital increases net worth. Any increase in net worth without a corresponding increase in the net unrealized appreciation of "subsection (e) assets" would enhance the possibility of satisfying the "fifteen per cent test."

As the above discussion indicates, the "fifteen per cent test" is based on purely objective standards, and, as a result, if the test is met, the shareholder will be entitled to capital gains irrespective of a "view" toward collapsing the corporation. In this respect, the "fifteen per cent test" has overcome the infirmities of a subjective standard. Under the "fifteen per cent test," a more-than-twenty-per cent shareholder who is a dealer will be entitled to capital gains treatment if he complies with the "fifteen per cent test," notwithstanding the fact that, had he not incorporated, he would not be entitled to the benefits of capital gains treatment but would be subject to ordinary income rates. However, any inconsistency created by the objectiveness of the criterion is somewhat mitigated by the fact that the "fifteen per cent test" does deter a shareholder from realizing too large a profit on his investment at capital gains rates.

Another interesting facet of both the original collapsible corporation statute and subsection (e) is that a shareholder pays either all capital gains or none.69 This all-or-nothing approach seems a bit rigid and could

---

69 It should be noted, that the fragmentation of gain may exist under section 341(d)(3), i.e., if some of the "collapsible" assets have been held for more than three years, then
be mitigated by an approach to the problem which would allow a particular shareholder to receive capital gains treatment on a portion of his gain and ordinary income treatment on the residue.\textsuperscript{70} However, under existing law, a shareholder must either fulfill the "fifteen per cent test" or be subject to ordinary income rates on his entire gain.

1231(b) Assets

Some of the most difficult rules in subsection (e) are those governing the categorization of section 1231(b) assets as "subsection (e) assets." The statute provides that section 1231(b) assets are "subsection (e) assets" "if the unrealized depreciation on all such property . . . exceeds the unrealized appreciation on all such property . . . ."\textsuperscript{71} Therefore, if there is this net unrealized depreciation on all section 1231(b) assets, the net unrealized appreciation on all other "subsection (e) assets" is diminished by this amount and only the remaining appreciation, if any, comprises the numerator.\textsuperscript{72} With respect to the "fifteen per cent test" the allowance of this offset is necessary because unrealized depreciation on any asset decreases the net worth of the corporation. To illustrate, assume, that a section 1231(b) asset is valued at one hundred dollars (adjusted basis) by the corporation. If this asset subsequently decreases in value (fair market value) by twenty dollars, the net worth of the corporation will also decrease twenty dollars because one element of the net worth computation is the value of assets at the current fair market value. Recalling capital gains treatment will ensue; however, as to other "collapsible" assets, ordinary income rates will result, if they have been held less than three years.

\textsuperscript{70} This approach has been recommended by the Advisory Committee on Subchapter C. of the Internal Revenue Code of 1954. See discussion on proposed § 343, infra, pp. 383-84.

\textsuperscript{71} Section 341(e)(5)(A)(ii).

\textsuperscript{72} Example:

\begin{center}
\begin{tabular}{lccc}
 & Basis & Fair Market Value & Unreal. App. or (Depr.) \\
\hline
Cash & 100 & 100 & — \\
Inventory & 800 & 1000 & 200 \\
\textsection 1231(b) Assets: & & & \\
Buildings used & & & \\
in the business & 500 & 400 & (100) \\
Equipment & 50 & 100 & 50 \\
Liabilities & 100 & 100 & — \\
\end{tabular}
\end{center}

As there is a net unrealized depreciation on § 1231(b) assets of $50, this net depreciation is used to offset the unrealized appreciation of $200 on the other subsection (e) assets. Thus, the unrealized appreciation on all subsection (e) assets is now $150. This becomes the numerator in the formula, and as the denominator (net worth), which is the fair market value of assets ($1600) minus liabilities ($100), remains a constant $1500, it reduces the ratio from 200/1500 to 150/1500, or from 13\% to 10\%.
that a decrease in net worth will increase the percentage for the "fifteen per cent test," it would be inequitable to charge a corporation with a decrease in net worth (denominator) and disallow a corresponding decrease in net unrealized appreciation (numerator).

When there is not a net unrealized depreciation on section 1231(b) assets as above, but an overall net unrealized appreciation on these assets, the full amount of the net appreciation is not necessarily included. The addition to the numerator equals only the net unrealized appreciation on the section 1231(b) assets which would have been ordinary income assets in the hands of a shareholder who owns more than twenty per cent in value of the outstanding stock of the corporation.\textsuperscript{73} An inequity results from this formula when there is a net unrealized appreciation on "ordinary income-1231(b) assets" (added to the numerator) and net unrealized \textit{depreciation} on other section 1231(b) assets which are not "ordinary income-1231(b) assets"; for although the net unrealized depreciation has, in effect, diminished the net worth (denominator), no offset against the net unrealized appreciation included in the numerator is provided for. Therefore, by reducing the denominator without a corresponding reduction of the numerator, qualification under the "fifteen per cent test" becomes more difficult.

Also in spite of the fact that the prevailing theme of subsection (e) is to disallow capital gains treatment to dealers and grant the treatment to investors wherever possible, the provisions relating to section 1231(b) assets can produce a most ironic result in that a more-than-twenty-per cent dealer can save every shareholder, including himself, from the onus of ordinary income rates. A situation can arise where a person, because he is a dealer in section 1231(b) assets, enables the corporation to qualify under the "fifteen per cent test." Assume there is a net unrealized appreciation on all section 1231(b) assets. Once this is determined, each asset must be considered in its turn to decide if any of them are ordinary income assets in the hands of the more-than-twenty-per cent shareholder, and if there is a net unrealized depreciation on the "ordinary income-1231(b) assets," there is a deduction of this amount from the numerator. Restating this in terms of figures, if the net worth of the corporation is five hundred dollars and the net unrealized appreciation on "subsection (e) assets" (other than section 1231(b) assets) is one hundred dollars, the shareholders will fail to qualify under the "fifteen per cent test."

\textsuperscript{73} Section 341(e)(5)(A)(iii). Hereinafter all § 1231(b) assets which would be ordinary income assets in the hands of a more-than-20% shareholder because is a dealer in such assets will be referred to as "ordinary income-1231(b) assets."
Suppose, however, that there is a net unrealized appreciation of forty-five dollars on all section 1231(b) assets but a net unrealized depreciation on "ordinary income-1231(b) assets" of thirty dollars. This amount is then set off against the one hundred dollars, the result being seventy dollars net unrealized appreciation on all "subsection (e) assets" and a percentage figure of fourteen. This means the shareholders may qualify for subsection (e) and pay capital gains rates—a result not possible without the existence of a more-than-twenty-per cent shareholder who is a dealer.

One well-known legal writer has recommended a solution to the inequity resulting to the shareholder discussed above.74 According to his theory, the portion of the net unrealized appreciation on "ordinary income-1231(b) assets" added to the numerator should be determined by applying to the net unrealized appreciation on "ordinary income-1231(b) assets" a percentage arrived at by dividing the total net unrealized appreciation on all 1231(b) assets (including "ordinary income-1231(b) assets") into the net unrealized appreciation on "ordinary income-1231(b) assets."75 Assume, for example, that the net unrealized appreciation on "ordinary income-1231(b) assets" is ten dollars and the net unrealized appreciation on all 1231(b) assets (including "ordinary income-1231(b) assets") is fifty dollars, then the amount to be included in the numerator would be two dollars (10/50 = 20%; 20% \times $10 = $2). The practical effect of this computation is to compensate for the "non-ordinary income-1231(b) assets" on which there is unrealized depreciation but which, under existing law, is not reflected as a reduction of the numerator.

Another effect of this proposed theory would be to render less likely the above-mentioned possibility of a dealer being responsible for converting what ordinarily would be ordinary income, even under subsection (e), into capital gains in derogation of the purpose of the collapsible corporation provisions. If the recommended ratio is applied to the first

74 If the approach in subsection (e) is to be continued, this rule for section 1231(b) assets should be amended so as to limit the amount of unrealized appreciation which is to be included in the tainted numerator only to that portion of the total net unrealized appreciation on all such assets equaling the ratio which the net unrealized appreciation of assets regarded as collapsible (because of dealer-shareholders) bears to such total.


75 Compare the above with the theory that the unrealized depreciation on all \$ 1231(b) assets should be set off against the unrealized appreciation on the "ordinary income—1231(b) assets" in order to ascertain the amount to be added to or subtracted from the numerator. Modrall, supra note 28, at 898.
factual situation presented78 above, the amount of the offset would be only twenty dollars \( (30/45 = 66\% \% ; \text{.66\%} \times \$30 = \$20) \). Therefore, only twenty dollars would be deducted from the net unrealized appreciation on other subsection (e) assets, leaving eighty dollars as the numerator and a percentage of sixteen which would not qualify the shareholders for the relief of subsection (e). Of course, other examples could be imagined in which the dealer could still save the corporation from ordinary income rates regardless of the application of the suggested formula. However, notwithstanding this possibility, the recommendation appears far superior to the present provisions of subsection (e).

More-Than-Twenty-Per Cent Shareholder-Dealers

Even though subsection (e) is primarily concerned with subjecting dealers, not investors, to ordinary income rates, failure of the corporation to qualify under the "fifteen per cent test" deprives every shareholder of capital gains rates. Ownership in excess of twenty per cent of the stock of the corporation by a shareholder will cause the net unrealized appreciation on property of the corporation in which he is a dealer to be imputed to the corporation, and, therefore, is includible in the numerator.77 Under these circumstances, failure of the corporation to fulfill the requirements of the "fifteen per cent test" will preclude both the dealer and every other shareholder (except five-per cent-or-less shareholders) from enjoying capital gains treatment. Thus, a more-than-twenty-per cent shareholder who is a dealer in property of the corporation "taints" this property for all the shareholders, and even investors are subject to ordinary income rates if the net unrealized appreciation on this "tainted" property plus any other "subsection (e) assets" exceeds fifteen per cent of the net worth of the corporation. If the net unrealized appreciation of the total corporate subsection (e) assets does not exceed fifteen per cent, the "fifteen per cent test" is applied shareholder-by-shareholder to determine which of the individual shareholders, if any, qualify. However, under the shareholder-by-shareholder test a pure investor, i.e., a person who is not a dealer (or hypothetical dealer)78 in any of the property of

---

76 The authors assume that Mr. Boland would pro rate net unrealized depreciation on "ordinary income-1231(b) assets" in the same manner as he pro rated net unrealized appreciation.

77 Section 341(e)(5)(A)(i). However, when considering § 1231(b) assets which are ordinary income assets in the hands of a more-than-20% dealer, the unrealized appreciation of these § 1231(b) assets is only considered if there is a total net unrealized appreciation on all § 1231(b) assets. § 341(e)(5)(A)(iii).

the corporation, regardless of per cent of stock ownership, will always satisfy the test since he is not credited with any additional "subsection (e) assets."

By rendering the determination of "dealer versus investor" a turning point in the statute, the legislators have compounded the problem of its practical application. In many instances, property will or will not be considered as a "subsection (e) asset" depending on whether or not there is a more-than-twenty-per cent shareholder who is a dealer in such property.\(^79\) The line of demarcation between dealer and investor is often a difficult question of fact to resolve.\(^80\) In addition, one of the most important factors in drawing this line has been the purpose for which the property was acquired by the individual, a determination which requires a subjective inquiry\(^81\)—the very problem the legislature was trying to circumvent. Since one of the reasons for including the "fifteen per cent test" in subsection (e) was to eliminate subjectivity from the statute,\(^82\) it would thus seem that the "dealer versus investor" dichotomy somewhat subverts congressional intent. Moreover, the "dealer versus investor" test must be applied not only to the corporation to see if it has any ordinary income assets but also to each of the shareholders which portends long and prodigious litigation on this point.

Also to be noted is the fact that, although a person has been labelled a dealer, it is possible that he had an "investment attitude" as to a particular transaction such that he would not be considered a dealer in regards to that one venture.\(^83\) Thus, we could have a situation where one who has

---

\(^{79}\) Whether or not there is a more-than-20% shareholder must be considered in determining the amount of "subsection (e) assets" under § 341(e)(5)(A)(i), (iii) but not under subsection (ii) and subsection (iii).


\(^{81}\) It has been held many times that the purpose of acquisition is of utmost importance. E.g., Gudgel v. Commissioner, 273 F.2d 206 (6th Cir. 1959); Sovereign v. Commissioner, 281 F.2d 830 (7th Cir. 1960). Although the "dealer or investor" question is basically a subjective one, the courts have used some objective standards in applying it to individual cases. In Keliher v. Brownell, supra note 80, the court considered the frequency and number of sales, improvements made on the realty, and the extensiveness of advertising. Accord, Dougherty v. Commissioner, 216 F.2d 110 (6th Cir. 1954).

\(^{82}\) Section 341(e) "is desirable in order to avoid determinations of subjective intent." S. Rep. No. 1983, 85th Cong., 2d Sess. 32 (1958).

\(^{83}\) It is well settled that a dealer may be an investor in the same kind of property in
been declared a dealer (possibly after a protracted inquiry) contends that this particular transaction was entered into for investment purposes only which again involves at least a partially subjective determination, subverting for a second time the intention of the framers of subsection (e).

Although subsection (e) is silent as to the applicability of the "investment attitude" exception to the law governing dealers, the conference committee did recognize the existence of the exception as applied to securities dealers and, no cogent reasons have been found to limit this exception to securities dealers, since, under existing law, other types of dealers have also sought and obtained relief by proving an "investment attitude." In view of the availability of the "investment attitude" exception to dealers, one curious situation could arise if the dealer had both a "view" to collapse the corporation and the requisite "investment attitude." This taxpayer would be a dual offender of the collapsible corporation provisions, i.e., dealer and "view," yet, if the corporation meets the "fifteen per cent test" (the "investment attitude" would prevent this shareholder from being responsible for any "subsection (e) assets"), the shareholders will be entitled to the relief of subsection (e). However, this possibility of unusual results does not seem sufficient reason to prohibit a dealer from relying on an "investment attitude" to prevent

which he is a dealer. E.g., Curtis Co. v. Commissioner, 232 F.2d 167 (3d Cir. 1956); S.E.C. Corp. v. United States, 140 F. Supp. 717 (S.D.N.Y. 1956), aff'd, 241 F.2d 416 (2d Cir. 1957) (per curiam), cert. denied, 354 U.S. 909 (1957); Charles E. Mieg, 32 T.C. 1314 (1959). However, before the courts will find that the dealer had an "investment attitude" as to the particular transaction, they generally require, inter alia, that the property in question be segregated from his ordinary income property. See United States v. Bondurant, 245 F.2d 265 (6th Cir. 1957); S.E.C. Corp. v. United States, supra.

84 It is the understanding of the conferees that, in applying the definition of subsection (e) assets, stock or securities held by a corporation (hereinafter referred to as "Corporation A") shall not be considered subsection (e) assets merely because a more than 20 percent shareholder is a dealer in stock or securities, if such shareholder holds his Corporation A stock in his investment account (pursuant to section 1236(a)). Therefore, the stock or securities held by Corporation A shall not be subsection (e) assets by reason of the more than 20 percent shareholder test unless, in the hands of such shareholder, the stock or securities held by Corporation A would, if held by such shareholder, constitute property gain from the sale of which would be considered ordinary income solely by reason of the application of section 341 as modified by this amendment.


85 See note 83 supra.

86 As to shareholders, who are more-than-5%-but-not-more-than-20% dealers or more-than-20% hypothetical dealers, they may still fail to qualify for the benefits of subsection (e) if, under the shareholder-by-shareholder application of the "fifteen per cent test," their "dealership" status adds a sufficient amount of unrealized appreciation to the numerator to increase the unrealized appreciation on all "subsection (e) assets" over 15% of the net worth.
taxation at ordinary income rates. This is particularly true since proof of an "investment attitude" would be a gargantuan task for one who is a dealer. Moreover, since a more-than-twenty-per cent dealer can cause innocent investors to realize ordinary income on their gain, a dealer with an honest "investment attitude" should be allowed to assert it. In addition, the shareholder who is also a dealer can always attempt to prove an "investment attitude" when he has engaged in a transaction as an individual and a denial of the right under subsection (e) would penalize him for incorporating.

Inherent in the answer to the "dealer versus investor" question is subjectivity. Determination of an "investment attitude" is also partially subjective. Regardless of the attempts of the legislators, this pyramiding of subjective tests points up that they have failed to exclude this element from subsection (e).

More-Than-Five-Per Cent-But-Not-More-Than-Twenty-Per Cent Shareholder-Dealers

Unlike a more-than-twenty-per cent shareholder, an individual who owns more than five per cent but not more than twenty per cent will not, under any conditions, "taint" the whole corporation or be responsible for the disqualification of other shareholders under the "fifteen per cent test."87 However, if the corporation qualifies because the net unrealized appreciation on ordinary income assets to the corporation plus net unrealized appreciation on ordinary income assets in the hands of a more-than-twenty-per cent shareholder does not exceed fifteen per cent of the net worth of the corporation, the "fifteen per cent test" must still be applied individually to each shareholder since the net unrealized appreciation on "subsection (e) assets" may vary depending on the status of the individual. (The net worth, however, will remain constant.)

Every shareholder starts with a numerator equal to the net unrealized appreciation on corporate "subsection (e) assets," i.e., assets which are ordinary income assets either to the corporation or to a more-than-twenty-per cent shareholder. However, if the shareholder owns more than five per cent but not more than twenty per cent of the stock, the remaining assets of the corporation must be viewed separately to determine whether a sale of that particular asset would have produced ordinary income to the shareholder.88 If so, that asset would be a "subsection (e) asset" as to

87 See §§ 341(e)(1)(B), (2)(B).
88 The "dealer versus investor" problem which was previously considered as to the
the individual only and any unrealized appreciation is added to the numerator for purposes of his "fifteen per cent test"; 89 if not, the asset is not a "subsection (e) asset" as to him. If, after adding the net unrealized appreciation on the shareholder's "subsection (e) assets" to the net unrealized appreciation on the corporation's "subsection (e) assets," the numerator exceeds fifteen per cent, the shareholder will be subject to ordinary income rates. However no other shareholder will be affected. If the percentage is fifteen or less, the gain realized is taxable only at capital gains rates.

The provisions of subsection (e) regulating the more-than-five-per cent-but-not-more-than-twenty-per cent shareholder-dealer are both sound and reasonable. The dealer realizes ordinary income without affecting the investor and the prevention of ordinary income from being converted into capital gains is accomplished.

**Hypothetical Dealers**

Subsection (e) gave birth to a new creature in federal tax law—the hypothetical dealer. If a person owns more than twenty per cent of the stock of a corporation and has engaged in certain specified corporate transactions within three years prior to the sale or exchange of his stock or liquidation of the corporation, he falls within this new category and, as such, can be denied the benefits of subsection (e). However, the imputation of hypothetical dealership status to a shareholder adversely affects only his tax liability and not that of any other shareholder.

Paraphrasing any part of subsection (e) necessarily sacrifices some accuracy, but, broadly speaking, a hypothetical dealer is a more-than-twenty-per cent shareholder who would be an actual dealer if his transactions were not on a corporate level. If the shareholder owns or during the preceding three years has owned more than twenty per cent of the outstanding stock of another corporation, seventy per cent of the assets of which were "similar or related in use or service"90 to seventy per cent of

---

89 See §§ 341(e)(1)(B), (2)(B).

90 This phrase is identical to the language used in the voluntary conversion provisions of § 1033 which provides for nonrecognition of gain if property is involuntarily converted into property "similar or related in service or use" to the property so converted. Courts have continually construed this standard narrowly under this section. See, e.g., McCaffrey v. Commissioner, 275 F.2d 27 (3d Cir.), cert. denied, 363 U.S. 828 (1960) (public parking lot not similar to rental warehouse); Clifton Invest. Co., 36 T.C. 569 (1961) (office building not similar to hotel building); Loco Realty Co., 35 T.C. 1059 (1961) (warehouse not
the assets of the instant corporation, and if, during the time which he held more than twenty per cent of the stock of the other corporation, either he sold or exchanged any part of his stock in the other corporation or the other corporation sold or exchanged property pursuant to a liquidation under section 337, he will be deemed a hypothetical dealer if the property imputed to him would render him a dealer in such property. The sales or exchanges of stock by the shareholder in the other corporation

similar to shoe factory). The consequence of having this term construed narrowly under subsection (e) would stifle the “hypothetical dealer” provision since under such a construction he would seldom be a shareholder in another corporation where 70% of the assets would be “similar” to the assets of the collapsible corporation.

However, in 1958, a regulation was adopted which provided that for purposes of applying § 1033, the replacement of involuntary converted property with property of “like kind” shall be treated as property “similar or related in service or use.” Treas. Reg. § 1.1033(g)-1 (1958) “Like kind” was taken from § 1031 which permits tax-free exchanges of property of “like kind.” The words “like kind” refer to the nature or character of property and have been construed broader than “similar or related in use or service.” See Commissioner v. Crichton, 122 F.2d 181 (5th Cir. 1941) (mineral rights similar to city lot); Treas. Reg. § 1.1031(a)-1(a) (1956) (property held for productive use may be exchanged for property held for investment). Cases under § 1033 since this regulation indicate that “similar” is to be construed broader than it was prior to the regulation, and is now analogous to the “like kind” requirement of § 1031. See Liant Record, Inc. v. Commissioner, 303 F.2d 326, 329 (2d Cir. 1962); Filippini v. United States, 200 F. Supp. 286 (N.D. Cal. 1961). Thus, when the drafters of subsection (e) included “similar or related in use or service” in the hypothetical dealer provision, they must have intended that this standard be broadly construed as this is the only way in which the “hypothetical dealer” provision of § 341(e) would be workable.

Another problem that arises under the hypothetical dealer provision is whether cash is to be treated as an asset of the other corporation which is “similar or related in use or service.” If cash is included, there will be much greater chance of having other corporations considered (because 70% of assets will be “similar”) even though a smaller portion of the fixed assets and activities of the corporations are related. If cash is excluded from “similar” assets, many corporations with related activities will not be considered because they happen to have a substantial amount of cash.

91 Section 341(e)(1)(C).
92 Section 341(e)(2)(C).
93 The operation of the hypothetical dealer provision of subsection (e) is illustrated by an example contained in the Senate Finance Committee report on § 341(e):

Assume that the sole asset of a corporation is appreciated land, and that the corporation is not a dealer in such property. If no shareholder of the corporation owning more than 20 percent of the corporation's stock is a dealer in such land (and if no more-than-20-percent shareholder owns, or has owned, within the preceding 3 years, more than 20 percent of the stock in a corporation more than 70 percent in value of whose assets are property similar or related in service or use to the assets of this corporation) then gain from sale of stock by any shareholder owning more than 20 percent of the corporation's stock will not come within the provisions of section 341(a).

are treated as if he sold or exchanged his proportionate share of the assets; and, similarly, a sale or exchange of assets by the other corporation pursuant to a section 337 liquidation is treated as if he sold or exchanged his proportionate share of the property. In this manner, the provision strips the shareholder of his corporate veil and views each transaction separately, thus making possible a determination as to whether the assets would be ordinary income assets on an individual level. If the shareholder has all the attributes of a hypothetical dealer, his “subsection (e) assets” include those assets of the corporation which comprise the assets that are “similar or related in service or use” to the seventy per cent of the assets of the other corporation. The net unrealized appreciation on the hypothetical dealer’s “subsection (e) assets” then goes into the numerator for purposes of his “fifteen per cent test.”

To illustrate the functioning of these provisions, assume A, B and C own a corporation which has no ordinary income assets. None of the three shareholders are actual dealers and neither A nor B is a hypothetical dealer. Therefore, there are no corporate “subsection (e) assets.” However, C, within the past three years, has had various corporate dealings which, under this provision, would make him a hypothetical dealer. Thus, C would have “subsection (e) assets” as to himself and the tax status of his gain would depend on whether he qualified under the “fifteen per cent test.” Regardless of C’s tax position, A and B would be subject to only capital gains rates since C’s status as a hypothetical dealer has no effect on the tax consequences of his co-shareholders.

Only a more-than twenty-per cent shareholder’s prior corporate history, and not his individual history, determines whether he is a hypothetical dealer. The exclusion of individual ventures stems from the fact that similar transactions on an individual basis would probably render the shareholder an actual dealer and his gains would be taxable as ordinary income under another part of subsection (e).

The approach that has been taken with respect to hypothetical dealers seems reasonable since one of the purposes of subsection (e) is to grant

94 Section 341(e)(1)(C)(i).
95 Section 341(e)(2)(C).
96 Section 341(e)(1)(C)(ii).
97 There may be occasions when the hypothetical dealer’s “subsection (e) assets” overlap, partially or completely, with the corporate “subsection (e) assets” in which case the numerator would be increased only by the net unrealized appreciation on the hypothetical dealer’s “subsection (e) assets” which were not also corporate “subsection (e) assets.” If the overlap were complete and the corporation had qualified under the “fifteen percent test,” the hypothetical dealer would, of course, also qualify.
relief to investors and deny it to dealers. Although a person, under existing law, can hide behind a corporate shield and escape dealership status, for purposes of this subsection, that person is, and should be, treated as an actual dealer even though he is not burdened with this stigma in other areas of the tax law. There exists no logical reason to allow such a person to avoid the onus of subsection (e) merely because his "dealership" transactions are corporate rather than individual.

Despite all its endeavors to prevent circumventions of the collapsible corporation provisions except under certain specified conditions, subsection (e) appears to have failed to close completely the tax avoidance door. Nothing in the new subsection prohibits a more-than-twenty-per cent dealer from selling enough of his stock to dip below the twenty per cent figure at which point he would no longer "taint" the entire corporation. Since a more-than five-per cent-but-not-more-than-twenty-per cent dealer does not affect the other shareholders, a more-than-twenty-per cent dealer could sell his stock to reduce his holdings to twenty per cent or less and save all other shareholders in the corporation (except possibly hypothetical dealers and more-than five-per cent-but-not-more-than twenty-per cent dealers) from being charged ordinary income rates on their gain. The dealer would not necessarily save himself since he ordinarily would have the same "subsection (e) assets" as when he was a more-than-twenty-per cent dealer (unless, of course, he lost some section 1231(b) assets because he was no longer a more-than-twenty-per cent dealer in such assets). In any event, these would not be corporate "subsection (e) assets" and, therefore, would not be included in the numerator of the non-dealers.

One danger lurking in the above theory is that of the "step-transaction."98 If a court closely scrutinized the reduction of stock ownership to twenty per cent or less, it might hold that the sale was only a part of a larger predetermined plan and disallow the separate effects which could result from a sale of stock by a more-than-twenty-per cent shareholder and, for instance, a subsequent liquidation under section 337. If the court refused to honor the sale, the effect would be that the more-than-twenty-per cent shareholder who had sold down to nineteen per cent would be deemed to own the original amount of stock at the time of

liquidation. Thus, he would be regarded as a more-than-twenty-per cent dealer and could possibly "taint" the corporation.

However, absent the application of the "step-transaction" theory, a dealer could save the other shareholders of the corporation under subsection (e). This result, however, is not directly contrary to the purpose of the statute in light of the fact that the more-than-twenty-per cent shareholder would be collapsed as to the amount of stock he sold to get to twenty per cent. Moreover, more than likely, the more-than-twenty-per cent dealer who has reduced his holdings would be subject to ordinary income rates on the stock which he retains and disposes of subsequently. This would result in ordinary income rates for the dealer and capital gain rates for the investor and would prevent the conversion of ordinary income into capital gains—consonant with the primary purpose of the new subsection.

The theory described above seems equally applicable to a hypothetical dealer. If a more-than-twenty-per cent shareholder were designated a hypothetical dealer, he could sell part of his stock to reduce his ownership to twenty per cent or below and on a subsequent sale or exchange of stock or liquidation no consideration would be given to the possibility of this shareholder being a hypothetical dealer because the test of determining hypothetical dealer status is not applied to a twenty-per cent-or-less shareholder. On the initial sale of part of his stock he would pay taxes at ordinary income rates unless he qualified under the "fifteen per cent test," but as to the gain from the remainder of his stock, he would be entitled to capital gain consequences. Therefore, if he could overcome the claim of "step-transaction," he would avoid ordinary income rates on his gain as to the last twenty per cent of his stock.

Situations to Which Subsection (e) Applies

Subsection (e) can be utilized by shareholders of collapsible corporations only in a certain few instances. Outside of a sale or exchange of stock, or a liquidation under either section 337 or 333, relief from collapsible sanctions is unavailable.

Sale or Exchange of Stock

When a shareholder sells his stock in a collapsible corporation he must satisfy each of the rules of subsection (e) relative to a shareholder of

---

99 Sections 341(e)(1)-(4).
his nature, whether he be a dealer, hypothetical dealer or an innocent investor. As has been seen, an innocent investor is subject to ordinary rates if the net unrealized appreciation on the corporate "subsection (e) assets" exceeds fifteen per cent of net worth. This would be true regardless of whether a more-than-twenty-per cent dealer who has "tainted" the corporation was simultaneously selling his interest in the corporation. Since the facts are as stated, an unintended result can occur. An investor can sell his stock in the corporation but, due to the existence of a more-than-twenty-per cent dealer, the investor will receive ordinary income treatment on the gain from his sale. Assume, however, that subsequent to the sale by the investor, but prior to sales by any other shareholder, the three year period recited by section 341(d) lapses. Thus, the investor's gain was taxable as ordinary income but the other shareholders' gain (including that of the more-than-twenty-per cent dealer who was responsible for the investor's plight) was taxable as capital gains because the collapsible corporation provisions no longer applied. This example only serves to point up another anomalous achievement of the collapsible corporation provisions.

Section 337 Liquidation

Although collapsible corporations were explicitly excluded from a liquidation under section 337, section 341(e)(4) now allows such a corporation to liquidate under section 337 if certain requirements are met. Gain or loss will not be recognized on the sale or exchange of property by a collapsible corporation if, at all times after the adoption of the plan of liquidation, the corporation satisfies the "fifteen per cent

---

100 Section 341(d) provides that "this section shall not apply . . . (3) to gains realized after the expiration of 3 years following the completion of . . . manufacture, construction, production, or purchase." § 341(d)(3).

101 Ibid.

102 Section 337(c)(1)(A) provides that: "this section shall not apply to any sale or exchange—made by a collapsible corporation . . . ."

103 Section 341(e)(4).

For purposes of section 337, a corporation shall not be considered to be a collapsible corporation with respect to any sale or exchange . . . within the 12-month period beginning on the date of the adoption of a plan of complete liquidation, if (A) at all times after the adoption of such plan, the net unrealized appreciation . . . does not exceed . . . 15 percent of the net worth . . . ,

(B) . . . the corporation sells substantially all of the properties . . . , and

(C) . . . no distribution is made of any property which . . . is property in respect of which a deduction for exhaustion, wear and tear, obsolescence, amortization, or depletion is allowable.

Ibid.
test,” and, if, during the period of liquidation the corporation sells “substantially all” of its assets to persons other than a more-than-twenty-per cent shareholder. An additional requirement is that there can be no distribution of depreciable or amortizable property, once again denying the possibility of a stepped-up basis. By containing a “no distribution” provision as well as a “substantially all” requirement, the statute thus prevents a corporation from selling “substantially all” of its assets and retaining only depreciable property to distribute to the shareholders.

Granting that these two provisions overlap somewhat, the “no distribution” clause is necessary to avoid permitting a stepped-up basis on property comprising the difference between all and substantially all. Also excluded from the nonrecognition of gain or loss provisions is any sale of depreciable property to a more-than-twenty-per cent shareholder or related person. However, such a sale will not completely disqualify the corporation from utilizing section 337 (as will failure to comply with the foregoing requirements); it only means that as to that particular sale gain or loss will be recognized. Finally, it should be noted that qualification under section 337 by the corporation does not automatically qualify the shareholder for relief. The “fifteen per cent test” must still be applied on a shareholder-by-shareholder basis.

The handling of the “fifteen per cent test” by the provisions of the section 337 exception seems somewhat baseless and impractical. Under the existing provisions, the corporation is refused section 337 treatment if, at the date of the adoption of the plan or anytime thereafter, the net unrealized appreciation on corporate “subsection (e) assets” exceeds fifteen per cent of the net worth. No prescribed times for the application of the “fifteen per cent test” with respect to complying with the provisions of section 337 are specified. It would seem more realistic, and, perhaps, make the statute more workable, to provide that the “fifteen per cent test” must be satisfied only when an asset is sold or otherwise disposed of. This would obviate the possibility of disqualification under subsection (e) merely because of market fluctuation between sales of assets. Moreover, if all of the corporate assets were sold simultaneously, this would be the only time when it would be necessary to qualify under the “fifteen per

104 Section 341(e)(4)(C).
105 Section 341(e)(4).
106 Section 341(e)(2). This is another of the exceptions contained in subsection (e) and provides for a shareholder-by-shareholder test once the requirements for a liquidation under section 337 are satisfied.
107 Section 341(e)(4)(A).
cent test." Neither would a corporation have to qualify at the date of the adoption of the plan of liquidation nor would it need qualify during the period when no assets were being sold. The desire of Congress to prevent persons from reaping too much profit would be achieved and at the same time the application of this subsection (e) exception would be facilitated.

If a collapsible corporation has recognized gain on the sale of assets prior to the adoption of a plan of liquidation under section 337, there exists the possibility of an offset against this gain which would save corporate taxes. Section 341(e)(4) provides that although gain or loss on the sale of a depreciable asset to a more-than-twenty-per cent shareholder will be recognized to the corporation, this type of sale will not automatically prevent qualification under the section 337 exception. Therefore, if a corporation has a depreciable asset which will realize a loss, this asset can be sold to a more-than-twenty-per cent shareholder and the loss will be recognized. The recognized loss will be set off against the gain which was recognized on transactions prior to adoption of the plan of liquidation, thus reducing corporate taxes. Subsection (e) contains no prohibition against this transaction so long as "substantially all" of the assets have been sold to purchasers other than a more-than-twenty-per cent shareholder. However, failure to satisfy the "substantially all" requirement, will of course, completely disqualify the corporation from the nonrecognition provisions of section 337.

Another beneficial effect to the shareholders when a plan such as the one outlined above is employed is that the sale of a "loss asset" which is also a "subsection (e) asset" neither increases nor decreases the numerator for purposes of the "fifteen per cent test." Since this is true, the corporation would be deriving the benefits of a double loss. First, the recognized loss offsets the recognized gain, and, secondly, unrealized depreciation has already decreased the unrealized appreciation to arrive at the net unrealized appreciation. Obviously, this was not an intended result, but the tax saving to the corporation and ultimately its shareholders is severely limited by the "substantially all" requirement contained in section 341(e)(4).

It would seem that a collapsible corporation with only several "subsection (e) assets" can always qualify under section 337. The statute does not provide any punitive measure for the simple sale of an asset by a corporation. The nature of the asset to the corporation determines whether the corporation pays tax at capital gains or ordinary income rates, and the tax status of the individual shareholder does not affect the corporation. Since the appreciation on the sale of assets prior to the
adoption of the plan of liquidation is not used in computing the numerator in the formula for purposes of a section 337 liquidation, the corporation could sell enough of its "subsection (e) assets" prior to the plan of liquidation to come within the "fifteen per cent test" and assure the applicability of the nonrecognition provisions of section 337 to the remainder of the assets.

However, the numerator, for purposes of the shareholder-by-shareholder test when the liquidation is complete, includes the unrealized appreciation on all "subsection (e) assets," even those disposed of prior to the adoption of the plan of liquidation. The reasons for excluding the appreciation for purposes of section 337 and including it for the shareholder tests are clear. As to the former, the statute is concerned only with the assets of the corporation from the adoption of the plan to the completion of the liquidation and is not involved with the history of the corporation. Furthermore, the collapsible corporation provisions are primarily aimed at the shareholders of the corporation and not at the corporation itself, and, as a result, relief to the corporation is not repulsive to the purpose of section 341.

However, as to the latter, if the appreciation were not included in the numerator for their individual tests, the shareholders would be assured of capital gains treatment both on the shareholder level and on the corporate level (unless the assets sold prior to the plan of liquidation were ordinary income assets to the corporation). This would result from the fact that the corporation must satisfy the "fifteen per cent test" before it can liquidate under section 337 and if the numerator were not recomputed, the prior sales of "subsection (e) assets" could be arranged so as to include enough appreciation which, if not included in the numerator for purposes of a shareholder-by-shareholder determination, would allow all the shareholders to qualify. In other words, there would be no "subsection (e) assets" for purposes of the numerator except those sold after the adoption of the plan of liquidation. Therefore, the corporation would pay tax at capital gains rates on the gain from the sale prior to adoption of the plan of liquidation (no tax at all on assets sold pursuant to section 337) and the shareholders, after guaranteeing qualification for everyone, would only be subject to capital gains rates on their entire gain even though a portion of it was attributable to property sold before the plan of liquidation and before they could qualify under the "fifteen per cent test."

108 Section 341(e)(4).
109 Section 341(e)(2).
To illustrate the foregoing explanation, consider the following example:

<table>
<thead>
<tr>
<th>Corporate Subsection (e)</th>
<th>Assets</th>
<th>Basis</th>
<th>Fair Market Value</th>
<th>Appreciation (Depreciation)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asset #1</td>
<td>$100</td>
<td>$200</td>
<td>$100</td>
<td></td>
</tr>
<tr>
<td>Asset #2</td>
<td>75</td>
<td>100</td>
<td>25</td>
<td></td>
</tr>
<tr>
<td>Asset #3</td>
<td>100</td>
<td>150</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>Asset #4</td>
<td>100</td>
<td>125</td>
<td>25</td>
<td></td>
</tr>
<tr>
<td>Asset #5</td>
<td>100</td>
<td>75</td>
<td>(25)</td>
<td></td>
</tr>
</tbody>
</table>

If all assets were included, the corporation would not qualify for liquidation under section 337 since the percent is 26.9 (175/650). Assume, however, that asset #1 is sold prior to the adoption of the plan of liquidation, the corporation realizing a taxable gain of one hundred dollars. The formula would then be 75/650 and the percentage 11.5, thus qualifying the corporation under section 337. Assets 2, 3 and 4 are sold to persons not connected with the corporation.

Since asset #5 is a "loss asset" it would benefit the corporation to sell it to a more-than-twenty-per cent shareholder in order to recognize the loss and offset it against the prior gain on asset #1 of one hundred dollars. Thus, the corporation would only pay capital gains rates on seventy-five dollars ($100 — $25).

Qualifying the corporation by the sale of asset #1 prior to the adoption of the plan of liquidation benefits only the corporation, not the shareholders. Upon completion of the liquidation, a shareholder-by-shareholder test must be made to determine which ones, if any, are entitled to capital gains rates. The one hundred-dollar gain on asset #1 is used in computing the numerator for this test. Under the facts given in this example no shareholder would qualify since the net unrealized appreciation of $175 exceeds fifteen per cent of the net worth (175/650 = 26.9%). As a result each shareholder (except those owning five per cent or less) suffers ordinary income tax consequences.

Section 333 Liquidation

The final exception in subsection (e)\(^{110}\) relates to a complete liquidation under section 333.\(^{111}\) Although section 333 expressly excludes col-

---

\(^{110}\) Section 341(e)(3).

\(^{111}\) Section 333(a)(2) provides that the liquidation must be completed within some one calendar month. In addition, the election to qualify under this section is only available if
lapsible corporations from its purview,112 subsection (e) makes it applicable if the "fifteen per cent test" is satisfied. However, for purposes of this exception, all assets which are ordinary income assets of the corporation or ordinary income assets to a more-than-five-per cent shareholder, not a more-than-twenty-per cent shareholder, are corporate "subsection (e) assets,"113 thus making it more difficult to qualify for relief. There is, however, no hypothetical dealer status with regard to a section 333 liquidation. Also, qualification of the corporation under the "fifteen per cent test" automatically qualifies all the shareholders under subsection (e) although the tax status of each shareholder's gain is then computed by means of a formula contained in section 333.114

The section 333 exception provides no prohibition against distributing depreciable property to the shareholders regardless of their stock ownership nor does it require that substantially all the assets be sold to persons other than a more-than-twenty-per cent shareholder. The factor which supposedly functions as a deterrent to the use of section 333 is that the corporation's accumulated earnings and profits are taxable to the shareholders on a pro rata basis, as ordinary income. Although this has resulted in an infrequent utilization of section 333 by normal corporations,115 this fact ordinarily will not deter its use by a collapsible corporation if the other facts would produce advantageous results since a collapsible corporation rarely accumulates much earnings and profits. As a result, one can expect collapsible corporations which qualify under the "fifteen per cent test" to liquidate under section 333 whenever the shareholders desire to distribute the depreciable property.116

Section 333 contains formulas which are used to compute ordinary
elections have been filed by shareholders owning "at least 80 percent of the total combined voting power . . . of all classes of stock entitled to vote . . . ." § 333(c)(1); § 333(a)(2).

112 Section 333(a).
113 Section 341(e)(5)(B).
114 Section 333(e).
115 Because of the drastic effect of taxing the accumulated earnings as a dividend at surtax rates to the shareholders at the time of the liquidation . . . it [section 333] has been used by shareholders only to a very limited extent. The advisory group understands that in the entire history of this provision only some 1500 corporations have elected to be governed by its rules.


116 It should be noted that a shareholder may possibly obtain a stepped-up basis, however, this is not the primary reason for pursuing a § 333 liquidation.
income\textsuperscript{117} and capital gains\textsuperscript{118} to the shareholder and section 334 contains a formula to compute the basis\textsuperscript{119} of the property distributed to the shareholder pursuant to a liquidation under section 333. Under these formulas a shareholder’s ratable share of the earnings and profits of the liquidating corporation is treated as a dividend and taxed to the shareholder at ordinary income rates. The remainder of the realized gain, to the extent to which it is recognized, is treated as a capital gain. However, the portion of the realized gain which is recognized is limited to the amount of cash and securities distributed to the shareholder. Thus, any of the realized gain resulting from the distribution of appreciated corporate assets (exclusive of cash and securities) will not be recognized to the shareholders. After the amount of recognized gain is determined, the basis of the distributed property to the taxpayer is computed by decreasing the basis of the stock by the amount of cash or securities received and increasing it by the amount of recognized gain.

To illustrate this sequence of events, assume that a corporation with a single shareholder has qualified for a section 333 liquidation under the “fifteen per cent test.” Assume further that it has $500 cash, a “subsection (e) asset” with a basis of $1,100 and a fair market value of $1,300, and earnings and profits of $100. The basis of the shareholder’s stock is $1,000. Thus, the realized gain, \textit{i.e.}, the amount by which the property distributed exceeds the shareholder’s basis for his stock, is $800 ($1,800 — $1,000). By applying the formula, we find that the $100 profit will be taxed at ordinary income rates (the shareholder’s ratable share of the earnings—in this case there is only one shareholder). To determine what portion of the total realized gain will be recognized it is necessary to compute the amount of cash (in this example there are no securities) distributed ($500). The excess of realized gain over the amount of cash distributed or $300 ($800 — $500) is not recognized. Of the $500 received in cash, $100 is taxed at ordinary income rates and the remainder ($400) is capital gains. The basis of the distributed property in the hands of the shareholder is the basis of the shareholder’s stock ($1,000) decreased by the amount of cash and securities distributed ($500) and increased by the amount of gain recognized ($500 = $400 at capital gains rates plus $100 at ordinary income rates). Therefore, the basis of the distributed property to the shareholder is $1,000 ($1,000 — $500 + $500) Thus,

\textsuperscript{117} Section 333(e) (1).
\textsuperscript{118} Section 333(e) (2).
\textsuperscript{119} Section 334(c).
since the basis of the "subsection (e) asset" to the corporation was $1,100, the shareholder does not receive a stepped-up basis.

Each shareholder is treated in the same way once the corporation has qualified for the section 333 exception; and any earnings and profits are taxed proportionately as ordinary income to the shareholders. Capital gains rates are allowed on the remainder of the recognized gain. Thus, unless a reason exists to distribute the depreciable property of the corporation, a collapsible corporation will derive very little benefit from a section 333 liquidation. Since the earnings and profits of the corporation will be ordinary income and the remainder of the recognized gain will be capital gains, a more favorable result could be accomplished by either a 337 liquidation or by a sale or exchange of stock and very likely there would be no gain taxable as ordinary income. The only type of shareholder who might suffer under another transaction but would be safe under a section 333 liquidation would be the hypothetical dealer. Therefore, it seems that section 333 will continue to serve a limited function in federal corporate tax law.

The Proposed Section 343

In December 1958 the Advisory Group on Subchapter C published its revised recommendations respecting collapsible corporations. The proposed statute, section 343, was designed to entirely replace section 341. The main purpose of the new section is to prevent the conversion of capital gains into ordinary income, and the two devices written into the statute to achieve this end are: (1) elimination of the subjective tests of section 341; and (2) fragmentation of the gain realized by the shareholder into ordinary income and capital gain.120

The former was to be accomplished by setting up two objective tests121 for determining a corporation's collapsibility, both of which would have to be satisfied before a corporation could qualify.122 As to the latter, if the corporation fails to qualify under the two tests, the gain of the

---

121 Under the proposed statute a corporation is deemed collapsible if: (1) the unrealized appreciation on its § 343 assets (generally ordinary income assets) is more than 15% of the net worth (excess of fair market value of all corporate assets over its liabilities) of the corporation; and (2) the unrealized appreciation on the corporation's § 343 assets exceeds 15% of the unrealized appreciation on all its assets. Id. at 42.
122 As in subsection (e) of § 341, if the corporation qualifies under § 343, the shareholders are generally entitled to capital gains rates.
individual shareholder would be taxable as ordinary income in an amount equal to his stock’s ratable share of the unrealized appreciation on “section 343 assets,” i.e., assets the sale of which would produce ordinary income. Thus, by the use of this fragmentation procedure, the corporate entity, in effect, would be disregarded in an effort to produce a fair and equitable treatment of the shareholders.

This, of course, is a more desirable result than the all-or-nothing approach taken by subsection (e). However, although the underlying philosophy of the statute is commendable and would obviate many of the problems of the present provisions, the statute is even more complex than existing law and, as a result its application would seem to portend new problems for everyone concerned.

CONCLUSION

Neither the provisions presently governing collapsible corporations nor the proposed revision has adequately remedied the ingenious methods of tax avoidance created by the taxpayer. In its piecemeal attempt to enact a statute which would prevent the use of the corporate form to convert what should be treated as ordinary income into capital gains,

123 Proposed § 343 takes a negative approach when defining § 343 assets. Thus, § 343 assets are any property of the corporation other than (A) money, (B) property (except § 1231(b) assets) which if sold would produce capital gain, (C) § 1231(b) assets, if there exists unrealized appreciation on all § 1231(b) assets considered in the aggregate, (D) property (other than inventory and stock of other collapsible corporations) 90% or more of the unadjusted basis of which consists of costs incurred by the taxpayer more than 3 years previously, and (E) normal inventory maintained and customarily sold by the corporation for a period of 3 years or more, exclusive of inventory which customarily increases in value by reason of aging for more than 6 months (e.g., whiskey). Revised Report of Advisory Group on Subchapter C of the Internal Revenue Code of 1954, op. cit. supra note 115, at 44.

124 Section 343 would also cover a situation where a person in the corporation was a dealer in assets of the corporation which were not corporate “§ 343 assets” by considering these “non-section 343 assets” as “§ 343 assets” for purposes of fragmenting the individual’s gain. See id. at 47.

125 The “fragmentation approach” looks through the corporate entity and treats the “ordinary income assets” of the corporation (§ 343 assets) as assets which would produce ordinary income in the hands of the individual shareholders. On the sale of stock by shareholders on distribution by the corporation, the pro rata share of the stockholder’s gain which is attributable to the unrealized appreciation of “ordinary income assets” of corporations would be taxed to him at ordinary income rates, while the remainder of his gain (which is attributable to the unrealized appreciation of the corporate assets which are not “ordinary income assets”) is taxed to him at capital gain rates. Thus, the shareholders gain is fragmented into ordinary income and capital gain.
Congress has not only made certain questionable concessions to "dealers" in allowing the conversion of ordinary income into capital gains, but at the same time it has seemingly punished the investor for his use of the corporate form by denying capital gains treatment where it ordinarily would be available.

Notwithstanding the complexity of the Advisory Group's proposals, it would seem that the ultimate solution must be based upon their approach which begins with the premise that with respect to the closely held corporation the individual shareholder's tax liability should be determined irrespective of his use of the corporate form. Such an approach would clearly avoid the injustice of denying the corporate investor the benefits of capital gains treatment when it should be made available to him. At the same time, since the closely held corporation is the only one under Congressional attack, it would also seem to accomplish the purposes of the present "collapsible corporation" provisions.

Joseph J. Hanna, Jr.
John A. Hoffman
G. Robert Wileman
RECENT DECISIONS

CORPORATIONS—A Corporation Is Not Guilty of the Criminal Conduct of Employees, Who, Although Ostensibly Acting Within the Scope of Their Employment, Are Acting With No Intent To Benefit Their Employer. Standard Oil Co. v. United States, 307 F.2d 120 (5th Cir. 1962).

The Pasotex Corporation operated pumping stations and pipelines for the purpose of gathering oil from various southwest Texas oil fields and transporting it to the refineries of the Standard Oil Company of Texas. Certain of these fields were operated under leases to Claude J. Thompson, Inc., while others were operated by Standard.

In a scheme devised to permit the Thompson wells to receive credit for the maximum production permitted under Texas regulation, which they were incapable of achieving, certain Pasotex employees at the pumping stations were induced by Thompson to falsify their records. In some instances, they credited oil overproduced by one Thompson well to another less productive Thompson well. In other instances, they credited Thompson with oil drawn from the Standard wells, the Standard employees at the pumping station acquiescing in the falsification.

The three corporations, along with several individual defendants, were subsequently indicted for a knowing violation of the Connally Hot Oil Act which forbids interstate transportation of oil produced in violation of state regulation. The trial court rejected the argument that the employees were not operating within the scope of their employment and the corporations were convicted. On appeal, the convictions of Standard and Pasotex were reversed. Held, a corporation is not guilty of the criminal conduct of employees, who, although ostensibly acting within the scope of their employment, are acting with no intent to benefit their employer.

While the question of whether a corporation can be found guilty of a criminal act was affirmatively resolved in New York Cent. & H.R.R.R. v. United States, debate has since raged as to the corollary of this question: Under what circumstances will the criminal acts of the agent be imputed to the corporate master? The tendency since the decision in New York Central has been to place less and less emphasis upon the individual’s position in the corporate structure, and more upon the determination of whether he is performing, or at least appears to be performing, his assigned duties, even though in a criminal manner.

4 Standard Oil Co. v. United States, 307 F.2d 120 (5th Cir. 1962).
5 212 U.S. 481 (1909).
6 E.g., United States v. Steiner Plastics Co., 231 F.2d 149 (2d Cir. 1956); St. Johnsbury
Although the language of some decisions has indicated that in the performance of these assigned duties, the agent must also be acting with an intent to benefit the corporation before his criminal acts will be imputed to it, the courts have generally tended to disregard the element of intent in favor of a more objective standard of liability. Thus, in *Old Monastery Co. v. United States*, the court summarily rejected the corporate defense that the acts of its president in selling liquor at prices in excess of wartime ceilings not only had not benefited the corporation, but actually had worked a detriment to it. In finding the corporation guilty on the grounds that, in selling the liquor, its president was performing his corporate functions, the court stated simply: "We do not accept benefit as a touchstone of criminal liability; benefit, at best, is an evidential, not an operative fact."

In *C.I.T. Corp. v. United States* the court carried this logic a step further and precluded even a consideration of the agent's intention to benefit the corporation as a determinant of corporate criminal liability by its statement that such liability was determined by "the function delegated to the corporate officer or agent." Similarly, *United States v. Steiner Plastics Mfg. Co.* held that "it is enough to show that the agents of the corporation acting within the area entrusted to them had violated the law."

On the other hand, New York, in a lower court decision has taken a somewhat more realistic position and has balanced the importance of benefit with the position of the agent within the corporate framework to arrive at an index of corporate intent. In *People v. Raphael*, a superintendent of an apartment house, as a condition precedent to leasing apartments took and pocketed bonuses from prospective tenants without his employer's knowledge. In acquitting the corporate employer for this violation of the Administrative Code of New York City, the court stated that corporate criminal liability may be imposed under any one of five conditions:

Trucking Co. v. United States, 220 F.2d 393 (1st Cir. 1955); United States v. George F. Fish Inc., 154 F.2d 798 (2d Cir.), cert. denied, 328 U.S. 869 (1946); C.I.T. Corp. v. United States, 150 F.2d 85 (9th Cir. 1945); Egan v. United States, 137 F.2d 369 (8th Cir. 1943).


8 147 F.2d 905 (4th Cir. 1945).

9 Id. at 908.

10 150 F.2d 85 (9th Cir. 1945).

11 Id. at 89.

12 231 F.2d 149, 153. (2d Cir. 1956).


14 N.Y.C. Admin. Code § U41-4.0(d) (1942).
[W]hen (1) the corporation has benefited or profited from the crime, or (2) its officers participated in the crime, or (3) its officers authorized, sanctioned or acquiesced in the commission of the crime by the agent or employee, or (4) it had knowledge of the crime, or (5) it was chargeable with negligence in not obtaining such knowledge, through reasonable inquiry.\textsuperscript{15}

However, even under this rule the court would go no further in determining the intent of the employee than to view the effect of his act upon the corporate interest. And, where a corporate officer was involved, his intent to benefit the corporation would be conclusively presumed. Thus, the Raphael court, while contrary to \textit{Old Monastery} in its consideration of benefit as an operative, rather than evidential, fact, formulated a rule just as objective as those set out by the courts purporting to look only at the function of the agent.

In deciding the instant case, the lower court applied the objective standards of liability, and combining the phraseology of \textit{Old Monastery} and \textit{C.I.T.} held that in determining corporate culpability “the touchstone is the function of the employee.”\textsuperscript{18} Consequently, the trial court was able to dismiss not only the fact that, in committing their criminal acts, the Pasotex employees acted with no intent to benefit their employer, but also the fact that the crime of the Standard employees consisted only of their acquiescence to the theft of their employer's oil. In reversing, however, the instant court not only correctly recognized the anomaly of the Standard conviction, but also went further to absolve Pasotex on the grounds that the benefits which accrued to it were merely incidental to the employees' intent to “aid Thompson in his criminal enterprise.”\textsuperscript{17}

In so deciding, the court has gone against the trend of the prior decisions, not by a renunciation of their principles, but by a reapplication of them. As did \textit{Old Monastery}, this court denied benefit as the touchstone of corporate liability, but while \textit{Old Monastery} has been interpreted as indicating that benefit was evidential only of \textit{corporate} intent, the instant case has made it evidential of “the purpose and motive for which the agent does the act in question.”\textsuperscript{18} In turn, it is this intent of the agent which the \textit{Standard} court made determinative of the liability of the corporate employer. If the agent's criminal act is done for the purpose of furthering the interest of the corporation, then his act is that of the corporation. But where the agents perform their usual tasks, not to further or advance the interest of the employer, but to further the interests of themselves or another, the mere fact of a resultant benefit to the employer will not support an inference of guilt.\textsuperscript{19}

It would appear, therefore, that the court has created a rule even broader than that formulated in \textit{Raphael}, for under the rule of that case the court would

\begin{itemize}
\item \textsuperscript{15} 190 Misc. at 584, 72 N.Y.S.2d at 750.
\item \textsuperscript{16} 196 F. Supp. at 574.
\item \textsuperscript{17} 307 F.2d at 129.
\item \textsuperscript{18} Id. at 128.
\item \textsuperscript{19} Id. at 128-29.
\end{itemize}
have found it unnecessary to inquire into the question of the employee's intent if a direct benefit had accrued. Additionally, while the instant court purports to be applying the "principles governing civil liability," they appear to be disregarding, at least insofar as the conduct of the Pasotex employees is concerned, the "dual function" rule, i.e., that liability will be imposed upon the master whenever the conduct was done in part to serve his purpose regardless of whether it also serves the interests of another.

In evaluating the scope of the court's decision, it is well to bear in mind that the Connally Hot Oil Act, although defining a statutory crime, is one which requires a general criminal intent. Thus, the court's decision should have no effect upon the so-called "welfare" statutes which impose a strict criminal liability upon the offender. In those cases, since the legislature has deemed that the forbidden act, no matter how innocently committed, is to be the sole determinant of guilt, the purpose of the employee, so long as he was performing his delegated duties, is not seen to be of great import in implicating or absolving the employer.

Consideration should also be given to the fact that the individuals in this case were relatively low in the corporate hierarchy. While it has been repeatedly held that the employee's position will not affect the corporation's liability, it would seem reasonable that a finding of an intent to benefit would become more probable as the rank of the individual wrongdoer increased.

Despite these qualifications, it is believed that the instant court has taken a major step in limiting the tendency to apply mechanical rules of liability to corporate criminal cases, and, if these qualifications are observed, the court's conclusions are believed to be sound. Though the court appears to have adopted a rule which imposes upon the government a burden of proof stricter than that required in civil cases, in view of the different principles upon which the two forms of liability are founded, the imposition does not seem to be an unreasonable one.

MONROE J. MIZEL

20 Id. at 127.
24 See Auerbach Shoe Co. v. Commissioner, 216 F.2d 693, 697 (1st Cir. 1954).
An employee of the United States was injured when he slipped and fell on a walkway provided by the defendant who was under contract to provide and maintain the walkway in good condition. Following the accident the injured employee and a witness made statements to their superior who, pursuant to the Federal Employees’ Compensation Act, filed a report which contained an account of the accident as reported by the injured employee, a signed statement made by the witness, and the superior’s own observation of the condition of the walkway. Subsequently, the United States Government, as assignee of the employee’s claim, brought suit contending that defendant’s failure to remove ice and snow was the cause of the injury. At trial, the plaintiff offered the superior’s report in evidence, contending that it was admissible under the Federal Business Records Act as a record made in the “regular course of business.” The court admitted it over objection. However, the report was neither shown nor read to the jury, and before charging the jury, the court, reversing its earlier ruling, held the report inadmissible. Held, an accident report required

1 Section 24, 39 Stat. 747 (1916), as amended, 5 U.S.C. § 774(a) (Supp. II 1959-1960), provides:

Immediately after an injury to an employee resulting in his death or his probable disability, his immediate superior shall make a report to the Secretary containing such information as the Secretary may require, and shall thereafter make such supplementary reports as the Secretary may require.


If an injury or death for which compensation is payable under §§ 751-756, 757-781, 783-791 and 793 of this title is caused under circumstances creating a legal liability upon some person other than the United States to pay damages therefor, the Secretary may require the beneficiary to assign to the United States any right of action he may have to enforce such liability . . . .

3 28 U.S.C. § 1732(a) (1958) (hereinafter referred to as FBRA) provides:

(a) In any court of the United States and in any court established by Act of Congress, any writing or record, whether in the form of an entry in a book or otherwise, made as a memorandum or record of any act, transaction, occurrence, or event, shall be admissible as evidence of such act, transaction, occurrence, or event, if made in regular course of any business, and if it was the regular course of such business to make such memorandum or record at the time of such act, transaction, occurrence, or event or within a reasonable time thereafter.

All other circumstances of the making of such writing or record, including lack of personal knowledge by the entrant or maker, may be shown to affect its weight, but such circumstances shall not affect its admissibility.

The term “business,” as used in this section, includes business, profession, occupation and calling of every kind.
by federal statute and made by an agent of the party offering it into evidence is admissible as a record made "in the regular course of business" under the Federal Business Records Act.4

The common law business records exception to the hearsay rule was based on the absence of a strong motive to misrepresent. Thus, where the records were prepared solely for the purpose of accurately recording the day-to-day activities of the business, the absence of any motive to misrepresent led the courts to hold the records admissible under the exception.5 Where, however, the records were prepared in anticipation of future litigation, the presence of such a motive generally resulted in their exclusion from evidence.6

Since the passage of the Federal Business Records Act the question of the admissibility of business records has been before the federal courts on several occasions, the leading case being Palmer v. Hoffman.7 In that case an accident report prepared by an employee of the offering party pursuant to the employer's regulations was held inadmissible under the Act. Judge Frank speaking for the United States Court of Appeals for the Second Circuit in that case concluded that the words "regular course of business" in the FBRA were not to be interpreted in the ordinary sense but were words of art taking their meaning from the common law.8 It was the opinion of that court that the only intent of Congress in passing the FBRA was to eliminate verification by the maker, necessary at common law, and not to change the nature of the record admitted.9 Therefore, under the FBRA, as interpreted by the Court of Appeals for the Second Circuit, a record would be admissible only where the circumstances would show reliability.10

In the Supreme Court, however, the case received a different treatment. Mr. Justice Douglas, reluctant to follow the reasoning of Judge Frank avoided stating that trustworthiness and reliability were the criteria. Instead, the Court held that the accident report was not a record made in the "regular course of business" because it was not connected with the inherent nature of the business, the business of the offering party being railroading, not causing accidents.11 The Court was apparently concerned with the subjective nature of the common law tests to assess trustworthiness, and attempted to remedy the problem by requiring that the document bear a certain relation to the business enterprise.

---

6 United States v. Becker, 62 F.2d 1007 (2d Cir. 1933) (express company records); United States v. Cotter, 60 F.2d 689 (2d Cir. 1932) (bank records).
7 318 U.S. 109 (1943), affirming 129 F.2d 976 (2d Cir. 1942).
8 129 F.2d at 983.
9 Id. at 989.
10 Id. at 991.
11 318 U.S. at 114.
The Court concluded that the words "regular course of business" referred to the day-to-day systematic recording of the "conduct of the business as a business," as exemplified by the keeping of such records as "payrolls, accounts receivable, accounts payable, bills of lading and the like" in which the accuracy required by good business practice provides an internal check against misstatements.

In the instant case the court held admissible an accident report very similar to the one rejected by the Supreme Court in Palmer, and in so doing it again endorsed a subjective test of trustworthiness as the determinant of admissibility under the FBRA. To achieve this result, the court first distinguished the inherent nature test of Palmer on the grounds that the Palmer Court was "obviously . . . concerned about a likely untrustworthiness of materials prepared specifically by a prospective litigant for courtroom use." This court then proceeded to decide the case in accordance with a liberal construction of the language and policy of the FBRA.

The cases in the Second Circuit, after Palmer, support the conclusions of the instant court that the test is one of subjective trustworthiness. These cases, using trustworthiness as the criterion, have liberally applied the FBRA and thus have allowed the admission of documents and records that would not have been admissible under the test established by the Supreme Court in Palmer. However, none of these cases have gone so far as to hold admissible under the Act an accident report made by an agent of the offering party. Thus, by admitting the report in the instant case, the court has culminated a gradual but significant trend away from the test announced by the Supreme Court in Palmer.

In making this final step the Trade Zone court initially laid down only two requirements for admissibility: first, that the record be a business record in the ordinary sense of that term as used by businessmen; and, second, that the record appear to have a minimal trustworthiness. In its finding that the records in question met this requisite reliability, the court quite correctly made no attempt to relate the making of an accident report to the inherent nature of the Government's business or to distinguish the facts in Trade Zone from those in Palmer on the grounds that the report in the instant case was prepared by an agent of the government pursuant to federal statute. Rather, it based its finding principally upon the fact that the accident report was not prepared primarily for litigation between the Government and the pier owner and, there-

---

12 Id. at 115.
13 Id. at 114.
14 304 F.2d at 797.
16 304 F.2d at 796.
fore, it was not clearly self-serving and untrustworthy.\textsuperscript{17} It reasoned that the fact that litigation was possible was not enough to show that the document was unreliable because all documents in business are prepared with the knowledge that litigation might result. Only where the document was prepared primarily for litigation would the self-serving nature become clearly evident.

The court conceded, however, that this report might not be admissible in litigation between the injured party and the Government because made in contemplation of that claim. Yet, the court goes on to point out that its possible inadmissibility in this regard does not preclude its admissibility in suits, such as the instant one, between the Government and a third party since the latter cases would involve different issues from those which would be raised by the former.\textsuperscript{18} Such a conclusion, however, appears to overlook the fact that this report was required by the Government under a statute which, in addition to providing a compensation scheme for injured employees, also contained a provision by which the Government became subrogated to the rights of the injured party.\textsuperscript{19} Under such circumstances it is difficult to see how the report if not credible in regard to the one suit, would be credible in another where basically the same facts will be in issue. By addressing itself to the question of whether the report was primarily prepared for litigation in the instant suit alone, the court has thus allowed the admission of a record which by traditional standards appears, at best, to be of minimal reliability.

Moreover, it is with little success that the court attempts to bolster the admission in this case on the ground that here the maker of the report had been on the stand and could have been subjected to cross-examination as to the contents of the report.\textsuperscript{20} For this ignores the fact that the report was sought to be introduced under the FBRA which does not require the maker to testify. Thus, the fact that the maker was subject to cross-examination as to the contents should not affect the admissibility under the terms of the statute, especially where the maker did not so testify although he was on the stand.

In evaluating the decision of the \textit{Trade Zone} court it is difficult to avoid concluding that the Supreme Court's decision in \textit{Palmer} was not intended to be a general authorization for the courts to determine the trustworthiness of a particular document. Judge Clark's dissent in the Court of Appeals' opinion in \textit{Palmer}\textsuperscript{21} expressly noted that the test of trustworthiness was too subjective and amounted to only a preliminary guess as to the existence of a strong motive to misrepresent. It would seem that by stating that the FBRA only applied to records which are necessary for the systematic day-to-day conduct of the business as a business, the Supreme Court was directly answering Judge Clark's

\textsuperscript{17} Id. at 797.
\textsuperscript{18} Ibid.
\textsuperscript{20} 304 F.2d at 792.
\textsuperscript{21} 129 F.2d at 998.
objection by providing objective standards for determining admissibility which would eliminate the necessity for guesswork on the part of the trial court.

However, while the line of reasoning followed by the instant court is subject to criticism, the result itself demands commendation. The result indicates that the court is willing, when given the opportunity, to liberalize the FBRA and thus expand the limits of admissibility for business records. While the Supreme Court in Palmer restricted the FBRA to a much narrower interpretation than this court has given it, the Palmer decision has been criticized for so doing. Judge Clark in his dissenting opinion in Palmer and in his concurring opinion in Trade Zone, in suggesting that the common law should not be read into the FBRA, also suggested that records made in the "regular course of business" in the ordinary business sense of the phrase should be admitted. He believes that it is imperative to get all the relevant material into the trial, and that the FBRA should be interpreted with this purpose in mind. Similarly, the words of the statute would seem to indicate that a more liberal interpretation should be given to the FBRA especially in the light of the phrase of part (a) of the act which states: "All other circumstances of the making of such writing or record, including lack of personal knowledge by the entrant or maker, may be shown to affect its weight, but such circumstances shall not affect its admissibility." Finally, since it is permissible in a federal court for the judge to comment upon such evidence once it is admitted, the proper probative value may be attributed to records, such as those in the instant case, by having the judge warn the jury that it may not be as reliable as evidence subject to cross-examination.

Trade Zone, while perpetuating a broadened interpretation of admissibility under the FBRA, takes it one step further by admitting into evidence under it a report made by the party offering it, even when the report was made with the knowledge that future litigation was possible. As such it clearly appears to endorse a criterion of minimal trustworthiness for admissions under the Act. It must remain for the future to see whether the Supreme Court will adopt this desirable trend or whether Congress will undertake to ratify it by amendment.

WILLIAM RAY FRIEDMAN


Appellant Killough was taken to police headquarters and questioned about the disappearance of his wife. After two days of questioning, during which time

23 129 F.2d at 998.
24 304 F.2d at 799.
Killough asserted his constitutional right against self-incrimination, he confessed to the murder of his wife. After this confession, he was finally arraigned before the United States Commissioner, pursuant to Rule 5(a) of the Federal Rules of Criminal Procedure. The following day, while in the District of Columbia jail, Killough consented to talk with an officer, who had participated in the earlier interrogation, concerning the disposition of his wife's body. During their conversation an attorney, an acquaintance of Killough's, offered his services which Killough declined, stating that other arrangements had already been made. At this time, some twenty hours after the preliminary hearing, Killough reaffirmed his earlier confession.

Killough was subsequently indicted for first degree murder. At the trial in the District Court the pre-hearing confession was excluded under the Mallory exclusionary rule. However, the second confession was admitted and Killough was convicted of manslaughter. The Court of Appeals reversed the conviction. Held, a confession elicited during an illegal detention renders inadmissible a second confession obtained twenty hours later but before the accused had conferred with counsel.

The exclusionary rule first enunciated in *McNabb v. United States* and later refined and limited in *Upshaw v. United States*, *Mitchell v. United States* and *Mallory v. United States*, makes inadmissible in federal prosecutions any statement obtained during the period in which the detention of the accused is in violation of Rule 5(a) of the Federal Rules of Criminal Procedure. However, this so-called "Mallory Rule" has generally been applied only to statements directly concerning the commission of the crime alleged which were made prior to the time the arrestee was arraigned before a committing magistrate. Thus,

---

2. Rule 5, Proceedings Before the Commissioner.
3. (a) Appearance Before the Commissioner. An officer making an arrest under a warrant issued upon a complaint or any person making an arrest without a warrant shall take the arrested person without unnecessary delay before the nearest available commissioner or before any other nearby officer empowered to commit persons charged with offenses against the laws of the United States. When a person arrested without a warrant is brought before a commissioner or other officer, a complaint shall be filed forthwith.
4. (b) Statement by the Commissioner. The commissioner shall inform the defendant of the complaint against him, of his right to retain counsel and of his right to have a preliminary examination. He shall also inform the defendant that he is not required to make a statement and that any statement made by him may be used against him. The commissioner shall allow the defendant reasonable time and opportunity to consult counsel and shall admit the defendant to bail as provided in these rules.
8. 318 U.S. 332 (1943).
statements concerning circumstances collateral to the crime, obtained during illegal detention, are admissible to impeach the accused’s testimony on the stand. A person who has identified the defendant during a period of illegal detention is allowed to identify him in open court, though evidence of the earlier identification is inadmissible. And a confession made to one crime while being legally detained for another crime is admissible though there has been no arraignment for the admitted crime.

In the area of reaffirmations of illegally obtained confessions, the Supreme Court has intimated that the “fruit of the poisonous tree” doctrine is of only limited applicability. Emphasizing this in United States v. Bayer, the Court said: “But this Court has never gone so far as to hold that making a confession under circumstances which preclude its use, perpetually disables the confessor from making a usable one after those conditions have been removed.” Three recent cases before the Court of Appeals for the District of Columbia Circuit have shed some light on just how long after the illegal “conditions” have been removed the exclusionary rule applies. Since the purpose of the Mallory Rule is to deter the police from improper conduct in violation of Rule 5(a), these decisions have necessarily turned on the question of whether the post-hearing confession was independent of the police wrongdoing in procuring the earlier confession.

In Jackson v. United States (the first Jackson case) the court held inadmissible a confession procured by having the defendant sign, immediately after the hearing, statements made during illegal detention, since it was not independent of the illegally obtained confession. However, in Jackson v. United States (the second Jackson case) the court ruled admissible an oral confession given two days after the hearing when the defendant had been advised of his right to remain silent by both judge and counsel. Similarly, in Goldsmith v. United States the court held that a confession, obtained after arraignment and after the advice of both magistrate and counsel, and confirming an inadmissible confession made before arraignment, is itself admissible and does not violate the Mallory Rule. In distinguishing these cases from the first Jackson case, the courts in Goldsmith and the second Jackson case relied heavily upon the fact

15 Supra note 14, at 540.
that in both cases the accused actually had the advice of counsel,20 who presumably advised the accused not only of his constitutional rights, but informed him that the earlier confession could not be used against him.

In the instant case the court considered the circumstances surrounding Killough's post-hearing confession to determine whether the confession was a product of the first confession and as such inadmissible, or whether it was indeed an independent statement, untainted by the illegality which vitiated the earlier confession. Judge Fahy summarizes the holding thus: "[W]e hold here, that a reaffirming confession which, though it followed a hearing, was made soon after an earlier confession obtained during unlawful detention which preceded the hearing was 'a result' of that illegality and must be excluded."21 The majority emphasizes two factors to support this view: 1.) Killough did not actually have the advice of counsel, and 2.) only twenty hours separated the second confession from the arraignment when Killough was first advised of his rights.

As to the first point, the majority expressly distinguishes this case from Goldsmith and the second Jackson case because in both of those cases the defendants actually had the advice of counsel before making their reaffirming confessions. While admitting that Killough had been fully advised of his right to obtain counsel, the majority recognized the vast difference between merely being aware of this right and actually having the advice of counsel. Unfortunately, the court itself substantially impairs the effectiveness of this argument in sustaining the holding by stating: "[N]owhere have we said that a post-hearing confession . . . must necessarily await the entry of counsel . . . ."22 Furthermore, the majority expresses a willingness, had the circumstances here required it, to reexamine the second Jackson and the Goldsmith cases23 and Judge Wright, concurring, is prepared to overrule them.24

However, in relating the two confessions in the instant case, the majority chose to rely primarily, if not exclusively, on the time element involved. Judge Fahy calls the twenty hour period separating the confessions "the decisive factor in this case."25 Judge Burger, dissenting, says that the majority makes time the "sole test."26 And after disclaiming any necessity for the intervention of counsel, the majority adds: "[W]e [do not] predetermine that the passage of no amount of time could remove the taint [of the confession]"27—thereby implying that in this case the passage of only twenty hours was paramount in determining that the taint had not been removed.

22 Id. at 11.
23 Id. at 6.
24 Id. at 15.
25 Id. at 11.
26 Id. at 25.
27 Id. at 11-12.
Finally, the majority also alludes to the issue of police attempts to subvert the exclusionary rule by pointing out that the officer who obtained both confessions was aware of prior cases in which reaffirming confessions were held admissible, though earlier pre-hearing confessions were inadmissible. But no real attempt is made to make this factor a supporting pillar of the holding.

By its holding the court places the instant case somewhere between the first and second Jackson cases. It extends to twenty hours the time period after arraignment during which admissible statements cannot be obtained from the accused, whereas in the first Jackson case the second confession was obtained immediately after the hearing. Moreover, in discounting considerable evidence that Killough’s second confession was indeed independent of the first, the court seems to have invoked a mechanical rule which refuses even to admit evidence establishing the independence of such a confession whenever that confession is made within twenty hours of the arraignment hearing.

The majority regards this holding as absolutely necessary if the Mallory Rule is to be preserved as an effective deterrent to improper police methods. They attribute the vigorous dissent to a dissatisfaction with the exclusionary rule itself. The use of the Mallory Rule as a means of reforming police methods at the expense of efficiency in crime detection is indeed open to serious question. But that rule is now a well established law of evidence in the federal courts. If it is to have its intended effect, the courts must discourage police procedures which, while paying lip service to the rule, violate the congressional mandate of Rule 5. Prior to the Killough decision, it was possible for the police, when they knew an illegal detention had been affected, to visit the accused soon after arraignment (and preferably before the assistance of counsel was available to the accused) to obtain reaffirmation of statements made during the illegal detention. This case eliminates that tactic as an effective means of gathering evidence.

Although it is possible to view the holding of this case as attaining a desirable result, it is submitted that the majority opinion does much to obfuscate an area of law already in a state of turmoil. By relying so heavily upon the time element, the court obscures the fact that in determining the admissibility of a reaffirmation of an earlier illegal confession the ultimate question is not when the reaffirmation was made, but whether it was independent of the earlier confession. By making the time element the determinative factor, the court greatly minimizes the importance of the single most relevant factor in establishing a reaffirming confession as independent—the knowledge of the accused that his earlier confession cannot be used against him.

It is suggested that a more practical solution to the problem of police avoid-

---

28 See id. at 13-14.
PRIVILEGED COMMUNICATIONS—THE ABSENCE OF CONFIDENTIALITY

In an anti-trust suit in a federal court the plaintiff, Radiant Burners, Inc., sought production of eight letters originally given to defendant's former counsel, and subsequently conveyed to its current trial counsel. Since these letters were allegedly written in anticipation of the present litigation, defendant invoked the attorney-client privilege and the work-product doctrine to prevent discovery. The United States District Court for the Northern District of Illinois determined that neither defense was valid and ordered the letters delivered to plaintiff. Held, the absence of confidentiality prevents application of the attorney-client privilege to corporations, though the application of the work-product doctrine is in no manner affected by the identity of the client.¹

The attorney-client privilege is based fundamentally on considerations of public policy, and on the necessity that clients should feel free to communicate with their attorneys about their problem "without fear of consequences or the apprehension of disclosure."² Although the courts have long realized the importance of this objective, they have also realized that its exercise, in any form, tends to suppress investigation and eventual disclosure of the truth.³ Therefore, there is much authority holding that the privilege should be confined to its narrowest limits.⁴ The inherent tendency of courts confronted with the problem

² Modern Woodmen of America v. Watkins, 132 F.2d 352, 354 (5th Cir. 1942).
³ City and County of San Francisco v. Superior Court, 37 Cal. 2d 227, 235, 231 P.2d 26, 30 (1951).
⁴ E.g., Prichard v. United States, 181 F.2d 326, 328 (6th Cir.), aff'd per curiam, 339 U.S.
is to endeavor to balance these diametrically opposed interests. Most courts thus require as an essential prerequisite to the application of the privilege that the injury to the attorney-client relationship which would result from disclosure be greater than the benefit to be gained from correct disposal of the litigation.\textsuperscript{5}

Although in making this determination the courts in the past have generally refrained from questioning whether the corporation-attorney relationship is one which should be sedulously fostered to the same degree as the individual client-attorney relationship, this consideration was the deeper issue involved in the case of \textit{Le Fever v. Lejkowits}.\textsuperscript{6} Although the court in that case denied the privilege to a corporation which had transferred certain business records to its attorney in contemplation of litigation on the ground that this transfer was a purely defensive measure, it also implied that the scope of the protection afforded by the privilege is to some degree dependent on the nature of the entity asserting it.\textsuperscript{7} Thus, it would seem that this final question must be considered together with traditional notions delineating the subject matter of the privilege, before its scope in the corporate atmosphere can be determined.

Despite these implications found in \textit{Le Fever}, the judiciary has historically refused to consider the special problems presented by the corporate assertion of the privilege in applying it without discussion to corporate clients.\textsuperscript{8} In reaching its decision, therefore, the \textit{Radiant Burners} court was the first to directly explore the basic question of whether the attorney-client privilege \textit{should} be extended to corporations.

Chief Judge Campbell, speaking for the court in \textit{Radiant Burners}, rested his denial of the corporate privilege on two principal grounds. First, he stressed the personal character of the attorney-client relationship, relating it to the common law and constitutional privilege against self-incrimination.\textsuperscript{9} It has been held with near unanimity that a collective group, whether or not incorporated, has no standing to assert the self-incrimination privilege.\textsuperscript{10} However, while the facts


\textsuperscript{6} 18 Misc. 2d 278, 178 N.Y.S.2d 172 (Sup. Ct. 1958).

\textsuperscript{7} See Id. at 280-81, 284-85, 178 N.Y.S.2d at 174-75, 178-79.


\textsuperscript{9} 207 F. Supp. at 773.

\textsuperscript{10} Wilson v. United States, 221 U.S. 361 (1911); Hale v. Henkel, 201 U.S. 43, 74-75
that the self-incrimination and attorney-client privileges are both essentially personal in theory and have similar historical backgrounds led Judge Campbell to equate the two, it is nevertheless true that the respective policies underlying each privilege are quite different. Whereas the one seeks to protect private persons from forced disclosures,\(^\text{11}\) the other seeks to promote free and confidential communication between client and attorney.\(^\text{12}\) Consequently, to hold that because the former is restricted to natural persons, the latter should be similarly limited, is to strain somewhat the limits of historical analogy.

The stronger reason for denying the corporation the attorney-client privilege is the second ground upon which the instant court relied, namely, the fact that the relationship between an attorney and a large corporation simply does not possess the confidentiality that the privilege was designed to protect. It is widely accepted that the communication must be confidential\(^\text{13}\) and must be intended to be so when made;\(^\text{14}\) therefore, the presence of third persons defeats this requirement.\(^\text{15}\) However, in applying the privilege to the corporate client, the courts in the past have relaxed this confidentiality requirement by resort to the doctrine that agents of either the attorney or the client are excluded from the secrecy rule.\(^\text{16}\) This is perhaps because of judicial recognition of the obvious —that the functions of agents are requisite to smooth commercial intercourse. Confronted with these considerations, the New Jersey court in Stewart Equip. Co. v. Gallo\(^\text{17}\) found no difficulty in applying this doctrine to highly placed corporate agents who made the confidential communications to counsel, since “a corporation can act only through its agent.”\(^\text{18}\)

However, in rejecting this relaxation of the confidentiality requirement, the court in Radiant Burners pointed to the abject disregard of the secrecy rule where the scope of the agency is widened, as it necessarily must be in large

\(^\text{11}\) United States v. White, supra note 10, at 698; 8 Wigmore, Evidence § 2259a, at 353 (McNaughten rev. 1961).

\(^\text{12}\) Baldwin v. Commissioner, 125 F.2d 812, 814 (9th Cir. 1942).

\(^\text{13}\) E.g., United States v. Pape, 144 F.2d 778, 782 (2d Cir.), cert. denied, 323 U.S. 752 (1944); Brown v. St. Paul City Ry., 241 Minn. 15, 34, 62 N.W.2d 688, 700 (1954).

\(^\text{14}\) Allen v. Rose, 199 Wis. 162, 165, 225 N.W. 831, 832 (1929).

\(^\text{15}\) 8 Wigmore, Evidence § 2311, at 601 (McNaughten rev. 1961).

\(^\text{16}\) See 58 Am. Jur., Witnesses § 492, at 275-76 (1948); 97 C.J.S., Witnesses § 276, at 787 (1957).


\(^\text{18}\) Id. at 17, 107 A.2d at 528; accord, Horlick's Malted Milk Co. v. Spiegel Co., 155 Wis. 201, 211-12, 144 N.W. 272, 276 (1913).
corporations. It argued that since an individual client cannot increase the extent of his protection by making agents of larger groups of individuals, it is anomalous to allow a corporation "to do the same thing through normal corporate operation."\(^{19}\) For this reason the court concluded that it is invalid to compare the single allowed exception to the secrecy rule—the presence of immediate office personnel necessary to the communication—with the "attempted extension of the term to encompass all those persons who constitute a corporate entity."\(^{20}\)

In reaching this result Judge Campbell correctly recognizes that the basic problem in this area is the "determination of what persons within the corporate structure hold its confidence" to the extent that they may personify the corporation and may properly be considered the client.\(^{21}\) However, his indiscriminant denial of the privilege to all corporations, though it solves this problem, seems unnecessary and to that extent unwarranted. Such a generalization equates large public issue corporations with small, closely held ones. Yet, this rationale denies the unassailable fact that not all incorporated businesses infringe upon the requirements of the privilege to the same degree. Where the corporate entity includes only several persons, there may be no real loss of confidentiality, and consequently no need to withdraw the privilege from such smaller corporations.

Moreover, a complete denial of the corporate privilege is unreasonable on another ground. Clearly, the confidentiality required by the privilege is violated to a lesser degree when the communication is made by officials high in the corporate hierarchy than when it is made by lesser agents. While the instant court recognized this fact, its ultimate determination of the problem neglected it. A broad preclusion of the corporate privilege without the drawing of a distinction between those in the corporate structure making the communication is seemingly unwarranted, even in light of the policy considerations underlying the attorney-client privilege.

A partial solution to this problem was offered by the United States District Court for the Eastern District of Pennsylvania in *Philadelphia v. Westinghouse Elec. Corp.*\(^{22}\) There the court, recognizing both the need to limit application of the privilege to corporations and also the injustice of denying it completely to all corporations, proposed a test to determine when a corporation may justifiably assert the claim of privilege. Through this proposed test that court attempted to give the corporation the benefit of the privilege when a true confidential relationship could be shown between the corporation and its attorney, while at the same time endeavoring to insure that the claim of privilege would not be successfully asserted to suppress discovery of all corporate communications merely because they were made by one of the corporation's employees to

\(^{19}\) 207 F. Supp. at 774.
\(^{20}\) Ibid.
\(^{21}\) Ibid.
one of its attorneys.\textsuperscript{23} Thus, it held that if the corporate agent or employee who makes the disclosure "is in a position to control or even to take a substantial part in a decision about any action which the corporation may take upon the advice of the attorney, or if he is an authorized member of a body or group which has that authority, then . . . he is (or personifies) the corporation . . . and the privilege would apply."\textsuperscript{24}

That the test is an obvious limitation of the corporate privilege is clear; nevertheless, it is supportable because while it guards against corporate misuse of the privilege, which justifiably troubles Judge Campbell in \textit{Radiant Burners}, it also protects free communications between attorney and client where it is consonant with the basic policy of the privilege. Although the practical effect of applying the test to a given situation is to some extent problematical, if practicable application is possible, the \textit{Philadelphia} court seemingly has found a commendable middle ground between complete denial of the corporate privilege and its free allowance.\textsuperscript{25}

Besides denying the corporation the protection of the attorney-client privilege the instant court also held that the particular letters in question did not fall within the scope of the \textit{Hickman v. Taylor}\textsuperscript{26} work-product rule. However, in so ruling the court pointed out that the fact that the client is a corporation in no way affects the work-product doctrine, distinguishing this doctrine from the attorney-client privilege on the grounds that the latter is the privilege of the client only, whereas the work-product rule is for the protection of the attorney.\textsuperscript{27} Yet, while the limits of each are thus theoretically delineated, it is nonetheless true that in practice the determination of which doctrine applies to which communications is sometimes impossible. Indeed, the same court which decided \textit{Radiant Burners} three weeks later held that the \textit{work-product} rule could be invoked to prevent compelling a corporation vice-president from answering questions relating to alleged conversations had between the vice-president, other corporate agents and employees, and corporation counsel, because possibly counsel's statements would thereby be revealed.\textsuperscript{28} It is indeed possible that the same result could have been reached if the attorney-client privilege had been relied on, assuming that it could still be claimed by corporations. Thus, while the two doctrines are designed to accomplish different results,\textsuperscript{29} if \textit{Radiant Burners} is to become fully effective in practice, a similar limitation on corporate

\textsuperscript{23} Ibid.
\textsuperscript{24} Ibid.
\textsuperscript{26} 329 U.S. 495 (1947).
\textsuperscript{27} 207 F. Supp. at 776.
counsel’s work-product protection seems necessary. Otherwise, under the guise of protecting counsel’s trial preparation, a corporation will still effectively be able to suppress discovery of its activities, almost to the same extent as it could have by use of the attorney-client privilege.

Although Judge Campbell’s opinion in Radiant Burners “is supported by a good deal of history and sound logic,” it seems doubtful whether a complete denial of the attorney-client privilege to corporations will find general acceptance among the judiciary. Nevertheless, to prevent widespread misuse of the privilege, a limitation in some degree on the inviolability of the corporation-attorney relationship is defensible. It would seem that the modification proposed by the Philadelphia court, assuming it is effective in practice, is more in keeping with the social necessity of reconciling the conflict between two traditional policy considerations—the protection of the attorney-client relationship and the need to reduce suppression of pertinent evidence.

GEOFFREY M. ALPRIN

RESTRAINT OF TRADE—A SELLER’S GOOD FAITH PRICE REDUCTION TO MEET AN EQUALLY LOW PRICE OF A COMPETITOR IS WITHIN THE SECTION 2(b) DEFENSE OF THE ROBINSON-PATMAN ACT, EVEN THOUGH THE SELLER OBTAINS NEW CUSTOMERS BY THE REDUCTION. Sunshine Biscuits, Inc. v. FTC, 306 F.2d 48 (7th Cir. 1962).

Sunshine Biscuits, Inc., engaged in marketing potato chips in Cleveland, Ohio, gave certain chain stores discounts without giving equivalent discounts to all other purchasers in competition with those stores. This was done in some cases to retain business, whereas in other instances Sunshine obtained new customers by the practice. In answer to a price discrimination charge by the Federal Trade Commission, Sunshine admitted that the effect of this practice “‘may be to injure, destroy, or prevent competition’ between the purchasers who received the discounts and those who did not,’” as prohibited by the Robinson-Patman Act, but raised the defense that the discounts were made in good faith to meet competition and were thus permissible under section 2(b) of the same act. The hearing examiner upheld Sunshine’s defense. On review, however, the Commission ruled that inasmuch as Sunshine had obtained new customers by meeting competition it could not avail itself of section 2(b). On appeal to the United States Court of Appeals for the Seventh Circuit the Commission’s ruling was reversed. Held, A seller’s good faith price reduction to meet an equally low


1 Sunshine Biscuits, Inc. v. FTC, 306 F.2d 48, 50 (7th Cir. 1962).
price of a competitor is within the section 2(b) defense of the Robinson-Patman Act, even though the seller obtains new customers by the reduction.4

In recent years the courts have filled many of the interstices in the "meeting competition" defense with rules made necessary by various complexities within the economic system. Such was the case in FTC v. A.E. Staley Mfg. Co.,5 in which the Court held that the section 2(b) defense was confined only to meet individual competitive challenges and that it could not be employed as a justification for a pricing system designed to meet competition in general.

Beyond the pricing restriction established in Staley, it has also been suggested that the competitor's price which the respondent was meeting must be a lawful price.6 At least, knowledge that the prices he meets are unlawful or that they are of such a nature as to be inherently illegal may be used to show the seller's lack of good faith.7 Moreover, since the defense is good only when the reduction in price is to meet the lower price of a competitor, it is said that under section 2(b) one may meet, but not beat competition.8

It logically follows that the "meeting competition" defense does not permit predatory price reductions to destroy an individual competitor or the competition in a particular locale. In Moore v. Mead's Fine Bread Co.,9 this limitation was emphasized when the Court stated that "if this method of competition were approved, the pattern for growth of monopoly would be simple. . . . [T]he profits made in interstate activities would underwrite the losses of local price-cutting campaigns."10

In considering these limitations upon the use of the section 2(b) defense, it is important to remember that the defense is operative only when there has been made a prima facie showing of price discrimination as defined in section 2(a). As a result, the price sought to be justified by this defense is, of necessity, a discriminatory price, i.e., a price not uniformly charged all the seller's customers.11 Nor is the price economically justified in the sense that it reflects a

4 Sunshine Biscuits, Inc. v. FTC, 306 F.2d 48 (7th Cir. 1962).
5 324 U.S. 746 (1948).
7 Standard Oil Co. v. Brown, supra note 6.
10 Id. at 119; accord, Maryland Baking Co. v. FTC, 243 F.2d 716 (4th Cir. 1957).
lower cost of doing business with the favored customer since the latter is charged a lower price than the seller's other customers solely because he has been offered a lower price by the seller's competitor and will not buy from the seller unless he meets the competitor's price.

Because section 2(b) permits a price which would otherwise be illegal, in applying the defense the courts must reconcile those interests protected by section 2(b) in allowing the seller to meet the price of a competitor by discriminating in price, and those protected by the Robinson-Patman Act in general in preventing discriminations which may have the effect of substantially lessening competition or tending to create a monopoly. Specifically, this becomes a problem of formulating rules which circumscribe the grant of power to discriminate represented by section 2(b) so that the undesired competitive effects of discrimination at the purchaser level are prevented while at the same time maintaining the defense as a protection for competition at the seller's level.

In the instant case although the court was directly faced with this task of resolving the conflict between those interests protected by the Robinson-Patman Act in general and those protected by the section 2(b) defense in particular, it chose not to reach its decision by attempting to reconcile these interests. Instead, it chose to direct its inquiry along the relatively narrow path of statutory construction. To do this, however, the instant court first had to dispose of two previous cases which contained language strongly suggesting that the "meeting competition" defense was inapplicable to price reductions used to obtain new customers.

In the first of these cases, Standard Oil Co. v. FTC, the Supreme Court had described the "meeting competition" defense as providing that "wherever a lawful lower price of a competitor threatens to deprive a seller of a customer, the seller, to retain that customer, may in good faith meet that lower price." Relying on this dicta, the FTC claimed that the Supreme Court had impliedly limited the applicability of section 2(b) to price cuts used merely to retain old customers. However, as the instant court correctly pointed out, the scope of this language becomes severely limited when it is read within the context of the issue which was then before the Court, namely, whether the "meeting competition" defense constituted an absolute defense to an otherwise discriminatory reduction in price. By reading the Supreme Court's language in the context of this question, the instant court was thus able to distinguish it as not being dispositive of the issue presented in Sunshine.

The second case which the Sunshine court had to distinguish before it could turn to its own construction of section 2(b) was the Second Circuit's opinion in Standard Motor Prods. Inc. v. FTC as the court in that case had stated


13 Id. at 242.
14 265 F.2d 674 (2d Cir. 1959), affirming, 54 F.T.C. 814 (1957).
that "it is well settled that a lowered price is within Section 2(b) only if . . . it is used defensively to hold customers rather than to gain new ones." However, again the instant court pointed out that the Standard Motor court was primarily concerned not with the "new customer" question but with the legality of "an industry-wide pricing system with decided anti-competitive tendencies." In regard to that system, that court held "that a lowered price is within section 2(b) only if it is made in response to an individual competitive demand, and not as a part of the seller's pricing system." Then, solely on the basis of Standard Oil and in an apparent effort to buttress its ruling, it continued by saying that the lowered price had to be used "defensively to hold customers rather than to gain new ones." Thus, nothing in Standard Motors indicated that the court did more concerning the "retaining-obtaining" issue than accept the language found in Standard Oil which the Sunshine court had already dismissed as being inapplicable to the instant case.

Having disposed of all applicable precedent, the instant court proceeded to find the basic rationale for its decision in the language of the section 2(b) proviso itself. Noting that section 2(b) permits a seller to show that his lower price was made to any purchaser, the court defined purchaser simply as one who buys and concluded that no justification existed for reading into the word any limitation restricting its meaning to those purchasers who had been customers of the seller before he lowered his prices.

Thus, the court avoided the laborious task of resolving the specific question with which it was presented within the framework of the larger problem of reconciling interests. However, in doing so, its reasoning appears somewhat superficial. Its interpretation of section 2(b) is not based upon any inquiry into either the act's legislative history or into its policies and objectives. Rather it is founded upon a consideration of the word "purchaser" in a vacuum, separated from the economic environment which gives the word its real meaning.

Moreover, while the instant court was justified in dismissing the Standard Oil and Standard Motors cases as not controlling in regards to the issue in the instant case, at the same time it failed to realize that these cases nevertheless are important in that they indicate a definite inclination on the part of those courts to consider section 2(b) as being confined by its inherent nature to a rather limited defensive situation. Consequently, the Sunshine court should have realized from these cases that the uniqueness of the case before it necessitated that the court completely and creatively evaluate the scope, effect and purpose of the defense as applied to this particular type of case.

Admittedly the court could and did find further support for its conclusion

---

15 Id. at 677.
16 Id. at 676.
17 Id. at 677.
18 Ibid.
in the thorough and well-reasoned dissenting opinion handed down by Commissioner Elman while the case was before the FTC.20 Commissioner Elman thoroughly analyzed the economic environment out of which the instant case arose and concluded that the per se approach advocated by the Commission's majority was both undesirable and impractical since in many cases no logical line could be drawn between a new customer and an old one, and even if such a line could be drawn, to preclude all section 2(b) price reductions for the purpose of obtaining new customers would be to prevent many sellers from increasing their share of the market.21

In the instant case, however, the court's opinion fails to reflect any such analysis of the facts giving rise to the price reduction. Neither is there evidence of an inquiry into the question of whether the particular reduction in question was of the defensive type that is protected by section 2(b). Yet, it would appear that such a finding should have been made by the court before ordering dismissal of the Commission's complaint.

This being true, it would appear that in future cases of this kind greater emphasis must be placed upon analyzing the facts of the individual competitive situation in question within the framework of the traditional criteria to determine if the particular discriminations fall within the protection of section 2(b). Moreover, such analyses must not only proceed on the basis of the established section 2(b) criteria but must necessarily include within their framework of reference all the interests sought to be protected by the Robinson-Patman Act as a whole.

JERRY L. GOODMAN


21 Sunshine Biscuits, Inc. v. FTC, No. 7708, Sept. 25, 1961, pp. 5-6 (dissenting opinion).
BOOK REVIEWS


In the days of Cosimo de'Medici, Antoninus, Archbishop of Florence, wrote as a moralist on social and economic problems. From his studies he concluded that the formation of cartels or the authorizing of monopolies for the purpose of securing dearer prices was forbidden. Although he was a brilliant scholar known for his common sense, beloved by his people, considered a saint while he lived and canonized after he died, Antoninus effected very little improvement in the commercial practices of his day.¹

We have these precepts with us today, now spelled out in statutes like the Sherman Act. Competition and free enterprise are by-words of our society. But there are differences which make the task of evaluation, judgment and persuasion more difficult. The precepts are stated in several places: statutes, decisions of judges and administrative agencies, and rules and regulations. Some have the breadth and generality expected of charters.² Others are out of date,³ badly worded, poorly conceived, or conflicting. More importantly, there just is no person or group of persons with the knowledge of the economy of an industrialized country like the United States equivalent to the grasp which our Quatro-Cento prelate had of the economy about which he wrote. Even single enterprises have become so large and complex that serious questions have been raised as to whether “outside” directors can be sufficiently informed to adequately perform a function of determining corporate policy.⁴

The need for economic knowledge as a basis for laws and their proper administration has long been recognized. But as the economy has become more complex, understanding has fallen further and further behind action.

Mr. Massel, lawyer and economist, has published the results of years of reflection on our inadequate knowledge of competition, one of the most

¹ Jarrett, S. Antonio and Mediaeval Economics xi (1914).
² Appalachian Coals, Inc. v. United States, 288 U.S. 344, 359-60 (1933).
³ As part of his efforts to encourage manufacturers, Alexander Hamilton persuaded the New Jersey legislature in 1791, to incorporate the Society for Establishing Useful Manufacturers, which, while failing in its original purpose, still enjoyed an exemption from taxes 145 years later. Schachner, Alexander Hamilton 278-81 (1946).
⁴ Chamberlin, Why It's Harder and Harder To Get A Good Board, Fortune, Nov. 1962, p. 109.
important aspects of the mosaic we call the economy.\textsuperscript{5} In order to place his subject in proper perspective, Mr. Massel first discusses the problems of formulating and administering public policies which bear on competition. He describes the complex structure of ultimate political, social and economic goals which form the basis for these policies, and reviews the confused skein of rules and regulations. He finds, for example, in the narrow field of antitrust that in addition to the Federal Trade Commission and the Department of Justice (who do not always adequately coordinate their work), at least twenty other federal agencies participate in antitrust administration.\textsuperscript{6} Moreover, neither Congress nor the Executive has made much progress in reviewing the effectiveness of antitrust operations.\textsuperscript{7}

After identifying the problems, and the lack of economic knowledge essential to their solutions, Mr. Massel discusses how economic analysis is currently used to help solve these problems and what might be done to improve its application.

The federal government, the states and municipalities are continuously producing laws and regulations having an impact on competition. Sometimes competition is intentionally fostered, at other times deliberately impaired. Perhaps, most often the results are unintentional because no one really knows what the effect will be. Mr. Massel especially notes how ignorance of effect upon competition beclouds the drafting of consent judgments by the Department of Justice and of orders by court and administrative agencies in antitrust proceedings. In such circumstances a substantial erosion of competition and, consequently, of the goals of competition can occur before the damage is recognized.

As the laws and regulations relating to competition involve the solution of economic and related problems, Mr. Massel concludes that “economics is the major discipline, other than law, which is involved.”\textsuperscript{8} Consequently, any remedy of the present inadequate situation “necessitates further coordination of the economic and legal disciplines and more effective cooperation between the two professions.”\textsuperscript{9}

Economic analysis is the tool which Mr. Massel believes can play an effective role, in the hands of competent economists, in providing clarifica-
tion of public policies regarding competition and in bringing about a more effective administration of the antitrust laws. To achieve such clarification and improvement, he suggests the following:

There is a pressing need to clarify public policies regarding competition and to improve their administration. A key factor in satisfying this need is the effective application of economic analysis. To achieve such clarification and improvement, several steps should be taken:

- Develop more affirmative conclusions about the influences of the various forms of competition on efficiency, costs, innovation, consumer sovereignty, economic growth, and stability.
- Produce a better coordinated structure of government regulation—federal, state, and local—bearing on competition.
- Coordinate the operations of the pertinent federal agencies.
- Eliminate those elements of tax policy that seem to hinder competition, such as present regulations that impose a tax penalty on dividing a large company into several smaller ones.
- Develop the means for conducting a continuing review of policies, the state of competition in the economy, and for spotting those markets that require special legislative or executive attention.

- Undertake a series of studies of the effects of antitrust enforcement on market competition, and the accomplishments of various types of decrees in order to develop a better understanding of the remedies which may be required to alleviate monopolistic situations.

- Improve the capacity of the judicial system and the administrative agencies to try economic issues, and to formulate effective remedies.10

The general studies could be made by government agencies or by research and academic institutions. A continuing review of competition in the economy would be carried on ideally by a central agency, without responsibility for prosecution and enforcement, organized along the lines of the Council of Economic Advisers.11

Mr. Massel strongly recommends joint studies by law and economic faculties which will develop men who can work effectively with other professions.12

Improvement in antitrust litigation calls for strengthening of the economic sections of the antitrust agencies by employment of top flight economists who would participate in all phases of a case, "planning the general strategy of the case, ... defining the issues, ... collecting and

---

10 Id. at 329-30.
11 Id. at 333.
12 Georgetown University Law Center's Institute for International and Foreign Trade Law has for some time been playing just such a role in fostering studies and discussions, involving participation by professors of law and economics.
presenting data, and in formulating the arguments." Mr. Massel suggests that "many, perhaps most, lawyers have yet to learn that some economists can make a greater contribution by analyzing evidence and helping with argument and strategy than by serving as expert witnesses."

There is no doubt that data and criteria about competition sufficiently reliable and meaningful to assist legislatures in formulating laws bearing on the subject, and courts and administrative agencies in enforcing the laws, are not to be found. Mr. Massel is very persuasive in his argument that economic analysis can provide an essential aid in policy making as it affects competition as well as in carrying out the antitrust laws. In the process he has charted out an unexplored land of opportunity for imaginative, diligent, and bold economists, which should prove to be a most attractive challenge to young scholars looking for socially worthwhile fields of endeavor.

Mr. Massel has no illusions as to the quality of the resources—both human and material—now available for this job. "We need to develop satisfactory analyses of the general state of competition." "[N]o scales are available to set benchmarks in the range from pure competition to pure monopoly." "We have few field studies which deal with the state of competition either today or in the past. We have yet to develop a theory or a body of data that can supply a firm conceptual and analytical base for examining such trends. There are no data covering the state of competition in bygone days to support any evaluation of trends."

"There is, today, no organized body of principles for economic analysis which will provide guidelines for solving the pointed decisional problems [in litigation] affecting competition. Nor is there a large group of economists equipped for the tasks and available for ready employment."

"Unfortunately, most of the debates about the relations between competition, efficiency, and the standards of living have been on theoretical grounds."

"Only in recent times has the economist entered the arena of problem-solving."

13 Massel, 168-69.
14 Ibid.
15 Id. at 86.
16 Id. at 179.
17 Id. at 87.
18 Id. at 181.
19 Id. at 26.
20 Id. at 176.
"The ready answers provided by economic theory will not do. Their philosophical bases contribute to methodology. But, their untested conclusions, taken out of a conceptual framework of static equilibrium, hardly fit the economy in being. Their generality, lacking the pointedness of an empirical approach to specific problems, is wide of the mark."21

"[T]here is a serious need for study of the structure and behavior of cost itself."22 "There is a clear need for better understanding about the behavior of costs and their relationship to competition."23 "There is a need to clarify the relationship between competition and the inflationary process."24

"[T]he economists [unlike the lawyers] have no institution for settling differences. There is no economic supreme court. Nor is there a jury to hand down an enforceable verdict. No economist has to accept another's opinion. There is no end to differences in general economic analysis, and there cannot be. Because of the lack of a unifying device, there is no formal consensus among economists."25

Despite the shortage of qualified economists and the inadequacies of doctrine, data, experience and tradition, Mr. Massel is enthusiastic about the role economists can play. He believes that an intelligent, adequately recompensed demand for economists as colleagues of lawyers will stimulate the improvements in economic analysis so obviously needed.

While wishing to see the federal judges deciding antitrust cases equipped with greater sophistication in economics, Mr. Massel does not suggest that economists could better decide such cases than could judges. Indeed, he is sufficiently apprehensive of an adverse reaction against economists by legislators so that he would not want to see policy decisions based entirely on an economist's predictions, "a most uncertain procedure in any process which must accommodate human reactions. . . ."26 While economists, like lawyers, must make forecasts, the economist's forecasts are not subject to . . . an unequivocal test. Nor, given the nature of economic problems, can they be. No institution is chartered to approve or disapprove. Even if an economist's peers were to accept his prediction, the ultimate test depends on what takes place in the economy or the market. Yet, even these do not provide conclusive proof. Even when the outcome matches

21 Id. at 122.
22 Id. at 27.
23 Ibid.
24 Id. at 30.
25 Id. at 174.
26 Id. at 119.
the prediction, there always remains the uncomfortable possibility that some unconsidered factors will be regarded as the strategic ones in some future analyses.27

Competition is not just economics, as Mr. Massel recognizes.28 It has been considered as the way of life under which man can best fulfill his purpose.29 Unless one holds the view that the economy is the helpless victim of an economic determinism which needs only be discerned, the role of the economists must of necessity be limited to the proper scope of his discipline whether in the determination of policy or the enforcement of laws. But a role is no less large or important for being defined. It all depends on how it is played. Economists of learning, common sense, lively and practical imagination, and a willingness to recognize the limits of their discipline, will always command respect.

Mr. Massel does not suggest that everything stand still while economic analysis is improved. We should use what tools are available now to get on with the job. But it will be interesting to see whether one day we must conclude that certain segments of our economy are so complex, and the human factor so important, that there is no better basis for predicting the future than the intuition of an intelligent, well-informed judge.

In this book Mr. Massel has made a substantial step in pursuit of one of the two aims he suggests for the more effective administration of policies dedicated to maintaining competition, namely, advancement of economic analysis in policy-making and administration. It is up to the universities and appropriate government departments to further contribute to the goal of improving economic analysis and its use by fostering studies and projects requiring the cooperative efforts of lawyers and economists.

JOHN T. MILLER, JR.*


One of the difficulties in any study of Congressional staffs is the wide variation in the staffing practices of the members and committees. Each Senator and Congressman operates almost like a separate agency with

27 Id. at 174.
28 Id. at 196.
29 See Kronstein & Miller, Regulation of Trade 1121 (1953).
* Attorney at Law, Washington, D.C.; Adjunct Professor of Law and Associate Director of the Institute for International and Foreign Trade Law, Georgetown University Law Center.
very few limitations other than those relating to maximum and overall salaries. The committees and subcommittees (of which there are over 200) likewise function virtually as independent institutions insofar as their personnel practices are concerned.

The most significant guide to the character and functions of the staff is likely to be the personality of the appointing member, or committee or subcommittee chairman. Their views as to the functions of a staff, their own working habits, the issues in which they are interested, their ambitions, and publicity awareness can play a much more important role in determining staff "personalities" than any provisions in the Legislative Reorganization Act.¹ Many a committee staff has undergone revolutionary changes in pace and method of operation with the advent of a new chairman even though the number of personnel changes may have been minor. Such changes obviously are even more pronounced when a House or Senate seat changes hands.

This situation is likely to date any particularized staff study during the time in which it takes to prepare it. Like painting a long bridge, or washing the windows of a skyscraper, the job requires redoing almost as soon as it is finished.

This particular book suffers severely from this handicap. It concentrates on a six year period from the start of the 80th Congress on January 3, 1947, when the Legislative Reorganization Act of 1946 first became fully operative, through the expiration of the 82nd Congress in 1952. Professor Kofmehl describes this as a "most appropriate" period because during it, changes in party control occurred in each of the three Congresses and the staffing provisions of the Legislative Reorganization Act were "institutionalized."² But these factors do not compensate for the ten year gap in time between the author's period of research and the publication of his report.

In recognition of this problem, the book concludes with a twelve page postscript "to acquaint the reader with major trends in congressional staffing through 1961." A substantial part of this deals with the pressure for more adequate minority staffing and attempts by new committee chairmen to place their "man" on their committees. These trends are characterized as a "threat" to the integrity of committee staffs,³ a view which will be questioned by those who regard the countervailing tendency

¹ Ch. 753, 60 Stat. 812 (codified in scattered sections of 2, 5, 15, 31, 33, 40, 44 U.S.C.).
³ Id. at 217.
towards institutionalized staffing as a threat to the representative character of Congress.

Some readers will undoubtedly regret the absence of any material on the practices of representative bodies in other countries. The question of providing staff assistance is a lively subject in Great Britain, where members of Parliament are hardly paid enough to sustain themselves in London during the sessions of the House of Commons. Whatever staff assistance these members enjoy, unless they are independently wealthy, is provided by their party organizations, and it is not unusual to see members of Commons writing or typing their own letters in large rooms provided for this purpose. Despite occasional complaints about the adequacy of Senate and House staffs, no member of Congress has recently been observed in a similar setting. Indeed, it is doubtful that any legislative body in the world has provided itself more generously with staff assistance. This comment is not made critically, but only to indicate the uniqueness of Congressional staffing practices in the United States, and its significance to the whole legislative process.

Despite these observations, this book will be welcomed by those concerned with the dearth of analytical information on Congressional personnel practices. It is apparent that the author has thoroughly researched the period on which he has focused attention. The arrangement of material is orderly and sensible. Except for the small type used, the book is very readable. Certainly Professor Kofmehl has made a significant contribution to the literature in this field and it is hoped that his work will inspire other more comprehensive studies of the work of Congressional staffs.

MILTON EISENBERG*


The study of socialist law and socialist legal systems has not developed in the West pari passu with the research and examination of political

* Adjunct Professor of Law, Georgetown University Law Center, Administrative Assistant and Counsel to Senator Kenneth B. Keating.
and socio-economic problems of the communist-controlled states. Scientific socialism being primarily an economic doctrine, and its political offspring, the dictatorship of the proletariat, has attracted the attention of Western economists and political writers rather than that of lawyers. It was only during the last decade that the study of the legal features of the communist-dominated countries was greatly intensified due to the perception that the legal order of a state, socialist and non-socialist alike, is the skeleton of its political and economic structure. Undoubtedly, this interest was further stimulated by the post-war territorial expansion of the orbit of socialist law, which today covers one fourth of the globe's territory and embraces one third of the world's population.

The Soviet Union, the oldest country among the contemporary socialist states, has also retained its primacy as the originator and source of socialist law. Although not all of the countries in the communist orbit have attained an equal degree of legal socialization, and some of them have tried to establish new and independent forms of socialist law, there is little doubt that in the sphere of socialist legal science the Soviet Union maintains the leading position, similar to that of England in the early period of the creation and development of common law. It is for this reason that general analyses of the legal institutions of socialist law are sometimes denominated as the presentations of the Soviet socialist law and Soviet legal system. This is particularly true of Dr. Grzybowski's book, which is much wider in scope than the title appears to indicate.

Dr. Grzybowski offers not only a thorough analysis of the Soviet legal institutions and their doctrines and functions, but also examines these features in almost all other socialist states by pointing out the comparisons and differences between various concrete legal forms and by contrasting them with similar legal institutions and their functions in the countries of civil and common law.

Beginning with a discussion of the general development of legal trends and institutions in the political, social and economic evolution of a modern state, Dr. Grzybowski reveals an outstanding knowledge of legal philosophy and legal principles as they have developed in civil law countries. He then examines certain aspects of the evolution of the Soviet legal


order from the early days of the Bolshevik regime, during the period the New Economic Policy and through the era of Stalin's personal dictatorship. Chapter three deals with the forms of adjudication in socialist economy and contains an analysis of various types of socialist courts and state arbitration boards as well as their structure and functioning. Of great interest is the chapter entitled "Homo Sovieticus," dealing with the legal status of a citizen in the socialist polity, particularly in the sphere of private and public law. The methods and efforts employed by the socialist state and its organs to re-educate its citizens in the spirit of socialist cooperation and legality are also examined by the author. The concept, evolution and problems of socialist legality, especially in the field of socialist criminal law and criminal procedure, are presented by Dr. Grzybowski with great clarity and are supported by references expressing the views of Soviet and other socialist jurists. Without predicting the future development of Soviet law, the author notes in his concluding chapter the two conflicting tendencies presently influencing its growth. On the one hand is the trend toward expansion of the rule of law; on the other is the increasing resort to social discipline by re-education rather than compulsion as a means of obtaining Soviet goals.

The purpose of Dr. Grzybowski's book is to give the Western reader a condensed picture of the basic principles and functions of the socialist legal systems and their institutions. In doing so he points out some of the fundamental differences between socialist law and common and civil law. In the first place, socialist law is the product of class dominance, the dominance of the proletarian class over all other strata of society. Second, the form of socialist law is not the only criterion by which a specific legal norm is to be evaluated. Much more important is the political content of a socialist law, that is, the motivation of the legislator and his interpretation of the law. In socialist states the motivation of the law and its interpretation can be given only by the political body that made the law and not by the courts. When necessary, such inter-

---

3 Id. at 41-48.
4 Id. at 48-53.
5 Id. at 53-56.
6 Id. at 266-67.
8 Yudin, Socialism and Law, in id. at 281-301.
9 All the constitutions of socialist countries, with the exception of the Hungarian Constitution, contain the provision which reserves the right of authoritative interpretation of the laws to the supreme legislative body or to a committee created by it. Only in
pretation will be made by the use of Marxian dialectics and in accordance with the needs of a particular stage of socialist evolution. Hence, the similarities between socialist and capitalist laws are merely formal and preclude the deduction of analogy between these two legal systems. In fact, the distinction made between the form and the content of socialist law makes this law basically different from the bourgeois concept of law. It is in the light of this well established principle of socialist law that further evolution of so-called socialist legality is to be considered.

Dr. Grzybowski's book suggests to the reader a compelling question: Is it reasonable to expect that the further strengthening of socialist legal order—proclaimed by Soviet and other communist leaders as their new policy of peaceful progress—will lead socialist countries to a point of development where their concepts of law will be identical with those of the West?

The answer to this question is partially given by Dr. Grzybowski, who says:

When in 1956 the Twentieth Party Congress called for the return to the rule of law in the Soviet Union, it had two aims in view. In the first place, the abuse of power was to be discontinued, the laws of the Soviet Union were to be reorganized into a clear system of rules. However, this was not understood as a change in the basic premises of the Soviet regime. The rule of law in its new meaning would still be subordinated to the needs of national economy which would continue to be administered by the government according to the plan. Furthermore, the leading role of the Communist Party within the social and governmental apparatus was reaffirmed.10

This opinion is supported by the views expressed in the most recent writings of Soviet lawyers, who once again emphasize that Soviet legality, in its essence, means the execution of the orders of the Communist Party, the guidance and direction by the Party in the development of socialist law, and the construction of the content of this law in accordance with the needs of a particular stage of historical development.11

It is clear that in view of this doctrine there is little, if any, hope that socialist legality may develop in the direction expected by those who anticipate the establishment and recognition of identical legal standards in socialist and in non-socialist law.

 Hungary is the binding interpretation of laws rendered by a supreme court. Gsoyski & Grzybowski, supra note 1, at 714-16.

10 Grzybowski at 177. For an official view of the position and role of the Communist Party in the Soviet Union, see Denisov & Kirichenko, Soviet State Law 142-44, 205-07 (1960).

This book is a most valuable contribution to the study of socialist law. It is a highly scholarly work and a profound analysis of the problems presented.

Unlike the work of Dr. Grzybowski, which is general in character, Professor Morgan's book deals with only one socialist legal institution and discusses its operation and organization in only one of the socialist countries. The book examines the historical development and the present position of the Attorney General in the Soviet Union, the Procurator General, and discusses the organization and the role of his department, the Procurator General's Office. This unique legal institution, found in all socialist legal systems under various names,12 is known in the Soviet law by its Russian term prokuratura, or the procuracy, in translation.

Professor Morgan has written the first book in the English language dealing exclusively with the institution of the procuracy in the Soviet Union, although this topic has been discussed more or less extensively by other authors in works describing the Soviet legal system.13 The principal title of Professor Morgan's book is to some extent misleading because the supervision exercised by the Procurator General does not extend merely to acts of administrative bodies, but to the decisions of the courts and other socialist institutions as well. Therefore, the subtitle, "The Role of the Attorney General's Office," is more appropriate and should have been used as the main title of the book.

The book presents a scholarly analysis of the rather complex and, in the West, little known problems involved in the supervisory prerogatives and duties entrusted to the Procurator General and his office. The study begins with an excellent and very useful introduction in which the author notes three different types of administrative supervision exercised today in the countries of common, civil and socialist law.14 The

12 As an institution of socialist law, the procuracy has been introduced under different names in all the existing socialist legal systems and its basic organization and duties defined in the respective constitutions. The Yugoslav communist regime, in its efforts to make itself distinct from other Communist regimes, tried to limit the rights and duties of the public prosecutor's office to the prosecution of criminal offenses before the courts. Only in exceptional cases, as directed by the government, was the public prosecutor to be entrusted with the supervision of the proper execution of the law. In the new Yugoslav Constitution (art. 131), which is to become effective by the end of 1962, the rights and duties of the public prosecutor are again defined with a striking similarity to those of the Soviet Procurator General. (Soviet Constitution, art. 113).


author reminds the reader that certain types of review of administrative action are recognized as indispensable in every modern state, regardless of the legal system to which it belongs.

Professor Morgan divides his book into two parts: the history of the Procurator General's supervision, and the scope of his office today. In the first part the author treats the role of the Procurator General from the moment of his original appointment by Peter the Great in 1722, until the beginning of the so-called "new era" in Soviet legal development, proclaimed after the death of Stalin in 1956. In this new era, the Soviet leaders claim, the government of arbitrariness is to be replaced by "the rule of law." 15

The organization and functions of the Procurator General's Office were subject to several reorganizations and modernizations during the era of the Empire, but, in essence, its tasks remained unchanged until the end of the tsarist regime. The Office was abolished in November 1917 by the newly established Bolshevik regime.16 It was considered that this institution was a part of the "old bourgeois order" which had to be destroyed in its entirety. The Bolsheviks, however, learned very soon that it was most convenient to have a powerful central organization under their command which could supervise the execution of their laws, under the pretext of the strict observance of socialist legality. Therefore, in May 1922 they reinstituted the position of the Procurator General with almost identical rights and duties as those given to him in the tsarist era.17 Of course, this new office was organized to become "the eye of the Party," 18 which replaced the tsarist absolutism with Bolshevik dictatorship.

Since its reestablishment and incorporation into the socialist legal system of the Soviet Union, the Procurator General's Office has been reorganized several times and its functions differently interpreted in various periods of the Soviet regime. At all times the procuracy has been intrinsically connected with the policy of the Communist Party. Two basic functions of this office, the general supervision of laws, and the specific tasks of judicial supervision and criminal prosecution have alternated in ascendency. During the era of the New Economic Policy, the basic function of the procuracy was to supervise the proper execution of the Soviet laws and thus to ensure the uniformity and existence of

15 1 Hazard & Shapiro, op. cit. supra note 11, at 3-6, 24-25.
16 Morgan at 22.
17 Id. at 41-43.
18 See id. at 17.
socialist legality. In the era of the five-year plans and during the great political purges in the late thirties, these functions were overshadowed by the execution of special tasks entrusted to the Procurator General. In this period the role of the procuracy in the liquidation of the kulaks as a class, and in the collectivization of agriculture, as well as Procurator General Vyshinsky's part in the political trials of 1936-1938, were of special significance.

Professor Morgan concludes that the general supervision of Soviet law appears once again to be the principal task of the Procurator General's Office. This supervision is all-embracing and includes the examination of administrative acts, judicial decisions, and control of the work of the cooperatives and other collective organizations of the Soviet state. The methods of supervision and control vary, including the ex officio checking of laws, regulations, ordinances and decisions, and the examination of the citizens' complaints. The instituting of special proceedings and the lodging of protests against unlawful administrative acts and judicial decisions are the principal means by which the procuracy assures observance of socialist legality.

In conclusion, Professor Morgan states that in the absence of constitutional restraints on administration, the Party and government prefer to rely on the institution of the procuracy, which is itself a branch of government, to watch over the operations of the rest of government. To the proposals made recently by a group of Soviet jurists that the supervision of socialist law should be entrusted to the Soviet courts, Professor Morgan answers:

[Although it would be an improvement in many respects, to allow Soviet courts to adjudicate many matters of an administrative nature, which are now outside their jurisdiction, [this] would not necessarily achieve results different from Procuracy supervision, because the courts are also completely under the domination of the Communist Party of the Soviet Union.]

There is no doubt that the conclusion reached by Professor Morgan is entirely correct. The courts in the Soviet Union, though formally in-

---

19 Id. at 44-75.
20 Id. at 76-95.
22 Morgan at 248.
23 Id. at 133-59.
24 Id. at 160-92.
25 Id. at 193-246.
26 Id. at 248.
27 Id. at 251.
dependent, and the procuracy, are but two functions of the dictatorship of the proletariat, as executed by the iron rule of the Communist Party. Inasmuch as the procuracy has the right to supervise the work of all Soviet administrative agencies and courts, this supervision is carried out within the framework of the laws enacted by the Party and the instructions given by Party leaders. The Procurator General is appointed by the Supreme Soviet on the proposal and with the consent of the Party’s Central Committee. Consequently, this supervisory authority is not and never will be placed above the policy of the Party; on the contrary, at all times he remains subordinated to it. The same is true for the Soviet courts which “serve as the organs of the proletarian state,” and whose task it is “to educate Soviet citizens in the spirit of patriotism and communism, in the spirit of strict adherence to the Soviet Constitution and Soviet laws” under the directives and guidance of the Communist Party.

Professor Morgan has produced a fine scholarly work of great value to those who are interested in a detailed study of the Soviet legal system, especially in the role of the procuracy, or attorney general, in that system. The extensive citation of authority and the thorough bibliography mark this as the product of serious scientific research.

Branko M. Peselj*

28 Denisov & Kirichenko, supra note 10, at 302; Hazard & Shapiro, supra note 11, at 45-46.
29 Denisov & Kirichenko, supra note 10, at 301.
* Member of the District of Columbia Bar and of the Bar of the Supreme Court of the United States; Adjunct Professor of Law, Georgetown University Law Center.
BOOKS RECEIVED


424