THE FEDERAL TAXATION OF MUNICIPAL EMPLOYEES

DAVID FELLMAN

I

IN THE great case of *M'Culloch v. Maryland*,¹ the Supreme Court held that, since the National Government is supreme within the sphere of its delegated jurisdiction, it is improper for a state to tax the notes issued by a federally-chartered bank, an instrumentality of the United States. The fact that there is no explicit provision for the exemption of federal instrumentalities from state taxation in the Constitution is, of course, not controlling, for much has been added to the original document by the process of interpretation. Accordingly, the taxing power of the states has been checked at those points where it impinges upon a federal agency or activity.² Thus, no state may tax property situated within its borders which belongs to the United States,³ or the compensation of a federal employee,⁴ or a corporation chartered by the Federal Government in order to effectuate any of its delegated powers, as, for example, the war power.⁵ The states may not tax the shares and operations of banks

¹A.B., University of Nebraska (1929), M.A., University of Nebraska (1930), Ph.D., Yale University (1934). Instructor in Political Science, University of Nebraska. Author of a series of four articles on *Due Process of Law in Nebraska* (1930) 9 Neb. L. Bull. 223, (1931) id. at 357, id. at 484, (1932) 10 id. at 496; *The Alien's Right to Work* (1938) 22 Minn. L. Rev. 137; *The Diminution of Judicial Salaries* (1938) 24 Iowa L. Rev. 89.


⁵Clallam County v. United States, 263 U. S. 341 (1923); New Brunswick v. United States, 276 U. S. 547 (1928); King County v. United States Shipping Brd. Em. Fleet Corp., 282 Fed. 950 (C. C. A. 9th, 1922); United States Spruce Prod. Corp. v. Lincoln County, 285 Fed. 388 (D. C. Ore. 1922); United States Shipping Brd. Em. Fleet Corp. v.
authorized by the Congress for a federal purpose,\(^6\) leases on restricted Indian lands,\(^7\) the franchise of a railroad chartered by the Federal Government,\(^8\) or federal obligations.\(^9\) Of course, the states may tax federal instrumentalities if the Federal Government consents.\(^10\)

In 1870, the Supreme Court held, in \textit{The Collector v. Day},\(^11\) that this rule of tax-exemption works both ways, in refusing to permit the imposition of a federal income tax upon the salary of a state judge. The fundamental proposition of the case was stated as follows:

"It is admitted that there is no express provision in the Constitution that prohibits the general government from taxing the means and instrumentalities of the States, nor is there any prohibiting the States from taxing the means and instrumentalities of that government. In both cases the exemption rests upon necessary implication, and is upheld by the great law of self-preservation; as any government, whose means employed in conducting its operations, if sub-

---


\(^11\) 11 Wall. 113 (U. S. 1870).
ject to the control of another and distinct government, can exist only at the mercy of that government. Of what avail are these means if another power may tax them at discretion?"12

In accordance with the doctrine of this case, many state instrumentalities have been held to come within the rule of tax-exemption, as, for example, state securities.13 Furthermore, the rule has survived the sweeping language of the Sixteenth Amendment, with its permission to tax incomes "from whatever source derived," since the Sixteenth Amendment has been judicially construed as conferring upon Congress no new power of taxation.14 This immunity of the state from federal taxation extends, of course, to such political subdivisions as the municipality, for, as the Supreme Court once declared, "A municipal corporation . . . is a representative not only of the State, but is a portion of its governmental power. It is one of its creatures, made for a specific purpose, to exercise within a limited sphere the powers of the State."15 Accordingly, the principles of tax-immunity which are applicable to the immediate instrumentalities of the state extend, by the same token, to the municipality and its agencies.

The attitude of Congress towards this tax-exemption, since the adoption of the Sixteenth Amendment, was first reflected in the Income Tax Act of 1913, which specified that in computing net income "the compen-

12 Id. at 127.
sation of all officers and employees of a State or any political subdivision thereof . . .” should be excluded.16 The same provision was included in the Revenue Acts of 1916 and of 1917,17 but was deliberately omitted from the Revenue Act of 1918,18 in order to leave “the constitutional question as to the authority of Congress to tax certain salaries to be settled by the courts in any case in which the question may be raised.”19 Soon afterwards, however, the Attorney General ruled that the salaries of officials and employees of a state are constitutionally immune from federal taxation.20 The Secretary of the Treasury decided to act in accordance with this ruling.21 Subsequent revenue Acts remained silent on the question until the passage of the Revenue Act of 1926, Section 1211 of which provided that “any taxes imposed by the Revenue Act of 1924 or prior revenue Acts upon any individual in respect of amounts received by him as compensation for personal services as an officer or employee of any State or political subdivision thereof . . . shall, subject to the statutory period of limitations properly applicable thereto, be abated, credited, or refunded.”22 Revenue Acts passed since 1926 have omitted any reference to the tax-exemption of such salaries. Thus, for the years 1913-1917, and for the years covered by the Revenue Act of 1926, the question of exemption is, to a great extent, a statutory one; for all other years the question is constitutional in character.

II

To establish a case for immunity from federal taxation, the municipal employee must show, first, that the activity with which he is connected is governmental in character. In the leading case on this point, South Carolina v. United States,23 the Supreme Court held that a state liquor dispensary system was taxable, stating that “the exemption of state agencies and instrumentalities from National taxation is limited to those which are of a strictly governmental character, and does not extend to those which are used by the State in the carrying on of an ordinary

2031 Ops. Att'y Gen. (1919) 441.
23199 U. S. 437 (1905).
private business." Similarly, in the recent liquor case, Ohio v. Helvering, the Court asserted that

"Whenever a state engages in a business of a private nature it exercises nongovernmental functions, and the business, though conducted by the state, is not immune from the exercise of the power of taxation which the Constitution vests in the Congress. . . . When a state enters the market place seeking customers it divests itself of its quasi sovereignty pro tanto, and takes on the character of a trader, so far, at least, as the taxing power of the federal government is concerned."

Since the line of demarcation between the governmental and the nongovernmental activity is a matter of construction, the decisions of the courts and administrative bodies must be consulted.

It is well settled that certain functions of local government, as, for example, the establishment of a judiciary, the provision of police protection, and the administration of the laws, are clearly governmental. Without question, the compensation of municipal policemen, firemen, judges, or such ordinary civil employees as clerks and tax officials, is not subject to federal taxation. Beyond a certain elementary point, however, the lines are less clearly drawn, as in the case of education, a primary municipal activity. Generally speaking, promotion of education is a governmental function. Thus, it has been held that the leasing of public lands for the benefit of schools is a governmental function.

---

1 Id. at 461.
2 292 U. S. 360, 368-9 (1934).
3 Prior to the enactment of the Revenue Act of 1926, the Treasury made this distinction, but § 1211 of the Act was broad enough to exclude all such compensation from taxation, whether in connection with either kind of state activity. For 1925 and later years, however, Treasury Regulations require that the services be rendered in connection with "essential governmental functions." See Mm. 3397, V-1 Cum. Bull. 36 (1926). This qualification was first inserted in the Treasury rules in U. S. Treas. Reg. 69, Art. 88, to be effective, in accordance with § 1211 of the Revenue Act of 1926, on or after Jan. 1, 1925.
4 The Collector v. Day, 11 Wall. 113 (U. S. 1870). In Freedman v. Sigel, 9 Fed. Cas. No. 5,080 (C. C. S. D. N. Y. 1873), it was held, on the authority of The Collector v. Day, that the United States may not impose a tax on the salary of a judge of New York City.
8 See the full collection of authorities in Cooper, Federal Taxation of Obligations Issued by State Educational Institutions (1937) 3 LEG. NOTES ON LOC. GOVT. 1.
9 Burnet v. Coronado Oil & Gas Co., 285 U. S. 393 (1932). Cf. Trinidad v. Sagrada Orden, 263 U. S. 578 (1924). See (1933) 27 ILL. L. Rev. 698. In the recent case, Helvering v. Mountain Producers Corp., 58 Sup. Ct. 623 (1938) cited supra note 7, the Supreme Court held that a lessee under an oil and gas lease of state school lands is not entitled to immunity from federal taxation, for the reason that "there is no sufficient ground for holding that
In a well-considered opinion, the Board of Tax Appeals has ruled that the compensation of an instructor in a state-supported university is not taxable, holding that such institutions are not conducted for profit, and are of general public concern. The Board rejected the notion that the test of what is a governmental function depends upon what was so considered at the time the Constitution was adopted; it depends, rather, "upon the necessity of exercising the function today," the criterion being "whether it is of general public concern" now. "Public needs vary with the changing conditions under which mankind finds itself."

There are, however, several borderline situations wherein the educational function is stretched beyond customary lines, and wherein the tax-exemption is rendered debatable. For example, among the new activities of many municipal school systems is the maintenance of school cafeterias, an activity which has been held recently to be a governmental function, since the cafeterias are not conducted for profit, are designed to improve the health of the students, and are, perhaps, educational as well, in teaching the nature of balanced meals. On the other hand, it has recently been decided that a cooperative book store on a university campus, operated by a closed association of faculty members and offering rebates to its members, is taxable, since the university has no interest in it. Although state courts have held a number of other school activities, including the construction of faculty residences, student dormitories and infirmaries, to be educational functions, they have not yet been tested in the federal courts with respect to the question of immunity from national taxation. Several federal courts having ruled that school athletic contests are not taxable, since they promote physical training and help support physical education courses, the Supreme Court finally

the effect upon the Government is other than indirect and remote", thus overruling the Burnet case.

G. Ridgely Sappington, 25 B. T. A. 1385 (1932). This has long been the view of the Bureau of Internal Revenue. S. M. 2726, III-2 CUM. BULL. 84 (1924).


25 B. T. A. at 1396.


Hoskins v. Commissioner, 84 F. (2d) 627 (C. C. A. 5th, 1936).


decided that the federal admission tax extends to college football contests for the reason that they constitute "a business having the incidents of similar enterprises usually prosecuted for private gain." Finally, it may be noted that the Bureau of Internal Revenue has ruled that the maintenance of a city library is a governmental function, as relating to the well-recognized duty of the state to establish and maintain a system of education. Although the educational facilities of the states and their subdivisions may be subject to other powers of Congress, as the regulation of foreign commerce, it may be said that they are considered governmental in character, and that this characterization extends to the newer forms which popular education may take.

Whether or not a city hospital is governmental in character depends upon the manner of its operation, the Bureau of Internal Revenue having taken the position that, if the hospital competes with the private business of operating hospitals, by taking all classes of patients regardless of their financial condition, and requiring all patients able to do so to pay for the treatment received by them, it is proprietary. The function is governmental, however, when the hospital is maintained for the indigent sick, and collections from patients represent a small percentage of the expenses. In a recent case, a federal district court held that the Boston City Hospital, which is maintained largely for the care of poor persons, and which receives but four and one tenth per cent of its expenses through paying patients, is governmental, being maintained for the common good of all without the element of special corporate benefit or pecuniary profit. The Board of Tax Appeals recently reached the same conclusion with respect to the Buffalo City Hospital, although a maximum fee of $3.50 per day is charged to those who are able to pay, on the ground that the hospital is operated without profit, and accepts patients regardless of financial resources, over sixty-six per cent being free

43 S. M. 3811, IV-2 CUM. BULL. 43 (1925).
44 In Board of Trustees of Univ. of Ill. v. United States, 289 U. S. 48 (1933), the Court upheld the collection of customs duties on scientific apparatus imported by a state university as a valid exercise of the federal commerce power, on the theory that there can be no encroachment on the power of the state where the state has no power over the subject to begin with. For a vigorous criticism of this case, see Johnson, Federal Taxation Affecting State Instrumentalities (1934) 68 U. S. L. REV. 248.
46 G. C. M. 10814, XI-2 CUM. BULL. 113 (1932). For the most recent administrative statement of this distinction, see Mim. 3838, rev., XV-1 CUM. BULL. 134 (1936).
patients. Such municipally-owned hospitals, therefore, stand on the same footing, with respect to tax-immunity, as public schools. It may be noted, finally, that by statute all local officials who require the use of or prescribe narcotic drugs, in their official capacity, are exempt from the provisions of the Narcotics Act requiring registration and payment of a special tax.

Another function related to the public health which is considered governmental is that of maintaining public parks. Thus, the salary of the superintendent of public parks of New Bedford, Mass., employed by an elective board of park commissioners, was held to be exempt from the federal income tax. The court held that the parks are open to the general public, as are roads and bridges, are not a source of revenue, have never been the objects of private enterprise, and are related to the public health. They are, in short, "essential to the health and general welfare of all the citizens of a state." A similar conclusion has been reached with reference to the salaries of the secretary of the Board of Park Commissioners of San Francisco, of an attorney employed by the commissioners of the Chicago park district, and of the director of a municipal playground in Los Angeles. However, the salary of the director of a commercial amusement park, although operated by a public commission, is taxable, since "the operation of an amusement park is not a usual, traditional, or essential function" of government.

Since the construction, maintenance and alteration of streets and sewers is a governmental function, the salary of a municipal engineer engaged in such work is tax-exempt. Accordingly, the salary of the

---

50 In Brush v. Commissioner, 300 U. S. 352, 371 (1937), it was said, obiter: "Certainly, the maintenance of public schools, a fire department, a system of sewers, parks and public buildings, to say nothing of other public facilities and uses, calls for the exercise of governmental functions."
52 Commissioner v. Lamb, 82 F. (2d) 733 (C. C. A. 9th, 1936).
53 Commissioner v. Schnackenberg, 90 F. (2d) 175 (C. C. A. 7th, 1937). These cases should lead the Bureau of Internal Revenue to change its rulings on the subject. Mem 3838, rev., XV-1 CUM. BULL. 133-4 (1936).
54 Ernest H. Hale, 33 B. T. A. 504 (1935). The fact that small fees are charged for towels, bathing suits, etc., in order to meet particular expenses, does not change the public character of a municipal playground.
55 Frank W. Darling, 34 B. T. A. 1062, at 1065-66 (1936): "The fact that governmental operation of a given enterprise may be preferable to private operation does not make such operation an essential or usual governmental function."
56 Halsey v. Helvering, 75 F. (2d) 234 (App. D. C. 1934). The Bureau of Internal Revenue recently ruled that sales of articles to states and their subdivisions for use in
chief street engineer of the Chicago Board of Local Improvements may not be taxed by the Federal Government, streets being for the benefit, convenience and comfort of the general public.\(^{57}\) It has been held, however, that one who is employed by the Chicago Board of Local Improvements to do work as a valuation expert, in condemnation proceedings in connection with a street-widening program, is engaged in a non-governmental activity. The reasoning of the court in this case is not persuasive.\(^ {58}\) In accordance with the prevailing view, a special local district engaged in constructing a bridge as part of a highway system is considered to be a governmental instrumentality, the fact that, responsive to a federal statute, the bridge plans must be approved by the Secretary of War\(^ {59}\) being immaterial.\(^ {60}\)

The Circuit Court of Appeals for the Second Circuit recently has ruled that the salary of the chairman of the Albany Port District Commission, which is engaged in establishing port facilities at Albany and Rensselaer, the two cities bearing the cost out of general taxation, is tax-exempt.\(^ {61}\) The court maintained that such an activity has long been regarded as a governmental function, as “providing for the welfare and prosperity of the people,”\(^ {61}\) pointing to illustrations from English, Continental and American experience. “In England and in Scotland, the right to erect a port was part of the royal prerogative. No port could exist except under the authority of the sovereign.”\(^ {61}\) Furthermore, the court pointed out that this activity has never been conducted for profit, and does not, therefore, withdraw any sources of revenue from the federal taxing power, since it has supplanted no private business to which the federal taxing power would normally apply. The essential point in the proprietary cases is “entrance into a trade enterprise.”\(^ {61}\) In accordance with the view expressed in this decision, the Board of Tax Appeals has reached the same conclusion with reference

the construction of sewers are tax-exempt, there being no difference between constructing a governmental instrumentality and operating it. S. T. 806, XIV-1 CUM. BULL. 416 (1935).

\(^ {57}\)John B. Hittell, 33 B. T. A. 276 (1935).

\(^ {58}\)Lyons v. Reinecke, 10 F. (2d) 3 (C. C. A. 7th, 1926). Relying upon the analogy of tort liability cases, the court held that street improvement is a quasi-private, corporate and ministerial duty, exercised for the advantage of the locality affected and its inhabitants. This definition would wipe out well-recognized distinctions between governmental and proprietary functions.

\(^ {59}\)34 STAT. 84 (1906), 31 U. S. C. § 528 (1934).

\(^ {60}\)Commissioner v. Harlan, 80 F. (2d) 660 (C. C. A. 9th, 1935).


\(^ {62}\)76 F. (2d) 515, 517 (C. C. A. 2d, 1935).

\(^ {61}\)Id. at 518.

\(^ {62}\)Id. at 519.
to an employee of the Port of New York Authority. However, the Supreme Court has recently ruled that the Authority's employees are taxable, on the ground that the burden on the state is not actual and substantial, but merely "conjunctural." In a recent case the Court of Claims ruled that tax-immunity does not extend to the one-third interest a city has in a wharf operated by a private company, the court asserting that the operation of a public wharf is not a "usual" function of government. Similarly, the Board of Tax Appeals has decided that the director of the port of the city of Beaumont, Texas, where fees are charged for the use of docks and wharves, does not come within the principle of tax-immunity.

The furnishing of transportation facilities by municipalities has been the subject of a considerable amount of litigation. The operation of a ferry by the town of Jamestown, all the capital being furnished by the town or on its credit, and the town now owning all of the stock, no dividends having ever been paid, has been held to be governmental. Since the town has no other public facilities to the mainland, this ferry is indistinguishable, in function, from a bridge or part of a highway; it is not a mere convenience, but "essential to the normal life of this community." In an earlier case, the maintenance of a county-operated ferry was held to be a governmental function, the court classifying ferries with roads and bridges as essential public activities.

Whether or not the operation of a street railway by a municipality is a governmental function presents an analogous problem. In 1911, the Supreme Court stated, in a dictum in Flint v. Stone Tracy Co.:

"It is no part of the essential governmental functions of a State to provide means of transportation, supply artificial light, water and the like. These objects are often accomplished through the medium of private corporations, and, though the public may derive a benefit for such operations, the companies carrying on such enterprises are, nevertheless, private companies, whose business is prosecuted for private emolument and advantage. For the purpose of taxation they

---

63 Helvering v. Gerhardt, 58 Sup. Ct. 969 (1938).
65 Shelby Wiggins, 27 B. T. A. 576 (1933). The Board relied mainly upon several Texas cases holding street railway systems and waterworks proprietary functions.
67 Id. at 923.
69 220 U. S. 107, 172 (1911). In Georgia v. Atkins, 10 Fed. Cas. No. 5,350 (C. C. N. D. Ga. 1866), it was held, as a matter of statutory construction, that the Congress did not intend to tax the earnings of a state-owned railroad, the court construing the word "corporation," as used in the statute (13 Stat. 275, as amended, 14 Stat. 135) not to include the "state."
stand upon the same footing as other private corporations upon which special franchises have been conferred.”

In 1924, however, a federal district court held that an employee of a municipally-owned and operated street railway system is exempt from the federal income tax, on the ground that this is a governmental activity comparable to highways and other means of communication in which the whole community is interested. The court asserted that in a large modern city, the street car system “constitutes the veins and arteries of the city necessary to its very life.” In the course of the following year, a different federal district court refused to grant an injunction to prevent the imposition of the income tax upon the salaries of the employees of the street railway system owned and operated by the city of Seattle, on the ground that the administrative officers should not be hampered in the collection of taxes in advance of a final and authoritative determination that such income is exempt.

The question was finally determined by a unanimous Court in 1934, in Helvering v. Powers. The precise issue here was the taxability of the compensation of the members of the Board of Trustees of the Boston Elevated Railway Company, a board created by the state, the members of which were appointed by the governor for a term of ten years, and were empowered to manage the company for a period of public operation. In holding such income taxable, the Court pointed out that the principle of tax-immunity has inherent limitations.

“And one of these limitations is that the State cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from usual governmental functions and to which, by reason of their nature, the federal taxing power would normally extend. The fact that the State has power to undertake such enterprises, and that they are undertaken for what the State conceives to be the public benefit, does not establish immunity.”

The Court asserted that the municipal street railway comes within the rule applicable to state liquor establishments, which had been held to be proprietary in character. It is immaterial that the trustees are

---

Footnotes:

68 Frey v. Woodworth, 2 F. (2d) 725 (E. D. Mich. 1924). The case was dismissed in the Supreme Court on the motion of the Solicitor-General, Woodworth v. Frey, 270 U. S. 669 (1926), probably because of the enactment of § 1211 of the Revenue Act of 1926. For criticism of the view set forth in this case, see: (1925) 25 Col. L. Rev. 653; (1925) 38 Harv. L. Rev. 793; (1925) 73 U. of Pa. L. Rev. 419.

69 2 F. (2d) 725, 728 (E. D. Mich. 1924).

70 Seattle v. Poe, 4 F. (2d) 276 (W. D. Wash. 1925).


72 293 U. S. 214, 225 (1934).

73 South Carolina v. United States, 199 U. S. 437 (1905); Ohio v. Helvering, 292 U. S.
called "public officers," or that they are empowered to fix rates, for it is "the nature of the enterprise, and not the particular incidents of its management" which is the controlling factor. 72

A different conclusion has been reached in respect to a municipally-owned waterworks. On the strength of the dictum in Flint v. Stone Tracy Co., already referred to, 73 a lower federal court on two occasions reached the conclusion that such an activity is proprietary, 74 holding that water is often furnished through the medium of private corporations, and pointing to the danger of extending tax-immunity beyond its proper sphere. This, also, was the view of the Board of Tax Appeals. 75 The Court of Appeals for the Eighth Circuit ruled, early in 1937, that the furnishing of water is a governmental function, but that the city must, in fact, own and operate the plant; that though the city owns a large portion of the stock, if its interest is less than ownership the corporation is a private one, and therefore taxable. 76 In March, 1937, the Supreme Court finally ruled on the question in Brush v. Commissioner of Internal Revenue, 77 in which a divided court 78 held that the

360 (1934). Said the Court: "We see no reason for putting the operation of a street railway in a different category from the sale of liquors. In each case, the State, with its own conception of public advantage, is undertaking a business enterprise of a sort that is normally within the reach of the federal taxing power and is distinct from the usual governmental functions that are immune from federal taxation in order to safeguard the necessary independence of the State." 293 U. S. 214, 227 (1934).

72293 U. S. 214, 226-227 (1934). The Bureau of Internal Revenue has ruled that the activities of the Board of Transportation of New York City, in connection with the subway system, are proprietary, and that its officers and employees are therefore taxable. I. T. 2782, XIII-1 Cum. Bull. 83 (1934).

To assure the street railway company a maximum annual dividend of 6%, the City of Cleveland directed, by ordinance, that the company must provide a revolving fund of $500,000. If the fund falls as low as $300,000, fares are automatically raised, and if it reaches $700,000, fares are automatically lowered. It has been held that the earnings in excess of the amount required to pay annual dividends are taxable, even though the excess must be put aside, the court pointing out that, since the company is privately owned, carrying on its business for profit, and the city owns no part of its capital stock, derives no income from it, and pays no part of its expenses, the tax does not burden the city. Cleveland Ry. v. Commissioner, 36 F. (2d) 347 (C. C. A. 6th, 1929), cert. denied, 281 U. S. 743 (1930).

73See note 67; supra.

74Blair v. Byers, 35 F. (2d) 326 (C. C. A. 8th, 1929); Denman v. Commissioner, 73 F. (2d) 193 (C. C. A. 8th, 1934).

75Susan H. Mathews, Executrix, 33 B. T. A. 682 (1935). Here the Board held that the same rule applies to the furnishing of electricity.

76Citizens Water Co. v. Commissioner, 87 F. (2d) 874 (C. C. A. 8th, 1937). The Board of Tax Appeals had been of the same opinion, 32 B. T. A. 750 (1935).

77300 U. S. 352 (1937).

78Stone and Cardozo, JJ., concurred in the result on the narrow ground that the petitioner had brought himself within the terms of the exemption prescribed by U. S. Treas.
operation and maintenance of a municipal water system is a governmental function. The particular issue here was whether or not the salary of the Chief Engineer of the Bureau of Water Supply of the City of New York is a part of his taxable income for the purposes of the federal income tax. The majority opinion asserted that "The public interest in the conservation and distribution of water for a great variety of purposes—ranging from ordinary agricultural, domestic and sanitary uses, to the preservation of health and of life itself—is obvious and well settled. . . ." Without an adequate supply of water, it was stated, "public schools, public sewers so necessary to preserve health, fire departments, street sprinkling and cleaning, public buildings, parks, playgrounds, and public baths, could not exist. And this is equivalent, in a very real sense, to saying that the city itself would then disappear." The Court was not impressed with the argument that at one time the business of furnishing water to urban communities was largely, even entirely, left to private enterprise. "Governmental functions", it declared, "are not to be regarded as non-existent because they are held in abeyance, or because they lie dormant, for a time. If they be by their nature governmental, they are none the less so because the use of them has had a recent beginning." Finally, it was pointed out that it is immaterial that the city makes a charge for the service, for compensation or fees may be required in respect to highways, schools, recording deeds, and the like, without detracting from their governmental character.

The dissenting opinion of Mr. Justice Roberts emphasized the belief that the burden here imposed upon the city is not a real and direct burden, since the city competes for engineering talent with private companies whose employees are subject to the same income tax. He thought that any consideration of tax-immunity, so far as the engineer in this case is concerned, "would be altogether remote, impalpable and unascertainable in influencing him to accept a position under the municipality rather than under a private employer." This would seem to represent the better point of view.

Reg. 74, Art. 643, the validity of which had not been challenged by the Government. This position is difficult to understand, since the Court does not consider itself bound by administrative interpretations of the law. In Helvering v. Powers, 293 U. S. 214, 224 (1934), speaking for a unanimous Court, Mr. Chief Justice Hughes wrote, concerning the same Treasury Regulation: "But the Treasury Department could not by its regulation either limit the provisions of the statute or define the boundaries of their constitutional application." Roberts, J., wrote a dissenting opinion; Brandeis, J., concurred therein.

The Court brushed aside certain contrary statements in South Carolina v. United States, 199 U. S. 437, 461 (1905), and Flint v. Stone Tracy Co., 220 U. S. 107, 172 (1911), as being dicta suggested merely by way of illustration.

See: (1937) 37 Col. L. Rev. 1019; (1937) 50 Harv. L. Rev. 980; (1937) 12 Ind.
The construction and operation of a commercial airport by a city, the Bureau of Internal Revenue has ruled, is not an "essential governmental function." It has been held that a state-owned bank is a proprietary activity, a ruling which, if undisturbed, would include comparable municipal credit agencies. A limited dividend housing corporation, most of whose preferred stock is owned by a municipality, is not a governmental functionary, yet is not taxable under the statutory provision of tax-exemption for non-profit civic organizations. Finally, it may be noted that the courts hold that when a state goes into the liquor business it enters a field of activity which is open to federal taxation. This rule applies, of course, to municipalities. The state's exercise of police power over the liquor traffic, however, is a governmental function, with which the Federal Government may not interfere through taxation. Thus, bonds which are required of liquor dealers by a local police regulation are not subject to national taxation, nor may the Federal Government impose penalties, in the form of taxes, to punish violators of state liquor laws.

In conclusion, it should be noted that, while the employees of local proprietary activities are subject to the federal income tax, the Bureau of Internal Revenue has ruled that the net profits of such organizations are not so subject, at least according to the present wording of the tax statutes. When this question first came to the attention of the Bureau, in connection with state liquor systems, it held the profits of the Oregon Liquor Control Commission taxable. This decision was soon reversed by the Bureau, for the reason that much of the profits are used for carrying on governmental functions, such as relief.


*Garden Homes Co. v. Commissioner, 64 F. (2d) 593 (C. C. A. 7th, 1933).
*Salt Lake City v. Hollister, 118 U. S. 256 (1886).
*Ambrosini v. United States, 187 U. S. 1 (1902). To the same effect is United States v. Owens, 100 Fed. 70 (E. D. Mo. 1900).
*T. 2797, XIII-2 CUM. BULL. 74 (1934).
*G. C. M. 13,745, XIII-2 CUM. BULL. 76 (1934); I. T. 2820, XIII-2 CUM. BULL. 77 (1934).
ever, shortly thereafter put this particular tax-exemption on a much narrower ground, holding, in a ruling on the taxation of the profits of the Montana liquor system, that, since the revenue Act imposes taxes on "individuals" and "corporations," these words, as a matter of statutory interpretation, do not and have never been held to include states or municipalities. The constitutional issue has thus been avoided, and wisely so, since the test of taxability is the source of profits, rather than their purpose. The situation at present seems to be as follows: where the activity is a proprietary one, although the compensation of the officers and employees engaged in it is subject to the federal income tax, the net income derived by states and municipalities from these activities is not taxable, for the reason that the Congress has apparently not expressed any intention of taxing such income. As a matter of statutory interpretation, therefore, the constitutional question being thus far untested, a municipality may go into any kind of business with the assurance that the net income therefrom will not be taxed by the Federal Government.

III

When is a local activity governmental, and under what circumstances is it proprietary? Manifestly, as the cases now stand, it cannot be said that the courts have as yet developed a clear and forthright distinction between these classifications. With respect to certain functions which are obviously governmental, the courts have had no difficulty in reaching a decision.

"It may be admitted that the reserved rights of the States, such as the right to pass laws, to give effect to laws through executive action, to administer justice through the courts, and to employ all necessary agencies for legitimate purposes of State government, are not proper subjects of the taxing power of Congress." When, however, one goes beyond the policeman, fireman, judge and town clerk, to consider the new activities of government, the basis of the distinction between the taxable and the non-taxable is not well-defined.

In the leading case of South Carolina v. United States, the Supreme Court suggested that the question as to whether or not an agency is governmental would depend upon the circumstances which prevailed at

---


93 Veazie Bank v. Fenno, 8 Wall. 533, 547 (U. S. 1869). Cf. the statement of the Court in Flint v. Stone Tracy Co., 220 U. S. 107, 158 (1911): "The exercise of such rights as the establishment of a judiciary, the employment of officers to administer and execute the laws and similar governmental functions cannot be taxed by the Federal Government."

94 199 U. S. 437 (1905).
the time the Constitution was framed. Considering the facts that in the eighteenth century the functions of government were few and simple, and that the greater part of business activity was in private hands, the Court suggested that it is obvious that the Constitution was meant to endow the Federal Government with a very full taxing power, and that it was not anticipated that the states, by extending their functions, could destroy that power. The Court concluded by saying that the exemption of state instrumentalities from national taxation is limited to those which are of a strictly governmental character. In the more recent liquor case, Ohio v. Helvering, the Court suggested that the test would depend upon whether or not the state "chooses to go into the business of buying and selling commodities." In another case, the Court stated that

"The true distinction is between the attempted taxation of those operations of the States essential to the execution of its governmental functions, and which the State can only do itself, and those activities which are of a private character."

In holding a municipally-owned street railway a proprietary activity, the Chief Justice asserted that a

"... State cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from usual governmental functions and to which, by reason of their nature, the federal taxing power would normally extend."

Thus, a variety of tests have been applied, the criteria being that the exemption is limited to those activities which are strictly governmental, or which are essential governmental functions, or which are, traditionally, usual governmental functions. The underlying test, it was recently stated by a federal district court, is whether or not the activity is for the common good of all without the element of special corporate benefit or pecuniary profit, and, similarly, another lower federal court has asserted that the essential point in the proprietary cases is "entrance into a trade

---

95 392 U. S. 360, 369 (1934).
97 Helvering v. Powers, 293 U. S. 214, 225 (1934); United States v. California, 297 U. S. 175, 185 (1936): "Hence we look to the activities in which the states have traditionally engaged as marking the boundary of the restriction upon the federal taxing power." See also, Commissioner v. Modjeski, 75 F. (2d) 468 (C. C. A. 2d, 1935), cert. denied, 295 U. S. 764 (1935); Galveston v. United States, 10 F. Supp. 810 (Ct. Cl. 1935), cert. denied, 297 U. S. 712 (1936).
enterprise." In the most recent case on the subject, however, *Brush v. Commissioner of Internal Revenue*, the Supreme Court made the following comment on these various words and phrases used to define a governmental activity:

"But these differences in phraseology, and the others just referred to, must not be too literally contradistinguished. In neither of the cases cited, was the adjective used as an exclusive or rigid delimitation. For present purposes, however, we shall inquire whether the activity here in question constitutes an essential governmental function within the proper meaning of that term; and in that view decide the case."

It would appear, therefore, that the latest blessing of the Court is bestowed upon the idea that the function must be *essential* to be governmental. If it be said that this is a very vague concept, it may be noted that the law is full of such vagaries.

Little help is derived, in seeking to rationalize this concept, by considering the cases dealing with state taxation of federal instrumentalities. Although it has been suggested by the Court that the rule, in a federal system, necessarily works both ways, and although it has been argued that logically the rule ought to work both ways, the fact remains that thus far no federal instrumentality has been judicially held to be proprietary in character. Indeed, the same function has been held to be proprietary, when carried on by the state, and governmental, when in the hands of a federal agency. For example, federally-chartered banks have been ruled beyond state taxing power, unless the Federal Government, of course, permits the states to tax them, while, on the other hand, a state bank, even if owned and operated by the state itself, is a proprietary activity. A municipally-owned street railway system is

---

100 Commissioner *v.* Ten Eyck, 76 F. (2d) 515, 519 (C. C. A. 2d, 1935).
a proprietary activity,\(^{106}\) while, on the other hand, the Panama Railroad Company, all of the stock of which is owned by the United States, is a governmental instrumentality.\(^{107}\) Although the Federal Government may tax state franchises,\(^{108}\) a state tax on a federal franchise is invalid.\(^{109}\) When a state owns and operates a railroad it is acting in a non-governmental capacity, and can therefore be penalized by the Federal Government for violating a federal statute;\(^{110}\) yet the conditions of federal efficiency are not subject to state control.\(^{111}\)

The reason for this difference between state and federal instrumentalities is found in the principle of federal supremacy, according to which "the federal government in all its activities is independent of state control."\(^{112}\) The concept that the whole is superior to any of its parts was clearly set forth by Mr. Chief Justice Marshall in *M'Culloch v. Maryland*,\(^{118}\) in the following words:

"The people of all the States, and the States themselves, are represented in Congress, and, by their representatives, exercise this power. When they tax the chartered institutions of the States, they tax their constituents. . . . But when a State taxes the operations of the government of the United States, it acts upon institutions created, not by their own constituents, but by people over whom they claim no control."

Furthermore, the Federal Government is one of delegated powers alone, and all of these powers are public or governmental powers. Thus, the Tennessee Valley Authority was sustained as a constitutional exercise of federal authority on the basis of the war power and the power of the Congress over navigation, even though it was established primarily

---

\(^{106}\)Helvering v. Powers, 293 U. S. 214 (1934).


\(^{108}\)Flint v. Stone Tracy Co., 220 U. S. 107, 152-165 (1911); Veazie Bank v. Fenno, 8 Wall. 533, 547 (U. S. 1869).


\(^{110}\)United States v. California, 297 U. S. 175 (1936).

\(^{111}\)Johnson v. Maryland, 254 U. S. 51 (1920); Ohio v. Thomas, 173 U. S. 276 (1899); Hunt v. United States, 278 U. S. 96 (1928); *Ex parte* Willman, 277 Fed. 819 (S. D. Ohio 1921).


\(^{113}\)4 Wheat. 316, 435 (U. S. 1819). See also the remarks of Mr. Justice Bradley, dissenting in *The Collector v. Day*, 11 Wall. 113, 128 (U. S. 1870).
for other purposes. This theory of our constitutional law has been given admirable expression by Judge Graham of the Court of Claims in the following language:

"The United States is a government of limited and enumerated powers. There is no specially granted or implied power to engage in private business as such. In selecting the means to carry out and perform its constitutional powers the government may invade the field of what is called private business, and to the extent that it does it is performing what it can only perform—a public function. A state by reason of its original and reserved sovereignty may engage as a separate personality or corporation in what is called 'private business,' and thus subject itself to certain liabilities. But when the United States enters the field of so-called private business even as a separate personality or corporation, in order to effectuate certain of its granted powers, its action in so doing is a public act and it is not liable to be treated as a private individual and be subjected to taxation as such."115

Finally, it may be noted that rules of constitutional law growing out of and relating to the federal system do not always work both ways, since, in many respects, it is not a system of equal reciprocity.116

The rule of public purpose as it relates to the state's taxing power does not help, either, in determining the criteria of a governmental instrumentality. Thus, for example, a state may constitutionally use tax funds to go into the banking business;117 yet such bank is subject to a federal capital stock tax.118 A state may go into the liquor business;


115 Alabama v. United States, 38 F. (2d) 897, 903 (Ct. Cl. 1930). This case was reversed, not on the merits, but on the ground that the Court of Claims had no jurisdiction over the case, 282 U. S. 502 (1931). On this point, see Stoke, supra, note 103; Hynning, Intergovernmental Taxation (1937) 15 CHICAGO-KENT REV. 87.

116 For a good treatment of this point, see Field, State versus Nation, and the Supreme Court (1934) 28 AM. POL. SCI. REV. 233. See also, Boudin, The Taxation of Governmental Instrumentalities (1933) 22 GEORGETOWN LAW JOURNAL 1, 254; 1 WILLOUGHBY, CONSTITUTION OF THE UNITED STATES, (2d ed.) 129-143, 183-253; Note (1934) 44 YALE L. J. 326, 334-9.


118 North Dakota v. Olson, 33 F. (2d) 848 (C. C. A. 8th, 1929), dismissed for want of jurisdiction, 280 U. S. 528 (1929). The Bureau of Internal Revenue has recently ruled, however, that employees of the Bank of North Dakota are state employees, within the meaning of §§ 811 (b) (7) and 907 (c) (6) of the Social Security Act, 49 STAT. 620, 42 U. S. C. § 301-2 (Supp. 1935), which except from the term "employment" as defined in the Act, "Service performed in the employ of a State, a political subdivision thereof, or an instrumentality of one or more States or political subdivisions." S. S. T. 113, XVI Int. Rev. Bull., No. 16, at 14 (1937). Thus, at present, the status of the Bank of North Dakota is as follows: (1) it is for a public purpose so far as the state's taxing power is concerned; (2) it is a proprietary agency, so far as a federal capital stock tax is concerned; (3) it does not fall within the social security taxes, being a state instrumentality.
yet, from the point of view of federal taxation, the activity is proprietary. A state may go into the street railway business, consistently with the public purpose doctrine; nevertheless it is a proprietary agency, and therefore within the scope of the federal taxing power. It is constitutionally proper for cities to go into the fuel business, the flour business, the gasoline business, and many other similar enterprises, so far as the due process clause and the doctrine of public purpose are concerned; yet, as the cases now stand, these activities would probably be considered proprietary in character.

Similarly, the distinction between governmental and non-governmental activities as applied in municipal tort liability cases is equally unsuitable as a basis for the distinction in the tax cases, although many courts cite tort cases for purposes of analogy. The distinction between proprietary and governmental agencies in tort law is highly illogical; the cases are in the greatest possible state of confusion, opposite conclusions having been reached by the state courts on very many subjects. Furthermore, the definition in tort law is a matter for the local state courts to determine; it is not a guide for the interpretation of national taxing power under the Constitution. The Court expressed this idea in the *Brush* case as follows:

"The rule in respect of municipal liability in tort is a local matter; and whether it shall be strict or liberal or denied altogether is for the state which created the municipality alone to decide . . . provided, of course, the Federal Constitution be not infringed. But a federal tax in respect of the activities of a state or a state agency is an imposition by one government upon the activities of another, and must accord with the implied federal requirement that state and local governmental functions be not burdened thereby. . . . The unimpaired existence of both governments is equally essential. It is to that high end that this court has recognized the rule, which rests upon necessary implication, that neither may tax the governmental means and instrumentalities of the other. . . . In the light of these considerations, it follows that the question here presented is not controlled by local law but is a question of national scope to be resolved in harmony with implied constitutional principles of general application."

---

124Standard Oil Co. v. City of Lincoln, 275 U. S. 504 (1927).
126See the exhaustive study by Borchard, *Government Liability in Tort* (1924-1925) 34 Yale L. J. 1, 129, 229; (1926-1927) 36 id. at 1, 757, 1039; (1928) 28 Col. L. Rev. 577, 734.
In addition to demonstrating that his compensation is derived from an essential governmental service, it is also necessary for one who claims exemption from federal taxation to show that he is, in fact, a bona fide local official or employee, and not merely an independent contractor. The Bureau of Internal Revenue recently stated the general rule as follows:

"One engaged to render a particular service to a State or political subdivision, or to bring about a desired result, or one who has entered into a contract to accomplish a specific object, is an independent professional agent or an independent contractor, and not an employee, as there is not present a control of such a nature as characterizes an employer and employee relationship."\textsuperscript{128}

On another occasion the Bureau stated:

"An officer is a person who occupies a position in the service of the State or political subdivision, the tenure of which is continuous and not temporary and the duties of which are established by law or regulations and not by agreement. An employee is one whose duties consist in the rendition of prescribed services and not the accomplishment of specific objects, and whose services are continuous, not occasional or temporary."\textsuperscript{129}

The distinction, between the independent contractor who is not exempt from federal taxation and the true official or employee who is, has been fully accepted in principle by the courts. In the leading case, \textit{Metcalf \& Eddy v. Mitchell},\textsuperscript{130} it was held that consulting engineers, who were employed by subdivisions of several states for work, on public water supply and sewage disposal projects, which was not permanent or continuous in character, whose duties were prescribed by contract, who took no oath of office and were free to accept other employment concurrently, were not state officers or employees. Said the Court:

"An office is a public station conferred by the appointment of government. The term embraces the idea of tenure, duration, emolument and duties fixed by law. Where an office is created, the law usually fixes its incidents, including its term, its duties and its compensation."\textsuperscript{131}

The Court pointed out that, in each case, the engineers were free to use their own judgment and discretion, and were required, under the contracts, to use their best professional skill, all of which gave them a liberty of action which excluded the element of control characterizing the relationship between employer and employee. Discussing the basic

\textsuperscript{129}Regulations 77, Income Tax (1933), Art. 643, at 201. For another statement of this principle see Regulations 94, Income Tax (1936), Art. 116-2, at 272-3.
\textsuperscript{130}269 \textit{U. S.} 514 (1926).
\textsuperscript{131}\textit{Id.} at 520.
reasons for the decision, the Court indicated that, in a broad sense, the taxing power of either state or National Government unavoidably has some effect upon the other. The rule of tax-exemption is designed to prevent either government from destroying or substantially curtailing the powers of the other. It therefore results that the rule must be given a practical construction, and must not be extended dogmatically so as to impair seriously the taxing power of the government imposing the tax. In this case, the Court believed that it was not shown that any direct burden was imposed upon any agencies of government. Apparently the Court thought that this tax would not compel the local governments to pay more for their consulting engineers: the tax being non-discriminatory and therefore applying to all on the same terms, competitive conditions would determine the rate of fees.

While there are a few guiding principles of a general nature on this subject, they are still vague and ill-defined, and they have not as yet been woven together into a clear-cut pattern. Accordingly, each case is, or should be, considered in relation to all the facts of the situation. This will appear to be true in examining the many cases having to do with the taxation of attorneys.132 As a rule, attorneys, when engaged by state governments to conduct particular investigations, criminal prosecutions, or civil litigation, while free to accept other employment concurrently, and engaged in public work only temporarily, are considered independent contractors.133 Similarly, attorneys engaged by contract to serve irrigation and reclamation districts,134 or bridge districts,135 have been held taxable. So, also, one who acts as attorney for receivers appointed by a state court is within the category of taxables.136

132See Thompson, The Exemption, for Federal Tax Purposes, of Attorneys' Fees from States and Political Subdivisions of States (1932) 6 Temp. L. Q. 166.
136Elam v. Commissioner, 45 F. (2d) 337 (C. C. A. 7th, 1930).
On the other hand, there are cases which hold that, although the attorney engages in private practice at the same time, he is tax-exempt if it appears that he is sufficiently under the control and guidance of a public authority, is paid a fixed salary, is in fact employed continuously, and gives preference to his public work over his private work.\textsuperscript{137} This is especially true, it has been held, if the office of counsel was created by a statute which also defines his duties.\textsuperscript{138}

So run the cases which are concerned with the federal taxation of attorneys having some connection with municipal governments or other local subdivisions of the state. A leading case on the subject concerned an attorney who was engaged, by contract, to represent several Texas municipalities in certain railroad grade crossing and public utility rate cases. A circuit court of appeals held that the fees which the lawyer received for such services were not subject to the federal income tax, on the ground that the services were rendered in connection with a governmental function.\textsuperscript{139} This decision was reversed by the Supreme Court, however, in a memorandum decision,\textsuperscript{140} on the authority of the Metcalf case. An attorney who is engaged by two municipalities, one paying him a small annual retainer plus fees for bond issues and litigated cases, the other paying him only by means of fees, who maintains his own office and staff, does other private legal work, takes no oath, and fills a position not created by law, with duties which are not prescribed by law, is an independent contractor.\textsuperscript{141} Under similar circumstances, the counsellor for the Des Moines Board of Waterworks Trustees\textsuperscript{142} and a special attorney for the Chicago Sanitary District\textsuperscript{143} have been held to be taxable independent contractors. The Board of Tax Appeals, however, has allowed exemption in a few cases in which the attorney devoted almost all of his time to the city's service, and


\textsuperscript{138}Commissioner v. Harlan, 80 F. (2d) 660 (C. C. A. 9th, 1935).

\textsuperscript{139}Howard v. Commissioner, 29 F. (2d) 895 (C. C. A. 5th, 1928).

\textsuperscript{140}Lucas v. Howard, 280 U. S. 526 (1929).

\textsuperscript{141}Register v. Commissioner, 69 F. (2d) 607 (C. C. A. 5th, 1934). The same conclusion was reached in the following cases dealing with municipal employees, on a similar set of facts: James M. Butler, 19 B. T. A. 718 (1930); E. A. Simpson, 28 B. T. A. 556 (1933); Harry D. Kremer, 31 B. T. A. 566 (1934); Walter G. Winne, 27 B. T. A. 369 (1932); Melvin G. Griffith, 31 B. T. A. 1029 (1935), \textit{petition for review dismissed}, 83 F. (2d) 1010 (C. C. A. 7th, 1936).

\textsuperscript{142}Blair v. Byers, 35 F. (2d) 326 (C. C. A. 8th, 1929).

\textsuperscript{143}Haight v. Commissioner, 52 F. (2d) 779 (C. C. A. 7th, 1931), \textit{cert. denied, sub nom.} Adcock v. Commissioner, 285 U. S. 537 (1932).
was paid on a definite monthly basis, or in which he was unable to engage in any private work which would interfere with his public work, and was under the continuous direction of a governmental superior, or in which his duties were "multifarious and continuous," and the town board could have required all of his time. Similarly, several circuit courts of appeals have ruled that, if the employment of an attorney by a county is continuous, the county commissioners have first call on his time and services, and he always gives preference to his public work, he is tax-exempt, even though he engages in outside practice, especially in those cases in which a statute establishes the office and duties of the attorney. The courts have reached the same conclusion in cases involving the attorney for a school district, and the general counsel for a municipal park district.

The Supreme Court has ruled that consulting engineers, employed by contract to do work on water supply and sewer systems, yet free to accept other employment at the same time, are taxable as independent contractors. As a general rule, when engineers are engaged by contract, do work at the same time for a number of different municipalities, and are paid on the basis of a percentage of the cost of construction, they are considered independent contractors. In one case, however, the Court of Appeals for the District of Columbia reached a different conclusion with respect to the taxation of the compensation of a civil engineer employed by two New Jersey townships. Here the engineer took an oath of office, as required by statute, his compensation was fixed by ordinance at $200 a year plus five per cent of the amount of all contracts for public improvements awarded by the townships, and

---

144 W. B. Mathews, 13 B. T. A. 1133 (1928).
148 Helvering v. Curren, 90 F. (2d) 621 (C. C. A. 2d, 1937).
150 Commissioner v. Schnackenberg, 90 F. (2d) 175 (C. C. A. 7th, 1937).
152 Consoer, Older & Quinlan v. Commissioner, 85 F. (2d) 461 (C. C. A. 7th, 1936); Pease v. Commissioner, 83 F. (2d) 122 (C. C. A. 6th, 1936), cert. denied, 299 U. S. 562 (1936); George W. Fuller, 9 B. T. A. 708 (1927); Edward M. Lynch, 30 B. T. A. 727 (1934); J. Paul Blundon, 32 B. T. A. 285 (1935). In Commissioner v. Modjeski, 75 F. (2d) 468 (C. C. A. 2d, 1935), cert. denied, 295 U. S. 764 (1935), it was held that a consulting engineer employed by the Delaware River Joint Commission, created by the legislatures of Pennsylvania and New Jersey to build a bridge, was taxable, since he devoted only two days a month to this work in a purely consultative capacity, even though he was paid a fixed annual salary.
he engaged in a private practice at the same time. The court held that the compensation he derived from the townships was not taxable, stating that "while it is true that his compensation was dependent upon specific contracts, they were not contracts between the township and himself, but merely the basis of the arithmetic between them." It does not appear that the unusual reasoning of this opinion is in accord with the great weight of authority on the subject.

An architect who is employed by a city board of education, who maintains his own office, is not required to give any certain time to the board, and is free to accept other employment, is an independent contractor. If the architect controls his own office and office expenditures, and his compensation is based upon a percentage of money expended, he is taxable, the court holding that regularity or continuity of work for a fixed or indefinite period, a fixed salary, and full-time employment are the essential criteria of a public office.

Real estate experts who are engaged contractually by municipalities to do valuation work in connection with local improvements, are paid on a per diem or percentage basis, and are employed for an indefinite period or for a particular bit of work involving expert services, are considered independent contractors. Similarly, a rate expert who is employed by various municipalities to do certain work in regard to public utility rates and franchise matters, whose compensation is per diem and agreed upon by an exchange of letters, who uses his own offices and does work for many clients at the same time, is an independent contractor. So, also, is a consulting actuary employed by various public retirement boards under the same conditions. Men

---


154A. Ten Eyck Brown, 19 B. T. A. 568 (1930), aff'd per curiam, 55 F. (2d) 1076 (C. C. A. 5th, 1932), cert. denied, 287 U. S. 602 (1932). So held in R. Clipston Sturgis, 10 B. T. A. 1394 (1928). In Emma B. Brunner, Executrix, 5 B. T. A. 1135 (1927), it was held that an architect employed by two cities on contract was taxable, but that, as a member of the Board of Supervisors having charge of the erection of public buildings in Cleveland, for a period of 18 years, he held a statutory office, the rights, duties and compensation of which were prescribed by statute, and therefore came within the non-taxable group.

155Underwood v. Commissioner, 56 F. (2d) 67 (C. C. A. 4th, 1932). This case was followed in John Reid, Jr., 28 B. T. A. 1217 (1933), which dealt with the city architect of San Francisco, who maintained his own office and staff, had a private practice at the same time, and was paid by the city on a percentage basis.

156Lyons v. Reinecke, 10 F. (2d) 3 (C. C. A. 7th, 1925); Mesce v. United States, 64 Ct. Cl. 481 (1928), cert. denied, 278 U. S. 612 (1928); Edgar N. Finn, 31 B. T. A. 439 (1934), aff'd mem., 81 F. (2d) 1018 (C. C. A. 2d, 1936); Harry Goldstine, 33 B. T. A. 173 (1935).


who are engaged by contract to index public records, or to direct a city port, or to collect delinquent taxes, have been held subject to the federal income tax. The full-time director of the cafeterias of a city’s public school system, however, who is paid a fixed annual salary, has been held to be a tax-exempt municipal employee. The same conclusion was reached in a case involving the taxability of the compensation of a pathologist in the Boston City Hospital; he was held to be a bona fide employee even though he did other work and had additional income, the court basing its decision upon the fact that he worked regular hours and was continuously employed for many years, under the control of the hospital board of trustees, and upon the further fact that his other services were not carried on during his regular hours and did not interfere with his hospital duties.

One who contracts with a city for the construction or repair of public buildings, or for the paving of streets, or for the collection and disposition of waste materials, or one who, by contract, furnishes such equipment as horses and carts or school busses, is not a public employee, but clearly an independent contractor. Thus, also, one who deals in the open market in municipal securities, which he buys through competitive bidding or by arm’s length negotiation, is not a public employee, and the effect upon government of a tax upon the income he derives from such dealings is remote and insignificant. It is well established that the mere fact that one has a profitable contractual relationship with government does not make him a public officer, and this rule has often been applied to contractors who seek immunity from state taxation on the ground that they are federal instrumentalities.

159 Russell v. Heiner, 45 F. (2d) 872 (W. D. Penna. 1930).
162 Hoskins v. Commissioner, 84 F. (2d) 627 (C. C. A. 5th, 1936).
164 Kreipke v. Commissioner, 32 F. (2d) 594 (C. C. A. 8th, 1929).
165 James A. Sackley Co. v. United States, 65 Ct. Cl. 304 (1928), cert. denied, 278 U. S. 609 (1928).
167 Edwin T. Foreman, 10 B. T. A. 981 (1928).
168 Suburban Transportation System, 29 B. T. A. 1106 (1934).
Finally, it may be noted that, in order to establish immunity from federal taxation, it must generally be shown that the compensation in question is in reality derived from the state or its subdivisions, and not from some other source.\textsuperscript{171} Thus, neither an auditor nor examiner who is appointed by a local court to report on the financial standing of corporations applying for approval as sureties, and whose compensation is derived from the corporations examined,\textsuperscript{172} nor an executor whose compensation comes from the estates administered,\textsuperscript{173} is within the rule of tax-exemption, for their compensation is not derived from the state. Pilots, therefore, are subject to the federal income tax although they are appointed by a public authority and although their duties are to a great extent regulated by law; they are paid by the private parties they serve, and are engaged merely in a private business.\textsuperscript{174} Thus, also, the salary of the president of the New York Society for the Prevention of Cruelty to Children was held subject to the federal income tax although the city of New York contributes half of the income of the society. This ruling was on the ground that the society is not a governmental agency; that, rather, it is a private corporation free, in general, from the control of the state.\textsuperscript{175} There were a few cases holding otherwise; for example, bank liquidators, paid out of bank assets, had been considered tax-exempt,\textsuperscript{176} until a recent Supreme Court decision reversed these cases and held such liquidators subject to federal taxation.\textsuperscript{176a}

\textsuperscript{171}See Smith, \textit{Federal Taxation of State Officers and Employees} (1937) 15 \textit{TAX MAG.} 443.


\textsuperscript{175}Lindsay \textit{v. Bowers}, 17 F. (2d) 264 (S. D. N. Y. 1927). The New York Court of Appeals had already held that the society was a private philanthropic organization, and therefore not subject to visitation by the state board of charities. People \textit{ex rel. Board of Charities \textit{v. New York Soc. P. C. C.}}, 161 N. Y. 233, 55 N. E. 1063 (1900).


\textsuperscript{176a}\textit{Helvering \textit{v. Therrell}}, 58 Sup. Ct. 539 (1938), \textit{rev'g} the \textit{Therrell}, \textit{Tunnicliffe}, and \textit{Freedman cases}, cited supra note 176.
The question as to the source from which compensation is derived has achieved a new significance in recent years due to the fact that under a growing system of federal grants-in-aid and federal relief expenditures, many local officers derive their salaries in whole or in part from federal sources. Of course, the Federal Government may require those who are paid from the Federal Treasury to pay income taxes, inasmuch as such taxes do not come within the principle of intergovernmental taxation. The Bureau of Internal Revenue recently stated the rule as follows:

“If all or part of the compensation of an officer or employee of a State or political subdivision thereof is paid directly or indirectly by the United States, such compensation (or part) is taxable, as for example, any compensation paid by the United States to officers of the National Guard of a State, or compensation paid by a State to officers or employees of an agricultural school or college wholly or partly out of grants from the United States.”

Accordingly, the Bureau has ruled that officers and employees of state emergency relief administrations are tax-exempt only in so far as they are paid by the state from its public funds; that, on the other hand, their compensation, to the extent that it is paid by the state either directly or indirectly from funds granted by the Federal Government, under the provisions of the Federal Emergency Relief Act, is subject to the federal income tax. The same ruling has been announced with respect to an employee’s compensation derived from funds granted to a state for the administrative expenses of an unemployment insurance act.

V

One must proceed with caution in seeking to generalize with respect to the distinction between taxable independent contractors and non-taxable public officers or employees. The Supreme Court has declared that “Just what instrumentalities of either a state or the federal government are exempt from taxation by the other cannot be stated in terms of universal application.” While a line must be drawn between those activities which are taxable, and those which are immune, “Experience has shown that there is no formula by which that line may be plotted with precision in advance.” Accordingly, each particular case must be decided upon the basis of its own facts. The law on the subject is being developed by the process of “gradual inclusion and

177 Regulations 94, Income Tax (1936), Art. 116-2, at 274.
179 I. T. 2859, XIV-1 CUM. BULL. 101 (1935).
exclusion” so characteristic of the development of the due process of law concept. Judge Graham of the Court of Claims has expressed this thought as follows:

“It is not possible, in the twilight that exists between the boundaries of what constitutes the relation of master and servant and an independent contractor, to draw a fixed line. The constantly varying varieties of human employment under present-day conditions necessarily render it so, and each case must of necessity, to a great degree, be decided upon its own facts.”

First, it should be noted that the burden of proof rests upon the person claiming exemption. This is necessarily so, for the taxing power is an expansive and highly essential power of government which ought not to be limited except in case of manifest necessity. In fact, a circuit court of appeals recently asserted that the burden of proof not only falls upon the instrumentality or individual seeking exemption, but that the burden in the court is greater than it was before the Board of Tax Appeals: before the Board it was sufficient if the exemption was established by a “preponderance of the evidence,” while in the court it must be shown “that there was no substantial evidence to support a finding that it was not an officer or employee of the municipality. . . .” Furthermore, in applying national tax statutes, the federal courts need not adopt state definitions as to whether or not a particular person is a public officer, nor is the court bound by the fact that the taxpayer has the formal title of a public officer. Nor need the federal courts accept the definitions of the Bureau of Internal Revenue inasmuch as the exemption is a matter of constitutional right, and “neither legislative enactment nor departmental regulation may whittle down that right.”

Although a number of the cases, holding claimants of tax-exemption to be independent contractors, point to the absence of an oath of office, this is not a conclusive fact; it is merely one of the facts to be taken into consideration. For example, there have been cases wherein men were held to be independent contractors in spite of the fact that they took an oath of office. A large number of the cases emphasize the

---

182 Mesce v. United States, 64 Ct. Cl. 481, 494 (1928), cert. denied, 278 U. S. 612 (1928)
184 Pease v. Commissioner, 83 F. (2d) 122 (C. C. A. 6th, 1936), cert. denied, 299 U. S. 562 (1936). Here the court ruled that a civil engineer was an independent contractor, in face of a previous decision of the highest court of the state, Wright v. Clark, 119 Ohio St. 462, 164 N. E. 512 (1928), which held a similar civil engineer to be a public officer.
186 Commissioner v. Murphy, 70 F. (2d) 790 (C. C. A. 2d, 1934), cert. denied, 293 U. S. 596 (1934); Buckner v. Commissioner, 77 F. (2d) 297 (C. C. A. 2d, 1935); Watson v. Commissioner, 81 F. (2d) 626 (C. C. A. 3d, 1936); Walter G. Winne, 27 B. T. A. 369
absence of a fixed and regular salary, in that compensation takes the form of a contingent fee, or is based upon a percentage of the costs involved, or upon some other variable and particular consideration; whereas, the presence of a fixed annual salary is not a conclusive fact, in itself, to establish a claim for exemption.\textsuperscript{187} The facts most frequently stressed, as tending to show that the claimant is an independent contractor, seem to be: that he is free to accept other employment at the same time; that his duties are prescribed by contract and not by statute or ordinance; that he maintains his own office and office force, and controls the work himself; that he is free to use special skills, or discretion, or his own judgment, in doing his work;\textsuperscript{188} and that he has no fixed tenure, works for no specified period of time, or only part time, or devotes but very little time to the work in question.

A similar indefiniteness necessarily results from any attempt to rationalize the cases in which immunity from federal taxation has been allowed. Thus, in many cases it has been held that one pertinent query is whether or not the claimant is under the control of public authorities, or whether or not his duties are prescribed by law; nevertheless, two federal circuit courts of appeals have very recently ruled that whether or not the claimant could use his own discretion is not a conclusive point, that rather, it is merely one of the elements to be considered, and that one may be entirely self-directed and still be an official or employee.\textsuperscript{189} It is emphasized, in some instances, that the taxpayer took an oath of office; yet it is held, elsewhere, that the omission of an oath of office is not necessarily a conclusive fact.\textsuperscript{190} The absence of a contract is cited to show that the taxpayer is not an independent contractor; on the other hand, the fact that the engagement is by contract has been held not to be fatal to the claim of exemption.\textsuperscript{191} Ordinarily, a point of great per-

(1932); E. A. Simpson, 28 B. T. A. 556 (1933); Melvin L. Griffith, 31 B. T. A. 1029 (1935), petition for review dismissed, 83 F. (2d) 1010 (C. C. A. 7th, 1936).


\textsuperscript{188}Underwood v. Commissioner, 56 F. (2d) 67, at 71 (C. C. A. 4th, 1932): "In short, it is very generally held that the right to control the manner of doing the work contracted for is the principal consideration in determining whether one is employed as an independent contractor or a servant."

\textsuperscript{189}Helvering v. Curren, 90 F. (2d) 621 (C. C. A. 2d, 1937); Commissioner v. Harlan, 80 F. (2d) 660 (C. C. A. 9th, 1935): "The test of his status is not the amount of control exercised over him in the performance of his duties, but whether he is an officer."


\textsuperscript{191}Halsey v. Helvering, 75 F. (2d) 234 (App. D. C. 1934); W. B. Mathews, 13 B. T. A. 1133 (1928).
suasiveness in establishing the status of a public official or a bona fide public employee is that the claimant devotes his full time to the public work in question, works regular hours, and has a definite term of employment; yet it has often been held that it is not a conclusive fact that the taxpayer does work in addition to his public work, if the public authority has first claim on, and might require all of, his time, or if his outside work does not interfere with his public work, to which latter he gives preference, or if, in fact, he devotes most of his time to such public work. Similarly, the absence of definite working hours or term of employment is not always conclusive; it often suffices if the taxpayer has been, in fact, in continuous service, especially for a long period of time. Finally, the payment of a fixed, regular salary is an element frequently given great weight in determining that an individual is a public officer or employee; yet the Board of Tax Appeals has ruled that payment per diem is not a fatal defect. Judge Hand recently stated that the test is not whether the "official" is self-directed, but whether the engagement is by the job (piece-work). Circuit Judge Wilbur has asserted that whether or not the taxpayer has a definite term of office, or is free to use his own discretion, are merely elements to be considered, and not finally conclusive of the point; the true test of his status, rather, is whether or not he is an officer. Perhaps this is as good a formula as any, for it is certain that no exact formula is deducible from the recorded decisions. All that can be said with any accuracy is that there are many different facts to be taken into consideration, that they are given a varying amount of emphasis, and that

---


198Helvering v. Curren, 90 F. (2d) 621 (C. A. 2d, 1937).

at some point the judicial "hunch" must be a factor in determining whether or not a given individual is a non-taxable public officer or employee.

VI

Mr. Justice Roberts wrote, in his dissenting opinion in the Brush case,\(^{200}\) that the decisions of the Supreme Court in the cases dealing with intergovernmental taxation "have not furnished the executive a consistent rule of action." In this connection he said:

"The need of equitable and uniform administration of tax laws, national and state, and the just demand of the citizen that the rules governing the enforcement of those laws shall be ascertainable require an attempt at rationalization and restatement."

Any effort at rationalization, however, should first take into account certain basic considerations which underlie the whole problem. To begin with, it ought to be noted again that the taxing power is a basic, fundamental and indispensable power without which government could not exist.\(^{201}\) Therefore, as the Bureau of Internal Revenue has suggested, "The protection of the sovereign power of the Federal Government to levy and collect taxes is no less important than the protection of governmental activities of States and political subdivisions."\(^{202}\) While the principle of tax-immunity may be an important matter, the Supreme Court once pointed out that "The limitation of this principle to its appropriate applications is also important to the successful working of our governmental system."\(^{203}\) Accordingly, when a taxpayer claims the benefit of an exemption from taxation, the burden of proof is upon him to show clearly that he is within the exemption claimed.\(^{204}\) He should, above all, be compelled to show that his claim is within the basic purposes of the rule of intergovernmental taxation, which is "... that each government, in order that it may administer its affairs

\(^{200}\) Brush v. Commissioner, 300 U. S. 352, 375 (1937).

\(^{201}\) Nicol v. Ames, 173 U. S. 509, 515 (1899): "The power to tax is the one great power upon which the whole national fabric is based. It is as necessary to the existence and prosperity of a nation as is the air he breathes to the natural man. It is not only the power to destroy, but it is also the power to keep alive."


within its own sphere, must be left free from undue interference by the other.\textsuperscript{206}

Whether or not any particular taxpayer is entitled to an exemption, therefore, should not be decided upon the basis of legal dialectic and abstract formula; rather it should be determined through an examination of all the facts in the case, in order to find out whether or not a unit of government is in reality discriminated against or burdened by the tax.\textsuperscript{206} In a recent case, the Circuit Court of Appeals for the Fifth Circuit expressed this thought in the following language:\textsuperscript{207}

"A constitutional question of great importance is involved. The correct answer to it is more aptly to be found in a painstaking examination of the facts and circumstances in evidence than in hairsplitting technicalities of pleading, however necessary such rules may be ordinarily. The law arises out of the facts in all cases, but, in determining what instrumentalities of a state are exempt from taxation by the federal government, the maxim requires special emphasis. Legal formulas are helpful to classify state activities, but in close cases it becomes necessary to examine the particular facts to determine whether the special instrumentality falls within the category of private business subject to tax or governmental function exempt therefrom."

Even so, the essential problem still remains: what question is to be answered by an examination of the facts? Is it merely to discover the naked fact of a tax upon an instrumentality of government, or is it to find out whether or not, in reality, a burden or discrimination against a unit of government is present?

The Supreme Court has stated, and frequently acted upon, the theory that the exemption is absolute, and not a question of degree. On one occasion it asserted that "Where the principle applies it is not affected by the amount of the particular tax or the extent of the resulting interference, but is absolute."\textsuperscript{208} On the other hand, there is an encouraging

\textsuperscript{206}Metcalf & Eddy v. Mitchell, 269 U. S. 514, 523 (1926).

\textsuperscript{207}The problem is not one of logical or legal absolutes, but of the promotion of a smooth practical interrelation of the two in recognition of their several sovereign necessities." Montgomery B. Case, 34 B. T. A. 1229, at 1245 (1936).

\textsuperscript{208}Regents v. Page, 81 F. (2d) 577, 582 (C. C. A. 5th, 1936).

\textsuperscript{209}Indian Motorcycle Co. v. United States, 283 U. S. 570, 575 (1931). Speaking of the principle enunciated in M'Colloch v. Maryland, Mr. Justice Holmes wrote, in Johnson v. Maryland, 254 U. S. 51, at 55 (1920): "The decision in that case was not put upon any consideration of degree but upon the entire absence of power on the part of the States to touch, in that way at least, the instrumentalities of the United States; . . . and that is the law today." In Trinityfarm Construction Co. v. Grosjean, 291 U. S. 466, at 471 (1934), the Court stated: "Its application does not depend upon the amount of the exaction, the weight of the burden or the extent of the resulting interference with sovereign independence. Where it applies, the principle is an absolute one wholly unaffected by matters or distinctions of degree." See also: Gillespie v. Oklahoma, 257 U. S. 501 (1922); Panhandle Oil Co. v. Mississippi, 277 U. S. 218 (1928); Burnet v. Coronado Oil
and growing tendency on the part of the federal courts to approach this problem more realistically, by trying to premise decisions upon a finding as to whether or not a government is, in actual fact, burdened or discriminated against. Thus, for example, in a number of cases wherein individuals held leases on restricted Indian lands, or had contracts with the Federal Government, or possessed federal licenses, and wherein the Congress had not expressly stipulated exemption from local taxation, tax-immunity has been denied on the theory that the effect of the local tax in question upon the Federal Government was only remote and inconsequential.209 Likewise, in many cases, particularly in recent years, the courts have sustained federal taxes levied against individuals holding contracts or leases with local governments, or having some other real or fancied relationship to them.210 As the Supreme Court stated in a

---

156 The Georgetown Law Journal [Vol. 27


In Railroad Company v. Peniston, 18 Wall. 5, at 36 (U. S. 1874), Mr. Justice Strong wrote: "It is, therefore, manifest that exemption of Federal agencies from State taxation is dependent, not upon the nature of the agents, or upon the mode of their constitution, or upon the fact that they are agents, but upon the effect of the tax; that is, upon the question whether the tax does in truth deprive them of power to serve the government as they were intended to serve it, or does hinder the efficient exercise of their power."

recent case,\textsuperscript{211}

"This Court, in drawing the line which defines the limits of the powers and immunities of state and national governments, is not intent upon a mechanical application of the rule that government instrumentalities are immune from taxation, regardless of the consequences to the operations of government."

The growing tendency of the courts to consider the real effects of an intergovernmental tax represents a highly desirable development in American Constitutional law.\textsuperscript{212} For, fundamentally, the complete exemption of state instrumentalities from federal taxation rests upon an insecure foundation. It is not inappropriate to suggest once more that, after all, the Sixteenth Amendment does give the Congress the power to tax incomes, "from whatever source derived,"\textsuperscript{213} and that, at best, the exemption of state instrumentalities from federal taxation rests not upon any express constitutional restriction, but only upon "an asserted implication."\textsuperscript{214} Furthermore, it is a basic principle of our constitutional law that, within the sphere of its delegated powers, the Federal Government is supreme. The Court has recently held that state instrumentalities are subject to the superior authority of the national commerce power, and that the nature of the instrumentality affected, whether governmental or proprietary, is an irrelevant matter.\textsuperscript{215} It is difficult to discover any real difference between the nature of the commerce power and the nature of the taxing power that would justify the two different approaches used when state instrumentalities are concerned. Despite the tender solicitude which the Court has exhibited for states’ rights during the past few years,\textsuperscript{216} there is reason to hope that the area of tax-immunity

\begin{itemize}
\item \textsuperscript{212}Educational Films Corp. v. Ward, 282 U. S. 379, 391 (1931).
\item \textsuperscript{213}Powell, National Taxation of State Instrumentalities, c. 7; Dowling, Cheatham and Hale, \\textit{Mr. Justice Stone and the Constitution} (1936) 36 Col. L. Rev. 351, 353-7; (1935) 35 Col. L. Rev. 301; (1932) 81 U. of Pa. L. Rev. 194; (1936) 84 U. of Pa. L. Rev. 758.
\item \textsuperscript{214}See Hubbard, \\textit{The Sixteenth Amendment} (1920) 33 Harv. L. Rev. 794.
\item \textsuperscript{215}Willcuts v. Bunn, 282 U. S. 216, 231 (1931).
\item \textsuperscript{216}United States v. California, 297 U. S. 175, 183 (1936): "Despite reliance upon the point both by the government and the state, we think it unimportant to say whether the state conducts its railroad in its 'sovereign' or in its 'private' capacity. . . . The only question we need consider is whether the exercise of that power, in whatever capacity, must be in subordination to the power to regulate interstate commerce, which has been granted specifically to the national government." Board of Trustees v. United States, 289 U. S. 48, 57 (1933): "The principle of duality in our system of government does not touch the authority of the Congress in the regulation of foreign commerce."
\item \textsuperscript{217}Schechter v. United States, 295 U. S. 495 (1935); United States v. Constantine, 296
will, in the future, be restricted rather than expanded. There is a tendency, although it is, perhaps, not very pronounced, which is favorable to the idea that, in order to justify a tax-exemption, it must be shown affirmatively that there is either a direct burden on, or a discrimination against, some unit of government.

VII

Because of the inadequacy of available statistics, it is very difficult to determine the net effect of the rule of intergovernmental taxation upon federal revenue. The Treasury Department has estimated that in 1935 the outstanding securities issues of state and local subdivisions amounted to about 19 billions of dollars. The corresponding annual interest charge has been put at 718 millions. How much of this could be reached by the federal income tax cannot be determined without knowing exactly how local securities are distributed, although it may perhaps be assumed that the bond-holding class is, for the most part, a taxable class. With respect to the salaries of local employees, the sheer number of local governments and employees may first be noted.


It is not without interest to note that the federal system of Canada does not require the rule of reciprocal tax-immunity. Thus, a province may tax a bank chartered by the Dominion Government, Bank of Toronto v. Lambe, 12 App. Cas. 575 (1887), the salaries of Dominion civil servants, Forbes v. Attorney-General for Manitoba, [1937] A. C. 260, or the salaries of Dominion judges, The Judges v. Attorney-General for Saskatchewan, 53 T. L. R. 464 (1937). So also, in Australia, a state may tax the income of a federal officer, Webb v. Outrim, [1907] A. C. 81. See also, Powell, M’Culloch v. Maryland in Canada and Australia (1933) 31 Mich. L. Rev. 797.

Powell, National Taxation of State Instrumentalities 98-99, brings out the interesting facts that between 1871 and 1934, the years of decision for The Collector v. Day and Ohio v. Helvering respectively, 18 cases came to the Supreme Court on the subject of the national taxation of state instrumentalities; that of the 8 cases in which immunity from taxation was upheld, only 3 were decided unanimously; while in the 10 cases in which immunity was denied, all except the first, South Carolina v. United States, were concurred in unanimously.

Mr. Justice Roberts, dissenting in Brush v. Commissioner, 300 U. S. 352, at 375 (1937), wrote: "It seems to me that the reciprocal rights and immunities of the national and a state government may be safeguarded by the observance of two limitations upon their respective powers of taxation. These are that the exactions of the one must not discriminate against the means and instrumentalities of the other and must not directly burden the operations of that other."


There are about 175,000 political jurisdictions in the United States, of which 16,366 are incorporated municipalities, and 127,000 are school districts. An authoritative study estimated that in 1932 there were 3,278,500 public employees in the country, that is to say about one-tenth of all those gainfully employed; of these, 252,000 were employed by the states, 591,500 by the municipalities, and 1,189,000 were engaged in public education. It has been estimated that the cities and towns of the United States employ more than a million full-time workers.

Of course, the annual salaries and wages of this army of public employees, in the aggregate, constitute a tremendous income. Students of public administration say that one-half of operating public expenditures go for wages and salaries, and that in 1932 public wages and salaries amounted to $4,520,954,000, which was 11.5 per cent of the total national income. Of this huge figure, municipal salaries included about twenty per cent of the total, $895,539,000, and counties, townships and special districts accounted for another ten per cent. The general average wage and salary level, however, is quite low, an authoritative estimate holding that the average compensation for full-time, permanent employees in all American municipalities in 1932 was $1,514, while in 1933 it was $1,259. Indeed, it was stated by Mr. Roswell Magill, while Under-Secretary of the Treasury, that the average salary of the state or municipal employee is so low that the possible tax yield from this source is not worth all the bother of current litigation, his estimate being that the revenue from this source would be less than $15,000,000 at the 1936 rates. On the other hand, the staff of the Joint Committee on Internal Revenue Taxation estimates that the annual revenue from state and local salaries now exempt would amount to about $45,000,000. Furthermore, it may be noted that, although the general average salary


224 Mosher and Kingsley, Public Personnel Administration (1936), at 40.

225 Ibid.

226 Better Government Personnel, at 90, 139.

227 Ibid. at 90.

228 Ibid. at 165.


230 Youngquist, Elimination of Intergovernmental Exemptions Based on Federal and State Sovereignty (1937) 15 Tax Mag. 649.
of municipal employees is about $1,500 a year, the figure represents only a composite average, and that many particular classes are well above this level. For example, the average annual compensation of police department employees in cities of 30,000 or over was, in 1932, $2,324, and for fire department employees, $2,299;231 six and seven-tenths per cent of all public employees in New Jersey, and about five per cent in Ohio, earned $3,000 or more in 1932.232 The average salary of 121,785 employees of 59 cities of New York in the same year was $2,144, while for 67,770 in the competitive class the average was $2,579.233 The average salary of 239,829 employees in eleven cities over 500,000 was $2,132 in 1936, while the average salary of 496,958 employees of 781 cities over 10,000 was $1,765 in the same year.234 If the income tax base is ever broadened, municipal salaries may become a considerable source of revenue.

In estimating the effect upon federal revenue of the rule of intergovernmental tax-immunity, it is also necessary to look beyond current salary averages to the general trend of local activity. This is clearly in the direction of municipal socialism. In 1932, for example, there were 92,500 persons employed by municipal public utilities,235 and there are today about 1800 municipal electric plants in the United States.236 More and more, cities are establishing bus lines, gas works, heating plants, docks and wharves, tunnels, depot terminals, airports, ice plants, and the like.237 This expanding local collectivism, hastened by the current depression, may in time reach such a point that its effect upon federal revenue will become pronounced.

One other consequence of the rule of intergovernmental tax-exemption has become apparent since the enactment of social security legislation by the Federal Government. The taxing power of the United States

232 Id. at 169.
233Fiftieth Annual Report, Department of Civil Service, State of New York (1933), at 54 ff.
234Municipal Yearbook (1937), at 267.
may be used, it is now clear, not only as a method of compelling individuals or corporations to contribute to the support of government, but also as a basis for a positive social policy, from the scope of which local public employees will necessarily be excluded. The Social Security Act of 1935 specifically exempts from the term "employment" as used in the Act, "Service performed in the employ of a State, a political subdivision thereof, or an instrumentality of one or more States or political subdivisions." The Bureau of Internal Revenue has interpreted the sweeping language of the statutory exemption to include all agencies of government, "... without distinction between those exercising functions of a governmental nature and those exercising functions of a proprietary nature." The rule of intergovernmental tax-immunity may thwart, in the future, at least in some measure, a national social policy premised upon an exercise of the taxing power.

Many proposals have been made to amend the Constitution in order to abolish the exemption of state and local securities and officials from federal taxation. Two joint resolutions are now pending in the Senate which propose to amend the Constitution to this end: one would abolish the exemption of both federal and state securities, the other would add the abolition of the exemption for state officers and employees. Although the exemption of state instrumentalities is based upon a highly questionable interpretation of the Constitution, and could be removed by the application of a fresh outlook upon the nature of federal supremacy, it is unlikely that such a drastic judicial volte face will ever occur. It is generally agreed that a constitutional amendment would be necessary in order to restore to the Federal Government its power to tax incomes "from whatever source derived."

---

1938] Federal Taxation of Municipal Employees 161

---

239 Tit. II, § 210 (b) (6) (old age benefits); Tit. VIII, § 811 (b) (7) (old age taxes); Tit. IX, § 907 (c) (6) (unemployment taxes).
240 Regulations 90, Art. 206 (5)-(6); Regulations 91, Art. 11.
242 Youngquist, Elimination of Intergovernmental Exemptions Based on Federal and State Sovereignty (1937) 15 TAX MAG. 649.
THE PARKING LOT CASES
LAURENCE M. JONES*

I.

THOUSANDS of automobiles are driven into parking lots and left in charge of the attendants without any consideration of the legal relation thus established between the parking lot operator and the owner of the car. The problem is new, one might almost say it has arisen within the last decade, for although there are a few cases arising before then they do not involve the typical parking lot situation. Like all new situations it has given the courts some trouble. Most of the difficulty has arisen from an attempt to apply settled principles of law to a new problem, from an attempt to apply an old rule to a new case. The courts have proceeded by a method which has well been termed a "jurisprudence of conceptions." They have tried to fit the relation existing between the owner of the parked automobile and the operator of the parking lot into one of the recognized legal relations of bailor-bailee, lessor-lessee or licensor-licensee, and then assumed that the obligations of the parties flowed automatically from that relationship. However much one may abhor that method of approach, since courts and lawyers do think and speak in terms of bailment, lease, or license, it seems worth while to consider the parking lot cases and to determine, if possible, which of the above terms most accurately describes the relation.\(^2\)

To attempt to reach a conclusion as to the nature of the relation between an operator of a parking lot and the owner of a parked car by counting the cases would be to follow an even more mechanical jurisprudence than that which has been attributed to the courts in deciding them.\(^3\) One must first classify the transactions into groups according to the manner in which the business is conducted, and then

---

\(^*\)A.B. University of Iowa (1930), J.D. Id. (1932); LL.M. Harvard University Law School (1933), S.J.D. Id. (1934); Member of the Iowa Bar; Assistant Professor of Law, Lamar School of Law, Emory University; author of Constitutional Provisions Regulating the Mechanics of Enactment in Iowa (1935) 21 IOWA L. REV. 79; Some Constitutional Limitations on State Sales Taxes (1936) 20 MINN. L. REV. 461.

\(^1\)Pound, Mechanical Jurisprudence (1908) 8 COLUM. L. REV. 605.

\(^2\)The writer makes no attempt in this article to discuss in general the elements of the above relations, but limits himself to a consideration of their application to the parking lot cases.

\(^3\)Recently, a writer made the statement that most of the parking lot cases adopt the view that the transaction is a lease. BROWN, PERSONAL PROPERTY (1936) 238. An earlier writer stated that the operator of a parking lot was a bailee for hire. BERRY, LAW OF AUTOMOBILES (4th ed. 1924) § 1414. Neither statement, as the following review of the cases indicates, is accurate.
consider the decided cases and see what obligations the courts have imposed on the parties, and whether any of the recognized relationships implies such obligations. Although there are, of course, infinite variations, parking lots may be divided into two types: first, those where the attendant merely collects the fee and designates the area in which to park, the driver himself doing the parking and retaining complete control over the car, locking it or not as he wishes; and second, those lots, usually enclosed, where the attendants take complete charge of the car at the entrance, park it, retain the keys and move the car about as necessary, giving the driver a check or ticket, upon presentation of which they deliver the car to him. In considering the cases, situations involving lots of the first type will be discussed first.

II.

The first of the parking lot cases to reach the courts was *Pennyroyal Fair Association v. Hite.*4 In that case the plaintiff, accompanied by others, drove his car to the fair grounds and paid the gatekeeper twenty-five cents for the privilege of parking it inside the fence. The gatekeeper did not exercise any actual physical control or authority over the car other than to indicate where it should be parked. The car was stolen and the fair association was held liable. The court indicated it considered the defendant a bailee of some sort but did not discuss its common law liability as such, since the case was tried and decided on the theory of a special agreement making the association an insurer. The plaintiff and his friends testified to making such an agreement with the gatekeeper, and the jury so found. The case therefore does not shed much light on the nature of the relation between the driver of a car and the operator of a parking lot, although it is interesting as an early case in which the court assumed the relation to be that of bailor and bailee, even though there appears to be a total lack of the physical control or possession necessary to constitute a bailment. The only possession which the defendant had is that which resulted from the car being within the enclosed fair grounds, and that possession, if it may be called such, seems hardly sufficient to constitute a bailment.5 However, on the theory of a special contract the defendant might well be liable irrespective of whether or not there was a technical bailment of the car.

---

4195 Ky. 732, 243 S. W. 1046 (1922).

5The requirement of possession on the part of the bailee is elementary, but what constitutes possession has caused the courts and writers some difficulty. For some recent discussions of the problem generally see, Bingham, *The Nature and Importance of Legal Possession* (1915) 13 Mich. L. Rev. 535, 623; Shartel, *Meanings of Possession* (1932) 16 Minn. L. Rev. 611; Brown, *Personal Property* (1936), Special Note on Possession, pp. 18-21.
Within two years after the Hite case was decided three other cases arose involving similar situations. In Suits v. Electric Park Amusement Company the plaintiff drove his car to an amusement park operated by the defendant and paid the entrance fee for himself and his companions. He parked the car in the space to which he was directed and locked the ignition. The park was completely enclosed except for one entrance and one exit at which attendants were on duty, but no extra charge was made for the privilege of parking cars inside the park. No system of checks or tickets was used and a car could be driven out at any time by any person without interference by the employees. The man directing the parking of cars within the park was a city policeman. The court held there was no bailment of the car and consequently the defendant was not liable for the loss of the car by theft. The essential element of possession, on the part of the amusement company, was lacking; there was not sufficient control over the car to make the defendant a bailee. The plaintiff tried to argue by analogy from the garment cases, where a customer in a store hands his hat or coat to a clerk or deposits it on the counter while trying on new clothes; but the court distinguished them, saying the storekeeper impliedly invited the customer to deposit the garment with him. The implied invitation to make the deposit would seem as strong in the present case, but the cases may be distinguished in that in the amusement park case the defendant did not purport to exercise any control over the thing deposited or to return it safely to the owner. All the defendant gave and all the plaintiff received was a privilege to park his car within the confines of the amusement park. That, in the absence of a special agreement such as was found in the Hite case, would not impose any duty on the amusement company to care for the car, nor any liability in case of its loss or destruction.

In an Oklahoma case, decided in the same year, the court again held the defendant not liable for the theft of a car parked within its grounds. The plaintiff and his family drove to the state fair and paid the entrance fee of fifty cents per person and twenty-five cents for their car. No system of checks or tickets was employed and at no time did the plaintiff ever turn over the physical control or possession of the car to the defendant. The car was parked, by the plaintiff, near the livestock pavilion from which it was stolen. Here again the court said there was no bailment and thus no liability. They defined a bailment as "a delivery of personalty for some particular purpose, or on mere deposit" and concluded:

---

*213 Mo. App. 275, 249 S. W. 656 (1923).

*Lord v. Oklahoma State Fair Ass'n, 95 Okla. 294, 219 Pac. 713 (1923).*
"The most that is shown by the evidence is that the plaintiff paid the defendant the sum of 25 cents for the privilege of taking the car within the defendant's inclosure, and that this was done for his own convenience, and without any thought upon the part of either of the parties that such car was either actually or constructively in the possession of the defendant."8

Since there was never any delivery of the actual control or custody of the car to the defendant, no bailment existed and no liability as bailee could be imposed on the fair association. And in the absence of some special contractual obligation the defendant would not be liable for the the loss of the car merely by reason of the grant of the license to park within its grounds.

In *Ex Parte Mobile Light & Railway Company*9 the plaintiff's son drove the car into a park operated by the defendant and left it while he attended a ball game. A charge of fifteen cents was made for entrance to the park; one attendant collected the fee and another directed the parking of the cars. A check was given all persons, which stated that the defendant charged only for the privilege of parking and assumed no responsibility for loss of, or damage to, the car. The car was stolen and the plaintiff sought to recover its value. Upon a demurrer to the complaint the court held there were not sufficient facts alleged to impose liability on the defendant. The court concluded there was no bailment, with the resulting duty to exercise reasonable care for the safekeeping of the car, for "An essential element of bailment is possession in the bailee",10 and here possession or control of the car was lacking. Neither could the court find anything in the manner of conducting the business which would impose upon the defendant a duty to guard the cars. There was no special contract, either express or implied, imposing any duty of due care on the defendant. As for the limitation of liability printed on the check handed the plaintiff's son, the court considered it in the nature of a receipt containing an "element of contract defining the subject matter of the transaction and the duties of the respective parties."11 However, they did indicate that if the defendant had incurred any duty toward the plaintiff in caring for the car, it could not have restricted its liability for the result of its own negligence by any such limitation.

The Tennessee court, in *Chattanooga Interstate Fair Association v. Benton*,12 held the defendant liable for the theft of a car parked within

---

8 *Id.* at 296, 219 Pac. at 714.
9 211 Ala. 525, 101 So. 177 (1924). In connection with this case there is an annotation on the liability of the operator of a parking lot in (1924) 34 A. L. R. 925.
10 211 Ala. 525, 526, 101 So. 177, 178,
11 *Id.* at 527, 101 So. at 179.
12 5 Tenn. App. 480 (1927).
its grounds. The plaintiff drove his car into the fair grounds, paying the gatekeeper a fee of fifty cents for the admission of the car. The gatekeeper informed the plaintiff, "We are responsible for your car and will take care of it." There were other attendants who directed the parking of cars within the grounds, but there was no evidence to show the exact manner in which the business was conducted or the extent of the control the defendant exercised over the cars. Although the court talked in terms of a bailment and the liability of a bailee, the case may be properly disposed of on the theory of a special contract made by the plaintiff with the gatekeeper. The case is similar to the Hite case, and, as in it, the defendant was properly held liable whether or not there was a technical bailment of the car.

In a case decided last year, an English court held the operator of a parking lot was not liable for the loss of a car stolen from the lot. The lot in question was triangular in shape with two sides open, and the plaintiff locked his car when he parked it but left the windshield open. He paid a fee of one shilling for parking the car and received a ticket containing the following printed provision:

"The proprietors do not take any responsibility for the safe custody of any cars or articles therein nor for any damage to the cars or articles however caused . . . all cars being left in all respects entirely at their owners' risk. Owners are requested to show ticket when required."

Shortly after the plaintiff left the premises a man claiming to be his friend and to be acting with his consent appeared and, with the permission of the attendant, reached through the open windshield, unlocked the car and drove it away. Sir Wilfrid Greene, M.R., in determining "the nature of the relationship between the parties" stated that "the character of the ground is . . . not without importance." He concluded there had been no delivery of the car to the defendant, and that the transaction was not a bailment but rather a license. However, the court stated that assuming there was a bailment the limitation printed on the ticket was sufficient to relieve the defendant from all liability.

Another case decided during the past year also involved a parking lot of the first type mentioned above. The defendant operated a hotel and in connection therewith maintained a free parking lot. The plaintiff, a guest at the hotel, parked his car on the lot and locked it, but during the night a thief broke into the car and stole some goods the

13Id. at 482.
16Id. at 248.
plaintiff had left in it. In discussing the law determining the defendant's liability the court remarked, "it may be one of the many and various rules relating to contract or negligence or agency or bailment or what have you." They concluded the defendant was not liable for the loss but did not clearly state the grounds for their decision. The case consequently adds little to those already considered, although the court did suggest that if the defendant were considered a bailee the burden of proof would be on the plaintiff to show negligence, and that he did not do.

III.

The first case involving a parking lot of the second type referred to above was Galowitz v. Magnen in which the plaintiff parked his car in a lot operated by the defendant near a bathing beach. The lot was enclosed with an eight foot wooden fence and had one entrance and one exit with attendants on duty at all times. The plaintiff was charged a fee of fifty cents for parking his car and received a ticket upon the back of which there appeared in fine print:

"The person accepting this ticket assumes all risk of accident, and expressly agrees that the management shall not be liable, under any circumstances for any injury to person, loss, or damage." The plaintiff pocketed the ticket and when he later returned for the car it had been stolen. The court held as a matter of law the contract was one of bailment; they compared the case to one of checking parcels or the storage of an automobile in a garage, which the courts, almost without exception, have treated as a bailment for hire. The limitation of liability printed on the ticket the court dismissed as follows:

"Its presence on the ticket or stub is quite as consistent with a contract of bailment as with one for mere rental of parking space. It seems to me obvious that plaintiff had the right to believe, from the fact that defendant maintained an inclosed space for parking cars, with an entrance and exit and attendants, that he was paying the parking fee in consideration of care and watchfulness to prevent injury or loss. . . . It is equally clear that defendant had a like understanding of his obligation, because, as he testified, he maintained this fenced parking space and three attendants 'looking after, taking care of the cars as they came in and went out'."

However, the case was sent back for a new trial because of a defect in

---

18 Id. at 561, 1 N. Y. S. (2d) at 162.
19 208 App. Div. 6, 203 N. Y. Supp. 421 (2d Dep't 1924).
20 Id. at 7, 203 N. Y. Supp. at 422.
22 208 App. Div. 6, 8, 203 N. Y. Supp. 421, 423 (2d Dep't 1924).
the complaint is not alleging the negligence of the defendant. In discussing the matter of the presumptions and burden of proof the court stated that failure to deliver upon demand raised a presumption of negligence and constituted a prima facie case against a bailee, but that this presumption of negligence might be rebutted by the defendant showing the goods were stolen; the burden then would be upon the plaintiff to show that the loss occurred due to the negligence of the bailee. The point is important in these cases as in most instances there is no evidence available other than the delivery of the car and its loss; consequently the matter of the burden of proof may control the decision in many of the cases.

The defendant in *Hartford Fire Insurance Company v. Doll*\(^5\) rented a plot of ground near a ball park and conducted a parking lot on it. He charged a fee of twenty-five cents and issued tickets stating, "We will endeavor to protect your car from all trespassing while parked with us."\(^6\) The cars were parked under the direction of attendants who tagged them, the tags being taken up when the cars left the lot. One Hanson, who was insured with the Hartford Company, parked his car in the lot and it was stolen. The plaintiff company paid the loss and sued the defendant. The court held the defendant liable as bailee for hire, and imposed on him the burden of establishing the facts necessary to excuse liability or to show the exercise of due care. The delivery of the car by the plaintiff and the failure of the defendant to return it constituted a prima facie case which the defendant was unable to rebut. Here again the court might well have imposed liability on the theory of a special contract irrespective of whether or not there was a technical bailment of the car.

In *Marine Insurance Company v. Rehm*\(^5\) the Louisiana court again held the operator of a parking lot liable for the damage resulting from the theft of a car parked in his lot. The insured, Klein, parked his car in a parking lot operated by the defendant, paying a fee and receiving in return a ticket upon which was printed:

"While we at all times endeavor to protect the property of our patrons, we will not be responsible for loss or damage to automobiles, or accessories thereto, or anything therein contained, by fire, theft, or any other cause whatsoever, except damage to automobiles and/or accessories thereto attached while being handled on our premises by our employees under our orders."\(^7\)

Sometime after Klein parked his car a thief drove it away; the car was later found in a damaged condition. The plaintiff insurance company paid the loss and sued the defendant for reimbursement. The

---

\(^5\) La. App. 226 (1926).
\(^6\) *Id. at 227.*
\(^7\) *177 So. 79 (La. App. 1937).*
\(^8\) *Id. at 80.*
court reviewed the common law cases and concluded that the rule there makes the transaction a bailment. They then held the defendant responsible as a compensated depositary under the civil law, the evidence indicating negligence on his part in failing to provide sufficient illumination and employees to protect the cars. In speaking of the limitation of liability printed on the ticket the court said:

“In our opinion the check given by the defendant in this case to Klein upon the receipt of his automobile was nothing more than a means of identifying his property or a mere receipt and was not a special contract.”

Such a view is in accord with a majority of the courts and seems sound.

In Beetson v. Hollywood Athletic Club the plaintiff, a member of the defendant organization, drove his car into a parking place provided by the club and turned the car over to the attendant in charge. At the time the plaintiff delivered his car to the attendant he signed a slip as required and left the keys in his car. For this parking service the defendant charged a fee of fifteen cents. The usual custom was for the attendant to remove the keys and leave them in the defendant’s office if he left the parking place. On the night in question the attendant left the parking place without removing the keys to the plaintiff’s car and it was stolen. The car was later recovered in a damaged condition and the plaintiff sued to recover the amount of the damages. The court here, as in the previous cases, considered the relation as one of bailment for hire, thus imposing on the defendant the duty of exercising reasonable care to preserve the plaintiff’s car from loss or damage. In considering the defendant’s negligence the court argued:

“... the disappearance of the plaintiff’s car could not have occurred had the defendant’s employees properly performed their duty. Indeed, the inference of negligence is well-nigh irresistible from the fact that, upon the occasion in question, the defendant’s attendant left its parking place without taking the slightest precaution to protect the plaintiff’s car against theft.”

The plaintiff was allowed to recover, the court making certain reductions in the amount of damages awarded by the trial court.

Seven years later the California court again had the parking lot problem before it. The plaintiff rented a car to one Lejeune who, shortly before midnight, parked it in a lot operated by the defendant, and when he returned some time later it was gone. The car was subsequently discovered in a much damaged condition and the plaintiff sought to recover the amount expended to recondition it. Lejeune paid a fee

---

22Ibid.
24Id. at 721, 293 Pac. at 823, 824.
of fifteen cents for parking and in return received a ticket with an identification number and the words "We Close 12 P. M. Not Responsible for Cars After Closing Time" printed on it. There were also signs posted on the lot indicating the closing time, but neither they nor the printed matter on the ticket were in any way called to the attention of Lejeune. The court held the defendant was not responsible for the damage to the car. They admitted the transaction was a bailment and that the burden of proof was on the defendant to show the theft was without his fault in order to relieve himself from liability for the loss. As the court put it:

"... if he relies upon the proposition that the property was lost by theft or fire without negligence on his part, the burden is on him to prove these facts, including his lack of negligence."32

But the court considered the printed stipulations on the ticket a part of the contract so as to limit the defendant's liability; they went on analogy to the railroad cases involving bills of lading and held the plaintiff bound to know what was printed on the receipt he received. Since the evidence clearly showed that the car was still on the lot when the employee left at midnight, the defendant could not be held liable. Thus, although the transaction was held to be a bailment, the operator of the parking lot escaped liability by means of the limitation printed on the ticket.

The defendant's wife, in *Keenan Hotel Company v. Funk*,33 parked his car in a lot operated by the defendant from which it was stolen. The attendant took charge of the car and requested the keys be left in it so he could move it about as needed to accommodate other cars. A fee of twenty-five cents was charged for parking and a check issued to each driver stating that the defendant was not responsible in case of fire, theft or accident. The court conceded the case to be one of bailment for hire and held the defendant liable for the loss of the plaintiff's car, not allowing defendant to relieve himself from liability for his own negligence by the limitation printed on the check. The court compared the case to that of a garagekeeper so far as the duties of the defendant were concerned. In considering the matter of burden of proof, the court held the plaintiff to have made out a prima facie case of negligence against the defendant by showing the delivery of the car, and the failure to redeliver upon demand, and then continued:

"... And such prima facie case is not overcome by a showing on the part of the bailee that the goods have been burned, or otherwise destroyed or stolen.

31 Id. at 357.
32 Id. at 356.
33 93 Ind. App. 677, 177 N. E. 364 (1931).
Before such prima facie case can be said to be overcome, the bailee must further produce evidence tending to prove, that the loss, damage, or theft was occasioned without his fault."

Although the court thus recognized the ultimate burden of proof to be upon the plaintiff, it imposed on the defendant the burden of showing that the loss was not caused by his fault in order to escape liability. As before suggested this rule would in many instances determine the case.

In a similar case decided in the same year the Michigan Supreme Court held the defendant liable for the loss, by theft, of a parked car. The plaintiff was an insurance company which had insured a car belonging to one Block against loss by fire or theft. Block parked the car in a lot operated by the defendant and it was stolen. The plaintiff paid the loss and took a bill of sale to the car and an agreement subrogating it to the claim against the defendant. The lot in question was fully enclosed except for the entrances and exits, and tickets were issued which had to be surrendered when the cars were removed. The lot was operated both during the day and at night and Block, who regularly left his car there, delivered the car in the morning and called for it early in the evening, no charge, other than the usual twenty-five cent fee, being made for the overtime parking. Most of the cars were left unlocked so the attendants could move them about. The court assumed the transaction to be a bailment and decided the case on the question of burden of proof. The majority agreed with the preceding case, putting the burden on the defendant to show not only that the car was stolen but that it was stolen without fault on his part in order to escape liability. They were supported in this view by a statute which provided that whenever a car was damaged while in the possession of a garage, or other establishment for hire, proof of the damage should be prima facie evidence of the negligence of the operator of the establishment. Since the only evidence outside of the delivery of the car and its disappearance indicated that the defendant had been negligent in his conduct, the court necessarily found for the plaintiff. Two of the judges dissented as to the burden of proof and the effect of the statute, de-

---

34Id. at 681, 682, 177 N. E. at 365, 366. The court is quoting from Employers' Fire Ins. Co. v. Consolidated Garage & Sales Co., 85 Ind. App. 674, 676, 155 N. E. 533, 536 (1927).


37The evidence showed that the only persons in charge of the lot in the evening were a woman and a little girl, that the exits were left unguarded, that the lot was not lighted, and that it was located in a neighborhood frequented by persons of questionable character.
claring the burden to be on the plaintiff to show that the loss was due to the negligence of the defendant:

"When plaintiff proved the car was delivered to defendant, and defendant failed to deliver the same on demand, plaintiff established a prima facie case, and, when defendant showed the car was stolen, he showed a prima facie excuse for failure to deliver the car. The burden was on the plaintiff to show the car was stolen through the negligence of the defendant. This it did not do." 88

Such a view would, of course, result in a judgment for the defendant in cases where there is no evidence other than the delivery of the car and its subsequent loss by theft.

The defendant in Baione v. Heavey 89 operated a parking lot in the city of Philadelphia where the plaintiff parked his car. The lot was not enclosed but was in charge of several attendants who took charge of the cars at the entrance and parked them, retaining the keys so they might move the cars about. A charge of thirty-five cents was made for parking and a check issued to each person which stated:

"Charges are for the use of parking space only and management assumes no liability of any kind." 40

When the plaintiff returned for his car it had been stolen, but was later located. The plaintiff sought to recover for the damage to the car, which was allowed. The court summarily dismissed the defendant's contention that the transaction amounted to a lease and held it to be a bailment, thus imposing upon him a duty of due care. As for the limitation of liability printed on the check the court said:

"The terms of the defendant's service stated on the check or ticket, in view of the other evidence on the subject, do not represent all the terms of the contract of, or relation between, the parties, but, if they did, defendant could not thereby obtain immunity from the consequences of the negligence of himself or his servants." 41

And as regards the proof of the defendant's negligence the court considered it sufficiently shown by the delivery of the car and the failure of the defendant to redeliver it or to explain its loss, thus in effect imposing on the defendant the burden of showing that the loss was without his fault.

In Doherty v. Ernst 42 the defendant operated a combined filling station and parking lot in which the plaintiff parked his car while he and

---

91Id. at 532, 158 Atl. at 183.
his wife attended the theatre. The lot was fenced on the sides not fronting on the street and on the street sides was curbed at all places except the entrance and exit. A fee of twenty-five cents was charged for parking but no checking system was used. The defendant usually kept the keys to the cars parked or had them left in the cars so he could move them about. On the evening in question the plaintiff left his keys in the car with the knowledge of the defendant. Shortly after the plaintiff parked his car a stranger drove it away, driving over the curbing; the car was later found in a damaged condition. The court found the defendant had taken the car into his "care and custody" for a compensation so as to make him a bailee for hire, and continued:

"The defendant, having become a bailee for hire, was bound in the circumstances disclosed to exercise due care in order to return the automobile to the owner in as good a condition as when received."43

Since the evidence was sufficient44 to support a finding of negligence on the part of the defendant, the plaintiff was allowed to recover.

In Leonard Brothers v. Standifer45 the defendant operated a free parking lot in connection with his store. The lot was open to the public, whether patrons of the store or not, and although no charge was made for parking, the lot was in charge of an attendant who issued checks to all persons parking cars within the lot. The plaintiff parked his car in the lot and it was stolen. The court treated the transaction as a gratuitous bailment and imposed on the plaintiff the burden of showing gross negligence in order to recover.45 They recognized that delivery by the bailor and failure of the bailee to redeliver ordinarily constitutes a prima facie case, but where the reasons for nondelivery are consistent with the legal obligation of the bailee, they imposed the burden on the bailor to show negligence on the part of the bailee. In the particular case the loss of the car by theft might be consistent with the defendant's duty to exercise only slight care, consequently the court imposed the burden on the plaintiff to show gross negligence by the defendant, and that he was unable to do. Thus the plaintiff did not recover even though the court treated the transaction as a bailment.

In Syndicate Parking, Incorporated v. General Exchange Insurance

4For a statement of the orthodox classification of bailments and the corresponding obligations of the bailor and bailee see, Brown, Personal Property (1936) § 80; Goddard, Bailments and Carriers (2d ed. 1928) §§ 12, 15, 16; Dobie, Bailments and Carriers (1914) §§ 4, 7, 21-24, 29; Jones, Law of Bailments (1836) 35; Story, Law of Bailments (9th ed. 1878) §§ 3, 23; Schouler, Law of Bailments (1880) 11-17; Coggs v. Bernard, 2 Ld. Raym. 909 (Q. B. 1703).
Corporation, Sheehan parked his car in a lot operated by the defendant, paying a fee of fifteen cents and receiving a receipt which stated that the defendant was not liable for loss of the car by theft unless a fee of seventy-five cents was paid and the car placed in a space where it could be left locked; cars parked in the fifteen cent spaces were required to be left unlocked so the defendant could move them about. Sheehan placed his car in a seventy-five cent space and locked it but apparently did not pay the additional fee. The car was stolen and the plaintiff, which had insured the car, paid the loss and sued the defendant. The court held the plaintiff was not bound by the terms printed on the receipt since the statement had not been called to the attention of Sheehan when he parked his car. They treated the case as one of bailment, and held that the delivery of the car and its subsequent loss constituted a prima facie case raising a presumption of negligence on the part of the defendant, but the proof of the theft of the car rebutted the negligence and the burden then was on the plaintiff to show the theft was due to the negligence of the defendant. The trial court found the defendant negligent but the majority of the appellate court held there was not sufficient evidence to indicate negligence on the part of the defendant, thus recovery was not allowed.

In five very recent cases the courts of Georgia and Pennsylvania had before them typical city parking lot situations of the second type, and in each case treated it as a bailment. In the first Georgia case, a car owned by the Hertz Driv-Ur-Self Sales Corporation was rented to Carroll who parked it in the defendant's lot, paying a fee and receiving a check in return. When he called for the car it was gone, having been delivered to another person. The plaintiff insurance company, which had insured the car, paid the amount of the loss and sued the defendant. The court treated the relation existing between Carroll and the defendant as one of bailment, thus imposing on the defendant the duty to use "ordinary diligence in caring for the thing stored," and making him liable upon his failure to redeliver the car unless he exercised such diligence. Because Carroll himself was a bailee of the car the defendant was liable to him, for interference with his right of possession, and also to the plaintiff's assignor for the injury to its right of property. Consequently the plaintiff had a good cause of action and a demurrer to its petition was properly overruled and verdict directed for it.

The other Georgia case allowed the plaintiff to recover from the operator of a parking lot on the theory of negligence without any dis-

46 Ohio L. Abs. 596 (Ohio App., 8th Dist., 1934).
48 Id. at 321, 185 S. E. at 606.
discussion of the problems involved. The case is unimportant except as another decision imposing obligations on the operator of a parking lot consistent with the theory of a bailment.

The same defendant was involved in all three of the Pennsylvania cases. In two of the cases the plaintiff drove his car into the lot, paid a fee of ten cents for parking and in return received a check stating, "Not responsible for fire or theft. All valuables must be checked." In both cases the car was stolen, and although later recovered was damaged and part of the equipment missing. The court treated the transactions as bailments for the mutual benefit of the parties, thus imposing on the defendant the duty to exercise care. In holding the defendant liable in spite of the limitation printed on the check, the court said:

"Whatever construction may be placed on the receipt, however, the appellant is confronted with the well-recognized rule that the right of a bailee to limit his liability by special contract does not go to the extent of relieving him against his own negligence." And concerning the burden of proof and the presumption of negligence the court held:

"If a bailee fails to return bailed property or give a satisfactory explanation for its disappearance, he has the burden of proving that the loss was not due to his negligence. This is upon the theory that, when a bailee has exclusive possession of the goods, the acts attending loss or injury must be peculiarly within his own knowledge, and therefore he is required to excuse or justify a failure to return the goods in a proper condition." Or as summarized by the court in the second case:

"... if the bailor proves the bailment and the failure of the bailee to return the property, he has made out a prima facie case, and it is then the duty of the bailee to go forward with proof to show that he used proper care over the bailed property."

Under this view the consequence of a parking lot operator's inability to explain the loss of a car would be recovery by the owner.

In the third case the plaintiff's son drove her car into the lot and delivered it, together with the keys, to the attendant. A fee of thirty-five cents was paid for parking and a check given the son which stated, "Not

---

61"Id. at 227, 188 Atl. at 625.
62"Id. at 228, 188 Atl. at 625.
63"Id. at 228, 188 Atl. at 625.
responsible for fire or theft."56 The car was stolen from the lot and
the court again held the defendant liable for the loss of the car, stating
that the terms printed on the check did not limit the defendant's liability
for its own negligence. Likewise they imposed on the defendant the
burden of proving it had exercised due care in order to relieve itself
from liability for the loss. As noted above the matter of the burden
of proof is particularly important in the parking lot cases. The rule
as enunciated in these cases takes note of the realities of the situation
and appears to furnish a satisfactory solution without imposing an undue
burden on either party.

The Ontario Court of Appeal, in Spooner v. Starkman,57 held the
operator of a parking lot liable for the theft of a car parked in his
lot. The plaintiff drove to Toronto and parked in the defendant's
lot, leaving his keys in the car. He paid a fee of fifteen cents and
received a ticket about two inches square upon which was printed the
name and location of the parking lot, the fee charged for parking, and
in small print, "Not responsible for Car or Contents."58 There were
also two small signs posted which stated that the defendant was not
responsible for cars parked on the lot, but the evidence indicated that
the plaintiff did not read either the signs or the ticket, nor were the
statements called to his attention. The court assumed the relation was
one of bailor and bailee and held that the defendant could not limit his
responsibility by the provision printed on the ticket, or by the signs
posted on the lot, unless it were clearly shown that the limitations were
called to the attention of the plaintiff. In referring to the limitation
printed on the ticket the court said:

"... the one outstanding fact and circumstance in my opinion is that the
ticket which was given to the plaintiff, instead of being designed to inform
him of the defendant's attempted limitation of his responsibility, was
designed to conceal it. ... I think if the defendant desired to limit his respon-
sibility as a bailee for hire, he must show that the attention of the plaintiff was
called to such limitation ..."59

The case is interesting in view of the remarks of the English court60
and the decision of the California court61 upholding such a limitation. However, the view here expressed seems sound and more likely to
produce a just result in most cases.

56Id. at 69, 194 Atl. at 773.
57[1937] 2 D. L. R. 582. 58Id. at 583.
Co., Cal. 1937).
IV.

One more case remains to be considered. In that case the plaintiff's wife drove his car to town and parked it in a lot operated by the defendant from where it was stolen. The car was later found in a somewhat damaged condition and the plaintiff sought recovery for the amount expended for repairs. The defendant operated the parking lot in connection with a filling station and a store, and the employees in charge of those businesses also looked after the parking lot. The lot was not enclosed and could be entered at other places than the regular entrance. No system of checks or tickets was used and the employees were instructed to have all persons parking cars lock them. However, the plaintiff's wife testified that she was told it was not necessary to lock the car so she did not do so. Signs reading "We are not responsible for loss or damage" were posted and a charge of twenty-five cents was made for the privilege of parking. The case is interesting because it does not clearly fall within either of the two types of situations discussed above. The trial judge held as a matter of law that the transaction was a bailment, thus imposing on the defendant the duty to exercise reasonable care; but the appellate court decided the relation between the operator of a parking lot and the owner of a parked car depended on the circumstances of each case, and the question therefore should have been left to the jury to determine whether or not a bailment existed.

"Whether a person simply hires a place to put his car or whether he has turned its possession over to the care and custody of another depends on the place, the conditions, and the nature of the transaction." Since the evidence as to the extent of the defendant's control or possession of the car was conflicting, the case was sent back for a new trial.

V.

Of the seven cases involving parking lots of the first type, only two held the defendant liable for the loss of the car, and those cases properly depend on the theory of a special contract making the parking lot operator an insurer. Although the courts in those cases talked in terms of a bailment, the expressions on that point are dicta since the decisions do not depend on a bailee's liability for lack of due care. Four of the other five cases definitely decided there was no bailment and, therefore, no duty to exercise due care as regards the parked cars. In all four cases the courts failed to find a sufficient delivery of possession to con-

---

"Osborn v. Cline, 263 N. Y. 434, 189 N. E. 483 (1934).
"Id. at 436, 189 N. E. at 483.
"Id. at 437, 189 N. E. at 484.
stitute a bailment; there was no taking of the physical control or custody of the car by the operator of the parking lot, no exercise of dominion over the car other than to designate the area in which to park. At most such a transaction would seem to be nothing more than a lease of parking space, and it would appear to be more accurate to speak of it as a license, a mere privilege to park being all that is granted. The failure of any of the cases of that type to impose liability on the operator of the parking lot for the loss of or damage to the cars, except as a result of a special contract, definitely indicates the transaction is not a bailment.

All of the cases dealing with parking lots of the second type imposed on the defendant the duty of exercising some degree of care towards the parked cars, and all but one held him liable for loss of, or damage to, the cars due to his negligence. All of those cases considered the relation between the operator of the parking lot and the owner of the automobile to be that of bailee and bailor, and those courts which specifically discussed the point found there was a sufficient delivery of possession to the operator of the parking lot, a taking of physical control and exercise of dominion by him over the car sufficient to constitute the transaction a bailment. The difference between the method of conducting the business in cases of the first type and those of the second type seems sufficient to justify a distinction in treatment, and the consistency with which the courts have imposed liability for the loss of or damage to parked cars in cases of the second type indicates quite clearly that the transaction is a bailment.

Although categorical statements are always hazardous, it seems fairly safe to conclude that no court would now hold a case of the first type to be a bailment; the essential element of possession is lacking and the obligations imposed on the operators of such lots are not consistent with the concept of a bailment. The most accurate description of the transaction in such a case is to call it a license, a privilege to park. There may, of course, be cases where the business is conducted in such a manner that the elements of a lease are present, but in most instances the term license seems more accurately to indicate the relation, a mere privilege to park being all that is granted. And it appears even more certain that no court would now hold a case of the second type to be other than a bailment; all the essential elements are present and the obligations which the courts have imposed on the operators of such lots are incident to a bailment. Cases of that type are so closely analogous to the cases involving garages that the same rules should be

*Notes (1934) 18 Minn. L. Rev. 352, (1937) 53 L. Q. Rev. 301 taking the view that such a transaction is, properly speaking, a mere license.
applied, and in the garage cases the courts, in nearly all instances, have held the transaction to be a bailment and imposed liability on the garagekeeper for failure to exercise due care. Consequently similar treatment in the parking lot cases of the second type seems almost inevitable. One may well conclude, as did the New York court, 66 that the relation between the operator of a parking lot and the owner of a parked car is a bailment, lease or license depending upon the circumstances of each case, the manner in which the business is conducted. 67

But classifying the transaction as a bailment, a lease, or a license, does not automatically determine all the rights and liabilities of the parties. There still remain the matters of special contract, limitation of liability and burden of proof to consider. And as the cases have indicated the operator of a parking lot may, by so agreeing, make himself liable to the owner of a parked car for its loss or injury even though such a responsibility would not be imposed upon him from the nature of the transaction. Likewise the operator may attempt by a limitation of liability, posted on the lot or printed on the ticket or check given the owner of the car, to escape responsibility for the car while parked. But, with two exceptions, the cases have not upheld such limitations where the loss or injury was due to the negligence of the operator of the lot and where the stipulations were not specifically called to the attention of the plaintiff. And any other holding would seem impracticable and conducive to fraud. 68

As regards the burden of proof, in all of the cases where the point was involved the courts applied the usual rule in bailment cases and held the plaintiff established a prima facie case by showing the delivery of the car to the parking lot operator and its subsequent loss or injury; and most of the cases went further putting on the defendant the burden of showing not only that the car was stolen, but also that the theft occurred without fault on his part in order to relieve himself from liability for the loss or injury. 69

---


68 The cases are divided as to the burden of proof in instances where the subject of the bailment is stolen or destroyed. The majority of the parking lot cases seem to put
Thus it appears that the courts, consciously or unconsciously, are distinguishing between the two types of parking lots, holding the first to be a license and the second a bailment; and they are adapting the principles of law relating to those recognized relationships to fit the needs of the new situations to which they are applied.

the burden on the bailee, but see, (1934) 14 B. U. L. Rev. 368 stating the rule to be otherwise. For a collection of cases on this point generally see, (1923) 26 A. L. R. 223. For cases involving garagekeepers see, (1921) 15 A. L. R. 681, (1926) 42 A. L. R. 135, (1930) 65 A. L. R. 431; Blashfield, Cyclopedia of Automobile Law and Practice (1935) § 5043; Berry, Law of Automobiles (4th ed. 1924) § 1412.
THE
GEORGETOWN LAW JOURNAL
Volume 27 Number 2
DECEMBER 1938

THE BOARD OF EDITORS

WILLIAM P. CONNALLY, JR., of Texas . . . . . . . Editor in Chief
J. F. McCARTNEY, of Illinois . . . . . . . . . . . . Associate Editor
GERALD P. O'GRADY, of Vermont . . . . . . . . . . Associate Editor
JAMES G. BOSS, of Maryland . . . . . . . . . . . . Supreme Court Editor
HENRY W. SWEENEY, of New York . . . . . . . . . Federal Legislation Editor
DAVID HOROWITZ, of Rhode Island . . . . . . . . Note Editor
WILLIAM J. SHAUGHNESSY, of District of Columbia . Recent Decision Editor
FRANKLIN N. PARKS, of District of Columbia . . Recent Decision Editor
SIDNEY Z. LEVY, of Pennsylvania . . . . . . . . . Book Review Editor
AUGUSTUS P. CRENSHAW, III, of District of Columbia . . . Secretary

STAFF

WILLIAM O. CRAMER
Missouri

RALPH W. DORIUS
Utah

MITCHELL S. DVORET
Illinois

CARY M. EUWER
Maryland

C. ALBERT FEISSNER
Pennsylvania

JAMES F. FOLEY
Rhode Island

LEONARD A. GOLDBERG
Alabama

SIDNEY M. GOLDFEINSTEIN
Connecticut

GEORGE M. GOOD
Michigan

ROBERT F. GRAHAM
District of Columbia

CHESTER HAMMOND
New York

C. JONATHAN HAUCK, JR.
New Jersey

JOHN W. HUYSSOON
New Jersey

JOHN M. MCKENNA
District of Columbia

MAX MALIN
New York

HARRY B. MERICAN
New York

WALTER D. MURPHY
Maryland

ARTHUR J. NADEAU, JR.
Maine

HENRY C. RUBIN
Pennsylvania

FREDERICK R. TOURKOW
Ohio

PHILIP TREIBITZ
New York

HAROLD GILL REUSCHELEIN, Faculty Advisor

181
THE SUPREME COURT OF THE UNITED STATES*

ALTHOUGH the Supreme Court has greatly reduced its docket in the disposal of cases by orders of the Court denying certiorari, rehearings and appeals, only eighteen opinions have been handed down during the current term, and the cases invoking the greatest public interest remain to be decided. The cases decided have involved mainly general questions of law as distinguished from cases involving economic and political or governmental theories which in recent years have occasioned the greater number of dissents. The fact that six of these eighteen cases were decided by a divided court would seem to indicate that the current term may witness a greater number of dissents than any of recent years.

PATENTS—RESTRICTIVE LICENSE

The Court held, in General Talking Pictures Corp. v. Western Electric Co.,¹ that a non-exclusive license limited to the manufacture and sale of a patented device for private use was valid and that a breach of the license was an infringement of the patent. In so holding, the Court refused to change its earlier decision in the same case² that where the patented device was knowingly manufactured and purchased for uses outside the scope of the license, the sale was not made under the patent or under the authority of the owner, the vendee was not a "purchaser in the ordinary channels of trade", and that both the vendor licensee and the vendee were guilty of infringement. Mr. Justice Black, joined by Mr. Justice Reed, dissented on the ground that the majority opinion was a departure from the established rule that a patented article, after being sold and passed to the hands of a purchaser, is no longer within the limits of the monopoly, and that the holder of the patent should not be allowed to restrict the use of the article after such sale. This argument was in accordance with Mr. Justice Black's dissent from the Court's holding in the same case at the last term in which he said the decision "will inevitably result in a sweeping expansion of the statutory boundaries constitutionally fixed by Congress to limit the scope and duration of patent monopolies."³ The soundness of this argument was emphasized by the fact that the Government filed a brief "to protect the public interest" on the ground that an affirmance of the first decision would hamper the administration of the anti-trust laws. When the Court decided to rehear the case it was felt by many that the majority

---

¹Written November 28, 1938.
²59 Sup. Ct. 116 (November 21, 1938).
³General Talking Pictures Corp. v. Western Electric Company, 304 U. S. 175 (1938).
⁴Id. at 183.
would adopt Mr. Justice Black’s view but the position taken by the Court in its last decision indicates that a change in the patent laws will be necessary to prevent the use of this type of license agreement.

FEDERAL PROCEDURE—DISMISSAL OF ACTION BY DISTRICT COURT

In The Polk Company v. Glover, involving the constitutionality of a Florida statute regulating the canning of citrus products, the Court, in a per curiam opinion, reversed a decree of the district court dismissing the plaintiff’s bill, and remanded the cause for further proceedings. The decision was based on the ground that the question of the constitutionality of the state statute, challenged as a denial of due process of law under the Fourteenth Amendment, was dependent on the underlying facts and could not be determined until the Court had before it the findings of fact by the lower court based on adequate evidence. Mr. Justice Black dissented on the ground, among others, that the majority opinion would require that all bills of this nature must be heard even though they do not state a cause of action and is therefore contrary to the rule of Missouri Pacific R. R. v. Norwood, that where the bill does not contain sufficient allegations to show the constitutionality of the statute, the district court’s decree of dismissal should be affirmed. However, the statement in the majority opinion that “the facts alleged in the bill were sufficient to entitle the plaintiffs to an opportunity to prove their case, if they could”, indicates a holding that the plaintiff’s bill does state a cause of action, in which event there would appear to be no conflict with the Norwood case. In this view, the Court, in its refusal to decide constitutional questions unless it has before it findings on the essential facts upon which the question of the constitutionality of statutes is so often dependent, appears merely to follow the rule of Borden’s Farm Products Co. v. Baldwin, without impairing the holding in the Norwood case. The application of the principle of the Norwood case in conjunction with that of the Borden case appears necessary for the disposal of cases of this nature and, if, as Mr. Justice Black suggests, the Court first determines whether the bill states a cause of action before remanding it for further proceedings, there is no reason why the two principles should conflict.

STATE TAXATION—FOURTEENTH AMENDMENT

In Guaranty Trust Company of New York v. Virginia the Court upheld a Virginia tax on income of a resident received from a trust administered in New York although the latter state had collected a tax on

---

1938] Supreme Court of the United States 183

would adopt Mr. Justice Black’s view but the position taken by the Court in its last decision indicates that a change in the patent laws will be necessary to prevent the use of this type of license agreement.

FEDERAL PROCEDURE—DISMISSAL OF ACTION BY DISTRICT COURT

In The Polk Company v. Glover, involving the constitutionality of a Florida statute regulating the canning of citrus products, the Court, in a per curiam opinion, reversed a decree of the district court dismissing the plaintiff’s bill, and remanded the cause for further proceedings. The decision was based on the ground that the question of the constitutionality of the state statute, challenged as a denial of due process of law under the Fourteenth Amendment, was dependent on the underlying facts and could not be determined until the Court had before it the findings of fact by the lower court based on adequate evidence. Mr. Justice Black dissented on the ground, among others, that the majority opinion would require that all bills of this nature must be heard even though they do not state a cause of action and is therefore contrary to the rule of Missouri Pacific R. R. v. Norwood, that where the bill does not contain sufficient allegations to show the constitutionality of the statute, the district court’s decree of dismissal should be affirmed. However, the statement in the majority opinion that “the facts alleged in the bill were sufficient to entitle the plaintiffs to an opportunity to prove their case, if they could”, indicates a holding that the plaintiff’s bill does state a cause of action, in which event there would appear to be no conflict with the Norwood case. In this view, the Court, in its refusal to decide constitutional questions unless it has before it findings on the essential facts upon which the question of the constitutionality of statutes is so often dependent, appears merely to follow the rule of Borden’s Farm Products Co. v. Baldwin, without impairing the holding in the Norwood case. The application of the principle of the Norwood case in conjunction with that of the Borden case appears necessary for the disposal of cases of this nature and, if, as Mr. Justice Black suggests, the Court first determines whether the bill states a cause of action before remanding it for further proceedings, there is no reason why the two principles should conflict.

STATE TAXATION—FOURTEENTH AMENDMENT

In Guaranty Trust Company of New York v. Virginia the Court upheld a Virginia tax on income of a resident received from a trust administered in New York although the latter state had collected a tax on

---

1938] Supreme Court of the United States 183

would adopt Mr. Justice Black’s view but the position taken by the Court in its last decision indicates that a change in the patent laws will be necessary to prevent the use of this type of license agreement.

FEDERAL PROCEDURE—DISMISSAL OF ACTION BY DISTRICT COURT

In The Polk Company v. Glover, involving the constitutionality of a Florida statute regulating the canning of citrus products, the Court, in a per curiam opinion, reversed a decree of the district court dismissing the plaintiff’s bill, and remanded the cause for further proceedings. The decision was based on the ground that the question of the constitutionality of the state statute, challenged as a denial of due process of law under the Fourteenth Amendment, was dependent on the underlying facts and could not be determined until the Court had before it the findings of fact by the lower court based on adequate evidence. Mr. Justice Black dissented on the ground, among others, that the majority opinion would require that all bills of this nature must be heard even though they do not state a cause of action and is therefore contrary to the rule of Missouri Pacific R. R. v. Norwood, that where the bill does not contain sufficient allegations to show the constitutionality of the statute, the district court’s decree of dismissal should be affirmed. However, the statement in the majority opinion that “the facts alleged in the bill were sufficient to entitle the plaintiffs to an opportunity to prove their case, if they could”, indicates a holding that the plaintiff’s bill does state a cause of action, in which event there would appear to be no conflict with the Norwood case. In this view, the Court, in its refusal to decide constitutional questions unless it has before it findings on the essential facts upon which the question of the constitutionality of statutes is so often dependent, appears merely to follow the rule of Borden’s Farm Products Co. v. Baldwin, without impairing the holding in the Norwood case. The application of the principle of the Norwood case in conjunction with that of the Borden case appears necessary for the disposal of cases of this nature and, if, as Mr. Justice Black suggests, the Court first determines whether the bill states a cause of action before remanding it for further proceedings, there is no reason why the two principles should conflict.

STATE TAXATION—FOURTEENTH AMENDMENT

In Guaranty Trust Company of New York v. Virginia the Court upheld a Virginia tax on income of a resident received from a trust administered in New York although the latter state had collected a tax on

---

1938] Supreme Court of the United States 183

would adopt Mr. Justice Black’s view but the position taken by the Court in its last decision indicates that a change in the patent laws will be necessary to prevent the use of this type of license agreement.

FEDERAL PROCEDURE—DISMISSAL OF ACTION BY DISTRICT COURT

In The Polk Company v. Glover, involving the constitutionality of a Florida statute regulating the canning of citrus products, the Court, in a per curiam opinion, reversed a decree of the district court dismissing the plaintiff’s bill, and remanded the cause for further proceedings. The decision was based on the ground that the question of the constitutionality of the state statute, challenged as a denial of due process of law under the Fourteenth Amendment, was dependent on the underlying facts and could not be determined until the Court had before it the findings of fact by the lower court based on adequate evidence. Mr. Justice Black dissented on the ground, among others, that the majority opinion would require that all bills of this nature must be heard even though they do not state a cause of action and is therefore contrary to the rule of Missouri Pacific R. R. v. Norwood, that where the bill does not contain sufficient allegations to show the constitutionality of the statute, the district court’s decree of dismissal should be affirmed. However, the statement in the majority opinion that “the facts alleged in the bill were sufficient to entitle the plaintiffs to an opportunity to prove their case, if they could”, indicates a holding that the plaintiff’s bill does state a cause of action, in which event there would appear to be no conflict with the Norwood case. In this view, the Court, in its refusal to decide constitutional questions unless it has before it findings on the essential facts upon which the question of the constitutionality of statutes is so often dependent, appears merely to follow the rule of Borden’s Farm Products Co. v. Baldwin, without impairing the holding in the Norwood case. The application of the principle of the Norwood case in conjunction with that of the Borden case appears necessary for the disposal of cases of this nature and, if, as Mr. Justice Black suggests, the Court first determines whether the bill states a cause of action before remanding it for further proceedings, there is no reason why the two principles should conflict.

STATE TAXATION—FOURTEENTH AMENDMENT

In Guaranty Trust Company of New York v. Virginia the Court upheld a Virginia tax on income of a resident received from a trust administered in New York although the latter state had collected a tax on
the identical income in the hands of the trustee. In answer to the contention that the Virginia tax was in contravention of the due process clause of the Fourteenth Amendment, the Court held that the decisions in Lawrence v. State Tax Commission\(^8\) and New York ex rel. Cohn v. Graves\(^9\) were controlling, although in neither of these cases were taxes actually collected by two states as in the instant case.

Though the Court had held that taxation of income by more than one state was not for that reason invalid\(^10\) later cases involving other forms of taxation indicated that the results of multiple taxation were at least considered undesirable.\(^11\) Whether this view would be extended to the field of income taxation was for some time in doubt\(^12\) despite the implications of the decisions in the Lawrence case and Maguire v. Trefry.\(^13\) In 1935 it appeared from the decision in Senior v. Braden\(^14\) that this doubt had been resolved in favor of such extension. However, the force of that decision was sharply restricted by the opinion in the Cohn case and the trend appears to be in the opposite direction. This development is now strengthened by the opinion in the Guaranty Trust Company case, in the holding that the receipt of the income in the state by a resident thereof gives the state a right to tax which cannot be destroyed by the previous taxation of the same funds by another state. However, since income from real estate was not involved in this case, the question whether that type of income may be taxed by more than one state, as advocated by Mr. Justice Stone in his dissent in the Braden case, must remain for later decisions.

CERTIORARI—GROUNDS FOR ISSUING

It is interesting to note that in The Schriber-Schroth Company v. The Cleveland Trust Company,\(^15\) involving the validity of a patent used in the automobile industry, the Court states that, after having denied certiorari because there was no conflict of decision,\(^16\) certiorari was later granted on the ground that litigation in other circuits with a resulting conflict of decisions was improbable because of the concentration of that industry in one circuit. Certiorari has also been granted on this ground in patent cases involving the movie industry in view of the possibility of confining such litigation to one circuit.\(^17\) Although it

\(^{286}\) U. S. 276 (1932).

\(^{290}\) Shaffer v. Carter, 252 U. S. 37 (1920).

\(^{300}\) U. S. 308 (1937).

\(^{326}\) Safe Deposit and Trust Company v. Virginia, 280 U. S. 83 (1929); First National Bank v. Maine, 284 U. S. 312 (1932). But see dissenting opinion of Stone, J., id. at 331.

\(^{293}\) Harding, State Jurisdiction to Tax Dividends and Stock Profits to Natural Persons (1937) 25 Calif. L. Rev. 139.

\(^{298}\) 253 U. S. 12 (1920).

\(^{305}\) 305 U. S. 639 (1938).

\(^{309}\) Paramount Publix Corp. v. American Tri-Ergon Corp., 294 U. S. 464 (1935); Altoona
is probable that the same course would be followed in cases involving
any field of law in order to prevent erroneous holdings of lower courts
from remaining unchallenged merely by the restriction of litigation to
one circuit, the principle seems to be limited to questions of patent law
since it is difficult to conceive of any cases not involving patents used
in a strictly localized industry in which a comparable situation could
arise.

THE SUPREME COURT AND CIVIL LIBERTIES, OCTOBER TERM, 1937

Though the Supreme Court decided few cases during its last term
which involve questions regarding civil liberties, the decisions are never-
theless of interest and importance.

Licensing of Distribution of Circulars

Outstanding is the case of Lovell v. City of Griffin,18 where the Su-
preme Court struck down a municipal ordinance which denied the right
to distribute circulars, pamphlets, and other printed material, without
prior approval by a municipal official. The decision is undoubtedly one
of great practical importance to the cause of freedom of expression by
minorities. In view of the huge expense in publishing a modern news-
paper, circulars and pamphlets play an important role in the efforts
of impecunious minorities to bring their messages to the people. Cir-
culars and pamphlets, as the Court recognized, have been historic
weapons in the defense of liberty.

The requirement of the invalidated ordinance that a license be se-
cured from a city manager before any literature may be sold or dis-
tributed was held by the Court to be void on its face, since no standard
was set for the exercise of the city manager's discretion and the official
was thus granted the uncontrolled power to license, and hence to censor,
the freedom of thought and the press. There was no restriction on the
official in respect to the protection of public morals, or maintenance
of public order, or the prevention of misuse or littering of the streets.
Standing as it was, unrestricted and unlimited, such power was held to
"strike at the very foundation of the freedom of the press by subjecting
it to license and censorship";19 and in view of the numerous prior hold-
ings of the Court,20 was in violation of the due process clause of the
Fourteenth Amendment.

Publix Theatres, Inc. v. American Tri-Ergon Corp., 294 U. S. 477 (1935); Robertson
and Kirkham, Jurisdiction of the Supreme Court of the United States (1936) 666.
18303 U. S. 444 (1938).

19Id. at 451.
(1931); Near v. Minnesota, 283 U. S. 697 (1931); Grosjean v. American Press Co., 297
U. S. 233 (1936); De Jonge v. Oregon, 299 U. S. 353 (1937); Herndon v. Lowry, 301
Whether an ordinance requiring a license for distribution which is restricted to the purpose of preserving public order and morals, or preventing the littering of the streets, can be upheld, is a question which is still in doubt. The requirement that a license be secured before distribution is without doubt a "prior restraint" of the press, a restraint strongly condemned in Near v. Minnesota and in the principal case itself. In Near v. Minnesota the essence of the doctrine of freedom of the press was held to lie in the distinction between prior restraint and punishment for the abuse of this freedom after the act has been committed.

Is, then, the power of the state limited merely to punishment for the abuse of the freedom of the press? Freedom from prior restraints has been held not to be an unlimited freedom, and where the public safety or the public policy requires it, prior restraints may be imposed. It would seem then that an ordinance requiring a license prior to distribution, which is limited to preserving public order, may be upheld. But restriction on the freedom of the press is the exception, not the rule, and a strong showing that the restriction is necessary for the preservation of public order will have to be made. In view of the strong position which the Court has taken on the maintenance of the freedom of the press, it will very likely regard with severity any attempt to restrict it. And, though the ordinance be valid, there is further constitutional protection in the requirement that it be enforced fairly and without discrimination.

In short, where public policies seem to conflict, a balance must be effected. An ordinance restricting the right to distribute literature will stand or fall, not so much on how clear a standard is set for the exercise of administrative discretion, but on the nature of the standards that are set.

Evidence Procured by Wire-Tapping

The Court in Nardone v. United States held that evidence secured by federal officers by means of intercepting telephone messages was rendered incompetent by Section 605 of the Communication Act of 1934. Ever since the decision in Olmstead v. United States, where

283 U. S. 697 (1931).
28"Of that freedom one may say that it is the matrix, the indispensable condition, of nearly every other form of freedom." Palko v. Connecticut, 302 U. S. 319, 327 (1937).
30302 U. S. 379 (1937).
32277 U. S. 438 (1928).
the Court, in the absence of statute, held that wire-tapping did not constitute an unreasonable search and seizure within the prohibition of the Fourth Amendment, the controversy has raged with respect to the morality of the practice of wire-tapping by officers to obtain evidence. This controversy, involving as it does a clash of conflicting public policies, was succinctly summarized by the late Justice Holmes in the *Olmstead case*: “Therefore, we must consider the two objects of desire, both of which we cannot have, and make up our minds which to choose. It is desirable that criminals should be detected, and to that end that all available evidence should be used. It also is desirable that the Government should not itself foster and pay for other crimes, when they are the means by which the evidence is to be obtained.”

This question was held to have been answered by Congress in enacting Section 605 of the Communications Act of 1934, the Court saying: “The answer is that the question is one of policy. Congress may have thought it less important that some offenders should go unwhipped of justice than that officers should resort to methods deemed inconsistent with ethical standards and destructive of personal liberty.” However, since the decision did not involve a reversal of the *Olmstead case*, this newly-enunciated protection from wire-tapping by federal officers rests upon statute rather than upon the Constitution itself.

**Due Process in Criminal Trials**

Whether a defendant, who is retried at the instance of the state because there had been errors prejudicial to it in the first trial, is denied due process of law within the meaning of the Fourteenth Amendment was decided in *Palko v. Connecticut.* 

A retrial at the instance of the Federal Government had been held by a closely divided court to be double jeopardy within the meaning of the Fifth Amendment, but the Court in the *Palko case* once again refused to read into the Fourteenth Amendment all the privileges and immunities embodied in the Fifth Amendment, unless “neither liberty nor justice would exist if they were sacrificed.”

Whether the procedure attacked in the *Palko case* was double jeopardy or not the Court refused to decide, because a decision as to the label to be applied would have no relation to the substantial nature of the

---

29 *Id.* at 470.
32 *Kepner v. United States, 195 U. S. 100 (1904).*
33 *Cf.* Twining v. New Jersey, 211 U. S. 78 (1908); Hurtado v. California, 110 U. S. 516 (1884); Maxwell v. Dow, 176 U. S. 581 (1900).
proceedings. Substantially, the Court held the prisoner was not
deprived of a liberty to which he was entitled, and the privilege granted to
the state was merely the reciprocal of the one enjoyed by him.

The *Palko case* is not authority for the proposition that a state may
harass a defendant by subjecting him to numerous trials where there
were no prejudicial errors in the previous trials. But if these acts are
in violation of the Fourteenth Amendment, they are so not because
they are called "double jeopardy," but because such conduct could not
be condoned without sacrificing the essentials of liberty. It cannot be
said that the procedure in the *Palko case* sacrificed these essentials.

In *Hale v. Kentucky*, the Supreme Court reversed the conviction of
a negro because the admitted systematic and arbitrary exclusion of
negroes from the jury list constituted a denial of the equal protection
of the laws guaranteed by the Fourteenth Amendment. This decision,
a substantial reaffirmation of the rights of the negro under the Fourteenth
Amendment, nevertheless laid down no new principle of law, the Court
having followed a consistent line of precedents established since 1880.

*Right to Vote—Poll Tax*

The decision in *Breedlove v. Suttles*, though a disappointment to
many who believed that a poll tax serves to disfranchise a substantial
portion of the propertyless members of the electorate reaffirmed
the established doctrine that the privilege of voting is not a privilege of
a citizen of the United States, but one derived from the states. A
state may grant or withhold this privilege, subject, however, to the
restrictions of the Fourteenth, Fifteenth and Nineteenth Amendments.
In upholding the Georgia statute making payment of a poll tax a pre-
requisite to voting, the Court held that it did not deny the petitioner
the equal protection of the laws, it was not an abridgement of the Nine-
teenth Amendment, and since the Fourteenth Amendment protects only
the privileges and immunities of citizens of the United States, it could
not be said to have denied the petitioner these privileges and immunities,

---

303 U. S. 613 (1938).

*Strouder v. West Virginia*, 100 U. S. 303 (1880); *Neal v. Delaware*, 103 U. S. 370
(1881); *Carter v. Texas*, 177 U. S. 442 (1900); *Norris v. Alabama*, 294 U. S. 587 (1935).


*The poll tax exists in Arkansas, Alabama, Georgia, Mississippi, South Carolina, Ten-
nessee, Texas and Virginia. In these states it is said to have the effect of reducing the
number of actual voters to 24% of the potential electorate, while in the states which
have no poll tax, 72% of the potential electorate vote. N. Y. Times, Sept. 18, 1938,
§ IV, p. 7.*

*Minor v. Happeresett*, 21 Wall. 162 (U. S. 1875); *Guinn v. United States*, 238 U. S.
347 (1915).

*Hamilton v. Regents of the University of California*, 293 U. S. 245 (1934).
since voting is a privilege derived from the state. With the law of the case, there can be little dispute. The classifications made by the statute were not so clearly unreasonable as to invalidate it, nor were they as clearly discriminatory as, for instance, the “Grandfather Clauses” which had been held to be unconstitutional.\(^40\) If the poll tax was clearly discriminatory, or was so high as to make apparent an attempt to deny to a particular group or economic class the right to vote, the question of its legality under the equal protection clause would certainly arise. But the Court failed to see, from the small tax involved, any discriminatory purpose. Finally, if voting is to be made a federal privilege, the Supreme Court cannot do it. Historically, the property qualifications for voting were removed by political and not court action,\(^41\) and the effect of the Supreme Court’s decision is to leave the question in the political field.

**Labor Injunctions**

No discussion of the cases involving civil liberties decided in the last term of the Court is complete without mention of the Court’s liberal interpretation of the scope of the Norris-La Guardia Act,\(^48\) an act designed to protect employees and their organizations from interference by injunctions in their exercise of important civil rights.\(^44\) In *Lauf v. E. G. Shinner and Co.*,\(^45\) the Court held the Act to apply whether or not an employer-employee relationship exists, and in *New Negro Alliance v. Sanitary Grocery Co.*,\(^46\) it was held to apply even to racial groups if they are involved in a dispute with an employer concerning terms and conditions of employment. These decisions are of considerable importance in preserving to parties engaged in industrial disputes their right to present to the public their side of the dispute in a truthful and peaceful manner.\(^47\)

---

\(^{40}\)Quinn v. United States, 238 U. S. 347 (1915).

\(^{41}\)Beard, Rise of American Civilization (1933) 542.

\(^{42}\)That the poll tax promises to become a political question of importance is evidenced by comments of President Roosevelt, N. Y. Times, Sept. 12, 1938, and Senator Glass, N. Y. Times, Sept. 14, 1938.


\(^{44}\)See Ibid., 29 U. S. C. § 104 for activities protected from interference by injunction. Of the right to picket, it has been said by the Supreme Court that “members of a union might, without special statutory authorization by a state, make known the facts of a labor dispute, for freedom of speech is guaranteed by the Federal Constitution.” Senn v. Tile Layers Protective Union, 301 U. S. 468, 478 (1938). See Frankfurter and Green, The Labor Injunction (1930).

\(^{45}\)303 U. S. 323 (1938).

\(^{46}\)303 U. S. 552 (1938). For a discussion of these cases see Note (1938) 26 Georgetown Law Journal 1026.

\(^{47}\)Senn v. Tile Layers Protective Union, 301 U. S. 468 (1938).
DECISIONS ON THE WAGNER ACT, OCTOBER TERM, 1937

One of the outstanding contributions of the Supreme Court at its October Term, 1937, was the development of the interpretation of the National Labor Relations Act.48 In the course of the preceding term, five cases had been heard and the decisions had resulted in laying the foundation upon which later decisions might rest.49

In the Jones & Laughlin case50 the Court had reviewed the general constitutionality of the law under consideration, the power of Congress to enact such a measure, the appropriateness of the procedure established, the propriety of the delegation of judicial power to the administrative agency, the jurisdiction of the National Labor Relations Board, and the validity of the statute as applied in that instance. The remaining cases were decided on the authority of the Jones & Laughlin decision, following findings, in each instance, that the law was properly applied in the existing situation. Each case involved an employer engaged directly in interstate intercourse, or predominantly engaged in the importation of raw materials and the exportation of finished products across state lines.

During the last term, seven decisions were handed down, and on five occasions writs of certiorari were denied.51 The causes considered dealt with procedure, the power of the Board to require affirmative action of a respondent found guilty of violating the Act, jurisdiction, and proper application of the definition of the term "employee" in Section 2 (3) of the Act. In almost every instance the Jones & Laughlin decision furnished the basis for the reasoning by which the Court reached its conclusion.

Three problems placed before the Supreme Court for final determination related to procedural questions. The process by which cases were to be handled by the Board and the courts had been held by the Supreme Court to provide adequate relief and protection against action of the administrative agency, in the Jones & Laughlin case. The question arose whether the Board might be enjoined from holding hearings or taking any other action before it had had an opportunity to determine

51 In one case, not discussed herein certiorari was denied, allowing to stand the lower court's decision that the questions were moot. National Labor Relations Board v. Delaware-New Jersey Ferry Co., 302 U.S. 738 (1937).
whether it had jurisdiction over the matter. The Supreme Court not only determined that the available administrative remedy must be exhausted before recourse is had to the courts, but did so in such terms as to lead to the conclusion that federal district courts have no jurisdiction over cases involving application of the National Labor Relations Act, except during recess of a circuit court of appeals or in relation to the enforcement of Board subpoenas. In the Mackay case the respondent contended that due process of law had been denied it by refusal of the appellant Board to issue an intermediate report by means of which it might have been appraised of the charges against it. On this point, the Court decided that such a step was unnecessary in view of the fact that the complaint specified the charges and the hearings developed them sufficiently to give the employer adequate notice of the subject matter of the proceedings. The third question of procedure arose in the prosecution by the Board of a case against the Republic Steel Corporation. In that case, the employer had petitioned the Circuit Court of Appeals for the Third Circuit for review of a Board order. When the administrative agency announced that it intended to withdraw its order for the purpose of instituting further proceedings, an injunction was issued to prevent such action and the National Labor Relations Board was required to file a transcript of the record with the circuit court of appeals. Upon appeal, the Supreme Court held that the court below had no jurisdiction over a cause until a transcript had been filed and that the Board was free to withdraw any order at any time prior to such filing.

In the Greyhound cases the Board presented the question whether

---

54The same question is presented in Consolidated Edison Company of New York, Inc. v. National Labor Relations Board, 58 Sup. Ct. 1038 (May 16, 1938).
55In the Matter of National Labor Relations Board, 304 U. S. 486 (1938).
56During the present term the Supreme Court has granted a writ of certiorari in a case which presents a situation the converse of that involved in this case. Ford Motor Company v. National Labor Relations Board, 59 Sup. Ct. 80 (Oct. 10, 1938). In the Ford case the appeal is against the action of the Circuit Court of Appeals for the Sixth Circuit in allowing the Board to withdraw its order, after the transcript has been filed, together with a petition for enforcement of the order. The decision of the Board to proceed in this manner was reached following the decision in Morgan v. United States, 304 U. S. 1 (1938) and before that in National Labor Relations Board v. Mackay Radio & Telegraph Co., 304 U. S. 333 (1938). The object of the Board in so doing was to perfect its procedure by submitting proposed findings of fact, proposed conclusions of law and proposed order in lieu of a trial examiner's intermediate report.
it was empowered to require the respondents to disestablish company-dominated unions as representatives of employees for purposes of collective bargaining and to post notices to that effect. The Supreme Court ruled that the Board might order a respondent to take any affirmative actions which would effectuate the policies set forth in Section 1 of the Act\(^59\) provided that it is shown by evidence that such action is necessary and that the remedy applied by the Board bears a reasonable relation to the action prosecuted and the end sought to be attained.\(^59\) In the *Remington Rand case*\(^60\) review was denied of a decision of the Circuit Court of Appeals for the Second Circuit holding, *inter alia*, that the Board might order reinstatement of striking employees, even though such action required discharge of persons employed to replace them, although allegations were made that some of the employees were guilty of misconduct. Certiorari was also denied in the *Carlisle Lumber case*,\(^61\) involving an essentially similar point.

The only rule which has been formulated for determining whether the Board has jurisdiction of any given enterprise was laid down in the *Jones & Laughlin case*, where it was held that jurisdiction depends upon whether conflicts which may reasonably be expected as a result of an unfair labor practice would have a substantial effect upon interstate commerce. The Court, in the *Santa Cruz case*,\(^62\) declared that no formula could be derived by which to decide arbitrarily what constituted an effect upon interstate commerce sufficiently substantial to give the Board jurisdiction. As in the *Jones & Laughlin case*, it was declared that this was a matter to be determined on the basis of the facts found in each instance.\(^63\) Subsequently, the Court allowed to stand a decision of the Circuit Court of Appeals for the Ninth Circuit in which it was held that a lumber manufacturer was within the jurisdic-


\(^{59}\) A similar question is presented in Consolidated Edison Company of New York, Inc. v. National Labor Relations Board, 58 Sup. Ct. 1038 (May 16, 1938), in which argument has been concluded, although in this instance the problem is whether the Board may order abrogation of a contract which had been negotiated by the employer under circumstances which accomplished a violation of the statute.

\(^{60}\) *Remington Rand, Inc. v. National Labor Relations Board, cert. denied, 304 U. S. 575 (1938).*

\(^{61}\) *Carlisle Lumber Company v. National Labor Relations Board, cert. denied, 304 U. S. 575 (1938).*

\(^{62}\) *Santa Cruz Fruit Packing Co. v. National Labor Relations Board, 303 U. S. 453 (1938).*

\(^{63}\) Consolidated Edison Company of New York, Inc. v. National Labor Relations Board, 58 Sup. Ct. 1038 (May 16, 1938), cited supra note 54, presents an unusually interesting aspect of the problem in that there the employer distributes none of its products outside New York State although it imports all of its fuel from outside the state and a strike in its plant would threaten interstate communication and transportation agencies, and also producers of goods for export to other states.
tion of the Board, although no raw materials were imported, but the greater part of its finished products was shipped to other states.64

The Supreme Court was also faced with the problem in the Mackay case of deciding whether employees who went on strike prior to the commission of an unfair labor practice by the employer might properly be deemed to be employees within the meaning of Section 2 (3) of the National Labor Relations Act.65 It was the opinion of the Court that so long as a labor dispute was current, it was immaterial whether the unfair labor practice occurred prior to or subsequent to the commencement of the dispute and the strikers remained employees for the remedial purposes of the statute. Certiorari was denied in four cases in which the interpretation of this section of the Act by the Board had been affirmed by the courts below. In the Carlisle Lumber case and the Jeffery-De Witt case68 the unfair labor practice had occurred before the enactment of the statute, but the labor dispute was current on the effective date of the Act. The Carlisle Lumber and Remington Rand cases involved allegations by the employers that striking employees had been guilty of misconduct and therefore were not entitled to consideration as employees within the meaning of the Act. The Black Diamond case67 merely raised the question whether persons who voluntarily left the employment of the petitioner came within the purview of the statute.68

JAMES G. BOSS*

67Two cases now before the Court raise questions related to those raised in the causes just discussed. National Labor Relations Board v. Columbian Enameling and Stamping Company, 59 Sup. Ct. 86 (Oct. 10, 1938), presents the question whether employees forfeit their status under Section 2 (3) by going on strike in violation of the terms of a contract with an employer, while in National Labor Relations Board v. Fansteel Metallurgical Corporation, 59 Sup. Ct. — (Nov. 21, 1938), the chief problem is whether employees forfeit such status by engaging in a "sit-down" strike and acting in contempt of a state court order, in the course of a strike which followed unfair labor practices by the employer.
68Comment on Civil Liberties prepared by Philip Treibitch; Comment on Wagner Act Decisions prepared by Harry B. Merican.
BANKRUPTCY— a subject of supreme importance to society if man is to be relieved of past mistakes so that he may resume his role of increasing the output of goods and services— has properly received from the Constitution and Congress the attention that it deserves.

For the Constitution provides that "The Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States" (Article I, Section 8, Clause 4). And, in pursuance of the plenary power thereby conferred, Congress has passed four bankruptcy acts — those of 1800, 1841, 1867, and the present one of 1898. Furthermore, the basic existing bankruptcy act, the Act of 1898, has been amended in 1903, 1906, 1910, 1917, 1922, 1926, and in every year from 1932 to 1938, inclusive.\(^2\)

\(^1\) 12 Stat. 19 (1800).
\(^2\) 5 Stat. 440 (1841).
\(^3\) 14 Stat. 517 (1867).
BANKRUPTCY ACTS BEFORE 1898

The first Act, that of 1800, was limited by its own terms to a five-year period of operation. It was repealed, however, in 1803 because the federal courts were not popular, most debtors were already in prison for debt, and the law was used by wealthy speculators to obtain discharges from their obligations. The second Act followed the panic of 1837. It was passed in 1841 and repealed in 1843. Daniel Webster's speech of June 5, 1840 was instrumental in the enactment of the provisions in this second Act, which for the first time allowed debtors to file voluntary petitions in bankruptcy, and contained the first statutory provisions with respect to the avoidance of preferences. The third Act, that of 1867, was also passed during a period of financial stress, which followed the close of the Civil War. Although this Act permitted a bankrupt to make a composition with his creditors, its defective administrative provisions caused such general dissatisfaction that it was repealed in 1878.

During the succeeding twenty years the only process for the realization and liquidation of insolvent estates was that provided under state insolvency laws, which were conflicting and proved ineffective in granting relief to honest debtors, in preventing preferences among creditors, and in checking fraud throughout the industrial centers of the country. With the phenomenal growth of interstate commerce and of interstate extensions of credit, moreover, the mercantile entrepreneurs considered it indispensably necessary to replace these ineffective and heterogeneous state laws by another federal bankruptcy act. The demand therefor arose within a few years after the repeal, in 1878, of the Act of 1867, continued with increasing intensity, and, hastened by the financial stress of debtors following the depression of 1893, finally resulted in adoption of the present Act, that of 1898.

ACT OF 1898, AS AMENDED THROUGH 1932

The Act of 1898 provided, as had the Act of 1867, that a person, as defined therein, in failing circumstances could effect a composition with his creditors. Although the purposes of the law were not novel,
its chief provisions, which were designed to carry these purposes into effect, were radically different, in the following ways, from those of the earlier bankruptcy laws of this country and also from the laws of all other countries:20

(1) The power of creditors to file bankruptcy petitions against their debtors was drastically circumscribed; the acts of bankruptcy were more limited in scope and in number than under the Act of 1867; and except where the debtor had fraudulently transferred or concealed property, or had admitted in writing his inability to pay his debts and his willingness to be adjudged a bankrupt, the creditors were required to show that at the time he committed an act of bankruptcy his assets, when fairly valued, did not equal the sum of his debts. A new definition of insolvency was thereby adopted. By contrast, under the English, Canadian, and most, if not all, of the Continental European laws, a debtor may be forced into bankruptcy for failure to pay his obligations as they fall due; and even under the Act of 186721 a banker, merchant, or trader who failed to pay his commercial paper within a short period after maturity could, on that sole ground, be put into bankruptcy.

(2) The criminal provisions of the Act of 1898 were similarly limited, and the grounds upon which a discharge could be denied were radically reduced in number, with the result that every debtor was guaranteed a full discharge in the absence of proof that he had committed a criminal offense or had fraudulently, and in contemplation of bankruptcy, destroyed or failed to keep books of account. To the extent by which these provisions permitted a debtor to avoid his indebtedness, they were unique in the civilized world.

(3) The purely administrative provisions of the Act were constructed on the theory that only creditors were concerned in the administration of the debtor's estate, the examination of the debtor, and his discharge; that the creditors could be relied on to meet together, elect competent trustees, and determine problems of administration; that they would be active in detecting and establishing the facts in cases involving fraud; and that they would protect the public interest at their own expense.

The Act of 189822 was a novel experiment in bankruptcy legislation, and under the stress of greatly changed social and economic conditions it has had quite unforeseen consequences. The most serious of these were those resulting from the breakdown of the theory of unlimited creditor-control and from the presumption that creditors can be relied on to take proper charge of the management and enforcement of the Act.

21See note 3, supra.
22See note 4, supra.
The amendments of 1903,\textsuperscript{23} 1906,\textsuperscript{24} 1910,\textsuperscript{25} 1917,\textsuperscript{26} 1922,\textsuperscript{27} and 1926\textsuperscript{28} served to strengthen the several so-called "acts of bankruptcy", the discharge and criminal provisions, and likewise various changes in the details of the administrative provisions of the Act, but they did not fundamentally change the Act of 1898. (The amendment passed on February 11, 1932\textsuperscript{29} merely exempted building and loan associations from being adjudged bankrupts.)

**Bankruptcy Reform Movements**

*Donovan Report*

Perhaps illustrative of the unforeseen consequences of the 1898 Act is the fact that whereas there had been 15,000 bankruptcy cases in 1921, involving secured claims of about $6,000,000 and liabilities of approximately $171,000,000, the number of bankruptcies and the magnitude of bankruptcy losses increased to such an appalling degree that in 1931 there were 60,000 bankruptcy cases involving secured claims of about $1,008,000,000. Moreover, the average amount paid to general creditors during the ten years ended December 31, 1931 averaged from only 5.1\% to 7.7\% of the amounts due them.\textsuperscript{30}

As a result of the increasing resort to the statute by corrupt debtors, a number of investigations, inquiries, and studies were made by various associations, committees, and organizations of lawyers and business men interested in the subject. These groups publicly criticized the administration of the law by the bench and bar of the country and advocated various reforms. In 1929 a thorough and searching investigation of bankruptcy administration in the Southern District of New York was conducted by Mr. William J. Donovan, representing the three bar associations of New York and Bronx Counties, with The Honorable Judge Thomas D. Thacher presiding at the hearings thereon.

The report\textsuperscript{31} outlined the prevalent abuses, their causes, and the principles upon which it was believed reform should be based; reported on the operation of the English and Canadian systems; and submitted specific recommendations for elimination of the major sources of the laxity, inefficiency, and corruption found prevalent, not only in New York but wherever inquiry in the United States was made during the course of the investigation. The committees and their staffs of lawyers and assist-

\textsuperscript{23}See note 5, *supra.*  
\textsuperscript{24}See note 6, *supra.*  
\textsuperscript{25}See note 7, *supra.*  
\textsuperscript{26}See note 8, *supra.*  
\textsuperscript{27}See note 9, *supra.*  
\textsuperscript{28}See note 10, *supra.*  
\textsuperscript{31}Donovan Report, House Judiciary Committee Print, 71st Cong., 3d Sess. (1931).
ants who aided Mr. William J. Donovan in the compilation of the report represented an organized effort to obtain, analyze, and integrate the considered opinion of every reliable and authoritative source of thought and experience, and the recommendations were submitted in a sincere belief that effective bankruptcy reform in the United States could be obtained only by adoption of the principles of administration embodied in such recommendations.

It was determined that the inefficiency and abuses found prevalent proceeded from two main features, which were not adapted to the changed business conditions. These were: (1) the slow-moving procedural machinery laid down by the Act, and (2) the theory upon which the whole administrative structure rested, namely, that the creditors in each particular case could be relied upon to control, supervise, and successfully manage the conduct of bankruptcy proceedings.

The report recommended: (1) more prompt administration of the law; (2) more simplified procedure and administration; (3) relieving the courts of administrative responsibilities and centralization of such responsibilities in the executive branch of the Federal Government; (4) limitation of creditor control through committee action to cases where the committees were genuinely interested; (5) the thorough examination of all bankrupts in all cases, permitting trustees to object to discharges; and (6) the strict enforcement of the criminal and discharge provisions of the Act.

Many of the changes recommended in the Donovan Report were suggested by the committee on legislation of the National Association of Referees in Bankruptcy and were approved in October 1929 at the convention of the association in Memphis, Tennessee.

It is interesting to note that at the time the Donovan Report was being prepared, The Honorable William O. Douglas, Chairman of the Securities and Exchange Commission (the executive governmental agency designated to aid the nation's bankruptcy courts in the administration of the corporate-reorganization provisions of the Chandler Act) held a law professorship at Yale Law School and was conducting extensive research studies in connection with studies made by the Yale Law School. Mr. Donovan acknowledged that without his aid much of the research work relating to the Donovan Report29 could not have been done. The United States Department of Commerce also carried on a series of studies concerning the causes of bankruptcies, at first independently, but later in cooperation with Yale Law School, which extended the inquiry into the administrative field.

The Donovan Report was the first thorough investigation of its kind

29Id. at (v).
conducted since the passage of the Act of 1898. It played an important part in molding the legislation that followed. It formed the basis of the study for the Chandler Act.

**Thacher-Garrison Report and the Hastings-Michener Bill of 1932**

In view of the increasing need and demand for reform and in view of the social and economic importance of having a sound bankruptcy law to meet the changing requirements of the day, former President Hoover authorized the Attorney General to undertake an exhaustive and vigorous investigation of the whole question of bankruptcy law and practice. The work was to be done under the direction of the Solicitor General, assisted by the Department of Commerce.

The Solicitor General, The Honorable Thomas D. Thacher, who had presided over the Donovan investigation hearings in New York City during 1929, and the Special Assistant to the Attorney General, namely, The Honorable Lloyd K. Garrison, submitted a report to former President Hoover on December 8, 1931. It outlined the exhaustive, nationwide scope of the investigation and the defects that were prevalent in the law and its administration, together with a proposed bill containing remedial amendments believed necessary to cure such defects.

In a message addressed to both Houses of Congress, dated February 29, 1932, President Hoover, on the basis of a review of the above-described report and apparent concurrence therewith, referred to statistics indicating the abnormal increases in bankruptcy cases, liabilities, and losses to creditors from 1921 to 1931. He concluded that the increases were not due to the economic situation, but to deeper causes, and he stated his views to the effect that a sound bankruptcy system should operate to: (1) relieve honest but unfortunate debtors of an overwhelming burden of debt; (2) effect a prompt and economical liquidation and distribution of insolvent estates; and (3) discourage fraud and needless waste of assets by withholding relief from debtors in proper cases. He also commented on the findings of the report, suggested amendments to the Bankruptcy Act, and earnestly commended the bill proposed by the Solicitor General to remedy and reform the bankruptcy system then in operation.

The reader should note that the Thacher-Garrison report did not favor the repeal, but rather the amendment, of the existing law.

---

83See note 4, *supra*.
84*Sen. Doc. No. 65, 72d Cong., 1st Sess. (1932).*
85*Id.* at vii-xii.
86*Sen. Doc. No. 65, 72d Cong., 1st Sess. (1932).*
87*Id.* at 39.
fact was again emphasized, in the course of the hearings on the Hastings-Michener Bill, by Mr. Lloyd K. Garrison.

The Hastings-Michener Bill, introduced in Congress early in 1932, attempted to perfect the Bankruptcy Act as a medium of distribution and provided for remedies to falling debtors without the stigma of an adjudication in bankruptcy. It was designed in a sincere effort to save business concerns without forcing them into liquidation. The provisions of the bill were so drawn as to: (1) relieve the debtor from the distasteful involuntary proceedings by permitting assignments for the benefit of creditors under the bankruptcy law; (2) offer wage earners relief against garnishments and other attachments without the stigma of bankruptcy; (3) draw a sharp distinction between, on the one hand, proceedings involving the adjudication and designation of the debtor as a bankrupt, the liquidation of his assets, and his thorough examination by salaried examiners, and, on the other hand, proceedings for the relief of debtors by provisions for extension of indebtedness in the nature of a moratorium, which would have been available only to "debtors" and not to "bankrupts", and which provided that the referees were to have jurisdiction over the entire proceedings in the attempt to prevent abuses and to simplify and expedite the proceedings; and (4) provide a simple process, under the administration of the bankruptcy courts, for the reorganization of corporations.

Furthermore, it provided measures to make the discharge provisions just and effective, and to discourage fraud. It gave the referees jurisdiction to grant discharges without application therefor. It provided, in the public interest, for a thorough examination of every bankrupt by a staff of full-time salaried administrators and examiners along with other measures aimed toward a simplified, effective, and expeditious administration of estates. Several procedural amendments were also proposed, including the delegation, to salaried administrators, of certain functions that the Donovan Report had recommended for administration by a Federal Bankruptcy Commissioner. Finally, the bill recommended that referees be placed on a full-time basis "as the reasonable convenience of the parties may permit".

The amendments proposed by the Hastings-Michener Bill emphasized

---

39 See id. at 309.
40 S. 3866, 72d Cong., 1st Sess. (1932).
41 Donovan Report, supra note 31, at 29 et seq.
existing, recognized defects and reforms proposed to strengthen our bankruptcy system. Although the bill was not enacted into law, the commendable work of the Department of Justice and its staff was not altogether fruitless. The bill was a little ahead of its time. Its proposed revisions, sincerely but possibly unwarrantedly, believed to be of too revolutionary a nature, were strongly opposed by the American Bar Association and others interested in effecting a reformation of the bankruptcy system. It accomplished, however, much foundation work, which did not have to be repeated, and made possible the enactment of much of the so-called emergency relief legislation that followed soon thereafter. It gave the Congress an intelligent factual basis upon which to reflect, compare, and contrast in enacting emergency relief legislation. In fact, most of the remedies sought to be put into effect by the Hastings-Michener Bill can be found incorporated in the Chandler Act, after, of course, being supplemented and strengthened in the light of continued and extensive research studies, investigations, conferences, statistical analyses, and hearings, including the studies, investigations, and recommendations of the Securities and Exchange Commission pursuant to Section 211 of the Securities Exchange Act of 1934, the reports of the Select Committee of the House of Representatives to Investigate Real Estate Bondholders Reorganization, and the McAdoo Committee reports on receivership and bankruptcy proceedings and administration in United States Courts.

There were two fundamental objections that, according to the House committee report, precluded enactment of the bill. They were presented by representatives of the American Bar Association and others, who were opposed, first, to the establishment of a central bureau for administration of the law through administrators and examiners and, second, to a complete revision of the Act because of the effect on the

48 Hearings before House Judiciary Committee on H. R. 6439 and H. R. 8046, 75th Cong., 1st Sess. (1937); and Hearings before Senate Judiciary Subcommittee on H. R. 8046, 75th Cong., 2d Sess. (1938).


50 Senate Special Committee Report to Investigate Bankruptcy and Receivership Proceedings and the Administration of Justice in the United States Courts (1936).


50 Hearings before Joint Judiciary Subcommittee on S. 3866, 72d Cong., 1st Sess. (1932).
interpretation of the Act by decisions accumulated in the intervening thirty-four years.51

No one should doubt the sincerity and earnestness of these conscientious objectors to the Hastings-Michener Bill, just as it would be error to question the sincerity and desire on the part of the proponents of the bill to bring about the equitable and wholesome objectives that all persons both for and against the bill felt were necessary. In recognition of this common purpose or end, with only the means causing the main opposition to the bill, the American Bar Association was requested, at the close of the hearings, to prepare and submit to the subcommittees a consensus of its opinion as to the manner in which the bankruptcy law ought to be amended.

CREATION OF NATIONAL BANKRUPTCY CONFERENCE52

As a result of such congressional suggestion the National Bankruptcy Conference, composed of judges, lawyers, accountants, economists, law school professors, and other groups and individuals interested in bankruptcy legislation, was created in 1932. Still in existence, it is an unofficial body made up of members representing, without binding, various interested groups, such as the American Bar Association, National Association of Credit Men, Association of the Bar of the City of New York, Federal Bar Association of New York, American Bankers Association, United States Chamber of Commerce, and American Institute of Accountants.

Committees were appointed, and the work of drafting a permanent, sound, and equitable bankruptcy system was begun on June 20, 1932. At the first session, after concluding that a "short bill", meeting the immediate necessities, should first be prepared and that a "long bill", covering desirable and necessary, though not urgent, changes should be presented at a later date, the Conference prepared the "short bill" or "Boston Draft", which was accepted in large measure by the American Bar Association Committee and included in a progress report to that Association.53

On invitation of Mr. Jacob M. Lashly,54 the second session of the Conference was held in September 1932 to perfect the "Boston Draft". Due, however, to the emergency relief legislation introduced in the House of Representatives shortly afterwards, all opportunity for early

---

51See also 57 A. B. A. Rep. 411 (1932).
52For a list of members see Analysis of H. R. 12889 Com. Print, 74th Cong., 2d Sess. (1936) 236, 237.
54Then Chairman, Standing Committee on Commercial Law and Bankruptcy, American Bar Association.
action on the draft was removed. Succeeding conferences prepared six drafts of the proposed revision of the Act before it was finally introduced in the House by The Honorable Walter Chandler on January 20, 1936.

BANKRUPTCY-RELIEF LEGISLATION

During January 1933 increased pressure from every part of the country for federal relief from overburdening debts began to be manifested to the Senate and House Judiciary Committees. It resulted in the speedy passage of various suggested emergency bankruptcy and moratorium measures. Members of the American Bar Association, the National Association of Referees in Bankruptcy, the Commercial Law League of America, the National Bankruptcy Conference, and other interested organizations gave freely of their services to congressional committees in an effort to aid the committees work out a relief program containing the fewest inconsistencies with sound and long-established legal principles.

The incoming administration embarked upon a plan of legislation designed to improve business trading, restore property values, reduce liabilities, and broaden the credit structure. To facilitate the payment of debts, credit and currency-expansion legislation was passed, and a "five-point bankruptcy relief program" for the relief of debtors was projected. Three of the "five points" dealt, respectively, with "Compositions and Extensions," "Agricultural Compositions," and "Extensions and Reorganization of Railroads Engaged in Interstate Commerce." These were set out, in a new Chapter VIII as Sections 74, 75, 76, and 77, after the jurisdiction of the bankruptcy courts had been enlarged to the extent necessary, by enactment of Section 73, which Congress passed as the "Amendatory Act of 1933" and which the President signed on March 3, 1933.

Concerning the three "points" referred to, Section 77, relating to the reorganization of railroads engaged in interstate commerce, was availed of most. It afforded greater latitude and flexibility and proved more economical than the equity receivership form of action.

With respect to Section 77, Congressman Chandler, in view of the

---

55Congressman from Memphis, Tennessee; Chairman of the Sub-Committee on Bankruptcy of the House Judiciary Committee.


57Id. at 1470, 11 U. S. C. at § 203.

58Id. at 1474, 11 U. S. C. at § 204.


increasing threat that more railroads might apply for reorganization under this section because of their reduced net incomes, introduced on April 25, 1938, a bill\textsuperscript{62} embodying significant departures from the procedures and purposes of the present Section 77. This bill, no doubt, will be reintroduced during the next session of Congress.

As originally passed, Section 75(a), known as the Frazier-Lemke Relief Act, was successfully attacked in the courts during the process of administration and was declared unconstitutional by the Supreme Court of the United States on May 27, 1935.\textsuperscript{68}

Subsequent to the above-mentioned decision Congress passed amendments to various subdivisions of Section 75, including subdivision (s), which were enacted and approved August 28, 1935.\textsuperscript{64} The constitutionality of subdivision (s), as amended, was approved and upheld by the Supreme Court on March 29, 1937.\textsuperscript{65}

Senator Frazier introduced a bill extending Section 75 as a permanent part of the Act, and it was so passed by the Senate on July 22, 1937. But the House limited its operation to two additional years, expiring March 1, 1940 along with other amendments. As thus amended, it was enacted and approved by the President on March 4, 1938.\textsuperscript{66} At the hearings,\textsuperscript{67} held December 17 and 18, 1937 and January 5, 6, and 7, 1938, Chapter XI of the Chandler Act was shown to be able to provide a more comprehensive form of bankruptcy relief with much less costly and complicated machinery. For this reason the aforementioned time limitation was agreed upon by the Senate committee and passed as stated above.

The fourth point in the bankruptcy-relief program dealt with corporate reorganization. It failed of passage in the 72nd Congress, but was reintroduced in various forms in the 73rd Congress, and was finally enacted and approved June 7, 1934\textsuperscript{68} as Section 77B. It was never directly passed upon by the Supreme Court, the bar of the country having apparently concluded that since the general purposes and provisions of 77B were so similar to Section 77,\textsuperscript{68} which had been upheld\textsuperscript{70}

\textsuperscript{62}H. R. 10387, 75th Cong., 3d Sess. (1938).
\textsuperscript{65}Wright v. Vinton Branch of the Mountain Trust Bank of Roanoke, 300 U. S. 440 (1937).
\textsuperscript{67}Hearings before House Judiciary Committee on S. 2215, 75th Cong., 3d Sess. (1937-1938).
\textsuperscript{68}48 Stat. 911, 912, 922-923, 991, 11 U. S. C. §§ 76 (a), 103, 103 (a), 107, 202 (a), 203, 203 (a), 204, 205 (a), 206, 207 (1934).
by the Court, that this statute would also be declared constitutional. In this connection it is to be noted that in affirming the decision of the Sixth Circuit Court of Appeals in the case of *Tennessee Publishing Company v. American National Bank*, the Supreme Court refused to pass upon the constitutionality of former Section 77B (b) (5) of the Act of 1898, as amended.

Significant, moreover, to observe is that after former Section 77B had been in operation less than two years, the Standing Committee on Commercial Law and Bankruptcy of the American Bar Association stated in 1936, on the basis of reports and statistics taken from the Dun & Bradstreet Monthly Review: "... We are of the opinion, however, that the debt reduction is a very substantial amount and that the law is developing into a fairly efficient instrument for the achievement of that purpose, debt reduction." Thus it appears that the opinion of many changed from the time the former Section 77B was enacted into law and that the bench and bar of the country, after giving the statute a fair trial and an opportunity to accomplish the debt reduction that was so urgently needed, found the statute to be a good workable law and far superior to the old equity receivership practice. This conclusion appeared to have been reached in spite of many shortcomings and ambiguities, which, however, are believed to have been cured with respect to substance, administration, and procedure by Chapter X of the Chandler Act.

An amendment adding subdivision (3½) to former Section 77B(c), authorizing debtors or trustees to lease or sell estate property with the courts' approval was introduced by Congressman Kramer and was approved and enacted on August 12, 1937.

The "Conservator in Bankruptcy Act", introduced by Congressman Sabath on January 27, 1936 as H.R. 6963, was reintroduced in the 75th Congress, reported favorably by the House Judiciary Committee on June 17, 1937, passed by the House, and sent to the Senate. It died, however, in committee. It would have added a new section, 77 C, to the Bankruptcy Act, giving the Securities and Exchange Commission the power to intervene in reorganization proceedings under former Sections 74 and 77B, so that, as a party in interest, the Commission could perform purely advisory functions to the courts. It provided,

---

7299 U. S. 18 (1936).
7Congressman Charles Kramer from California.
7Congressman Adolph J. Sabath from Chicago, Illinois; Dean, House of Representatives.
moreover, for the regulation of protective committees under the jurisdiction of the Commission. This bill doubtless will be reintroduced in the coming session of Congress, in accordance with a sincere and conscientious desire to bring about effective reforms in all phases of the reorganization field.

The constant and active interest in bankruptcy legislation and reform shown by the American Bar Association is interesting to note. In commenting on the bill referred to immediately above, for instance, the Association's Standing Committee on Commercial Law and Bankruptcy reported in 1938,\(^7\) without making any recommendations, that "in its judgment whatever is good in H.R. 6963 is now incorporated in the Chandler Bill (Chapters X and XI), the draftsmanship of which is superior to that of the Sabath Bill. If and when the Chandler Bill becomes a law, there will be no place in the picture for H.R. 6963 and its passage by the Senate would serve no purpose."

The fifth point in the bankruptcy-relief program found expression in the "Municipal Debt Readjustments" law, which, as embodied in Chapter IX, containing Sections 78,\(^7\) 79,\(^6\) 80,\(^8\) and 80,\(^8\) was enacted and approved on May 24, 1934,\(^2\) notwithstanding vigorous opposition from the American Bar Association.\(^3\) The Association believed that in the adoption of these sections there was an unconstitutional encroachment by the Federal Government upon the sovereignty of the states—a belief that was confirmed on May 25, 1936, when the Supreme Court declared these three sections unconstitutional.\(^4\)

Former Chapter X, containing Sections 81,\(^5\) 82,\(^6\) 83,\(^7\) and 84,\(^8\) and providing for the composition, through proceedings in bankruptcy, of the indebtedness of insolvent taxing agencies, was enacted and approved on August 16, 1937.\(^8\) This Act will expire on June 30, 1940. It was drawn to meet the objections of the majority opinion of the Supreme Court's decision in Ashton v. Cameron County Water Improvement District,\(^9\) and expressly avoided any restrictions on the states in the exercise of their sovereign powers. It was declared constitutional by

\(^{7}\)Advance Program of A. B. A. of the Sixty-First Annual Meeting, Cleveland, Ohio (July 25-29, 1938), 78.
\(^{7}\)Ibid., 11 U. S. C. at § 302.
\(^{7}\)Ibid., 11 U. S. C. at §§ 301-303.
\(^{8}\)58 A. B. A. Rep. 119, 122, 354 (1933).
\(^{9}\)Declared unconstitutional in Ashton v. Cameron County Water Improvement District, 298 U. S. 513 (1936); rehearing denied, 299 U. S. 619 (1936); 31 Am. B. R. (n. s.) 96 (1936).
\(^{5}\)Ibid., 11 U. S. C. at § 402
\(^{5}\)Id. at 659, 11 U. S. C. at § 404.
\(^{8}\)See note 84, supra.
the Supreme Court in *United States v. Bekins* and *Lindsay-Strathmore Irrigation District v. Bekins*,\(^{91}\) decided April 25, 1938. In his opinion, Mr. Chief Justice Hughes distinguished these cases from *Ashton v. Cameron County Water Improvement District*,\(^{92}\) holding the new law to be a valid exercise of the bankruptcy power.

In summarizing the conclusions of the Standing Committee on Commercial Law and Bankruptcy of the American Bar Association in 1934 with regard to the "five point program of bankruptcy relief legislation" enacted into law, Chairman Jacob M. Lashly stated:

"These acts unquestionably met an emergency need that was upon the American people at the time of their passage and yet presses there. They have afforded a stay which has resulted in the averting of violence and expressions of deep unrest in many sections of the country; they have created a diversion that is needed now; and they will, as time goes along, make a real contribution to the whole subject of compositions, extensions and rearrangements among creditors and debtors. But it is not believed that any of these or all five of them will make a very significant contribution to the debt reduction, the *sine qua non* of release and recovery."

Observing a remarkably desirable elasticity of thought, the same committee, in reporting on corporate reorganization, stated in 1935:

"... If, as appears now, the fundamental principle involved in this procedure is sound and practicable, if the Law shall successfully pass the test of its constitutionality and if and when it shall have been amended so as to clarify its provisions and simplify and accelerate its operation, the federal judiciary will need to be augmented so as to enable them to discharge the added burdens which will undoubtedly be cast into their courts through its more popular use. Most important of all, the law gives promise of developing into a fairly efficient instrument for the achievement of that vital purpose, debt reduction."

The quotations above indicate that sentiment was gradually growing in favor of corporate reorganization, which enabled debt reduction, a necessary element in the process of restoring the nation's wealth ratio to a sound norm, to be effected. In prosperous times this ratio amounts to about 2.5 to 1, but in 1933 it reached the discouragingly low relationship of 1.4 to 1, which is computed by dividing $250,000,000,000, the estimated value of the wealth in this nation at the close of 1933, by $180,000,000,000, the estimated amount that the nation and its people owed one another.\(^{95}\)

MITCHELL S. DVORET

---

\(^{91}\) U. S. 27, 49, 50 (1938).

\(^{92}\) See note 84, supra.

\(^{93}\) A. B. A. Rep. 96 (1934).


\(^{95}\) Id. at 91.
NOTES

THE ATTEMPT TO SIMPLIFY THE FEDERAL ESTATE TAX*

This past spring an attempt was made to simplify the legislative structure underpinning the Federal Estate Tax. Few would argue that federal tax law is oversimple; yet the attempt at simplification came to naught. A veritable storm of opposition arose against the proposed change.¹ The story involved should prove to be of some interest.

Legally the federal estate tax is in reality two taxes. Section 301 (a) of the Revenue Act of 1926 imposes the basic Federal Estate Tax. Section 401 of the Revenue Act of 1932, as amended, imposes what is known as the additional Federal Estate Tax. In practice, the additional tax swallows the basic tax, the total federal tax levied upon any given estate being determined by the provisions of the additional tax. The sole use made of the rates and exemptions of the basic tax is in the determination of the credit due the taxpayer for state death duties paid.

A credit for state death duties paid was first introduced into the Federal Estate Tax in the Revenue Act of 1924.² That Act³ allowed the taxpayer to credit up to 25 per cent, against its federal liability, death taxes paid to one or more of the states.⁴ In response to pressure exerted by state officials,⁵ and as a measure of generosity in view of the fact that total federal tax collections were at the time outrunning budgetary requirements, the Federal Government, in the Revenue Act of 1926, increased the credit for state taxes paid to the present level—80 per cent of the amount due the Federal Government under the provisions of the Revenue Act of 1926.⁶ Most of the states,⁷ to derive

---

¹Much of the factual material herein contained was collected in connection with work done for and in collaboration with Messrs. L. L. Ecker-Racz, Louis Shere, and Carl Shoup of the U. S. Treasury Department.

³W. J. Shultz, AMERICAN PUBLIC FINANCE AND TAXATION, (1931) 558.
⁵Thus, if a taxpayer's state tax amounted to $3000, and its gross federal liability (before allowance of the credit) amounted to $10,000, the Federal Government allowed the taxpayer a $2,500 credit, thereby reducing the federal liability to $7,500, and total state and federal liability from $13,000 to $10,500.
⁶Preliminary Conference on Inheritance and Estate Taxation, appearing as an appendix to the 1924 Proceedings of the National Tax Association.
full advantage from this provision, have passed laws which in effect provide that in no case shall the liability to state death taxation be less than the amount allowed by the Revenue Act of 1926 as a credit against the Federal Estate Tax for state death taxes paid.

The crediting device has proved an effective means of insuring death duties as a source of state revenue against the danger of interstate competition for wealthy residents. For example, residents of Nevada, a State without a death tax, have paid no less total federal and state death tax since 1926 than have residents of Alabama, a State that has a death duty equal to 80 per cent of the federal basic estate tax. Due to the operation of the crediting device, Nevada, despite its refusal to pass either an estate or an inheritance tax, no longer gains a competitive advantage as a tax-free haven over states that impose taxes equal to 80 per cent of the basic federal tax.

The 72nd Congress, in trying to balance the federal budget, provided an additional estate tax in the Revenue Act of 1932, and further provided that this additional tax was not to be subject to the credit for state death taxes. This additional tax was rendered more severe in 1934 and again in 1935. Yet it remains free of any credit for state death duties paid. The result has been that the credit allowed for state taxes has declined year by year in relation to the total liability to the federal tax (before credit) from a high of 75.6 per cent for returns filed during 1931 to 18.5 per cent for returns filed during 1936. It is to be expected that, in each succeeding year, as fewer returns are filed under revenue acts passed prior to 1935, the credit for state taxes paid will continue to diminish in relation to gross liability to the federal tax.

The following statement appears in 1926 Annual Report of the New York State Tax Commission 12-13:

"There is great danger, if not a probability, that, with the Federal Government entirely withdrawn from this field of taxation, the State laws would become so unequal and discriminatory that there would be an irresistible demand for their complete abolition ... the credit provision of the present Federal law constitutes not an unwarranted interference with, but a guaranty to the States which desire such a system of taxation, that they shall not suffer an unwarranted interference on the part of other States."

Section 402 (a) of the Revenue Act of 1932 has not been repealed or altered in effect by subsequent revenue acts.
Statistics of Income for 1930 (Bureau of Internal Revenue, U. S. Treasury Department) 60-61.
Id. (1935) at 62-63.
The Revenue Bill of 1938, H. R. 9682, as proposed by the Committee on Ways and Means and accepted by the Committee of the Whole House, would have eliminated the additional estate tax by substituting its rate schedule for the original rate schedule fixed in the Revenue Act of 1926.\textsuperscript{16} The Committee on Ways and Means expressed the belief that this change would greatly lessen the complexities involved in the determination of the tax.\textsuperscript{17} In allowing the elimination of all references to the original rate schedule of the 1926 Act, and in therefore providing a single rate scale where two had existed, this change in the structural basis of the Federal Estate Tax would certainly have been a step toward tax simplification. As for the credit for state death taxes paid, the Committee proposed a 16.5 per cent credit against the gross liability to the Federal Estate Tax, under the belief that such a credit would be substantially equivalent to the credit of 80 per cent allowed against the 1926 rates.\textsuperscript{18} In large part, the opposition that arose against this attempt to simplify the Federal Estate Tax was based upon the belief that the proposed credit would be less favorable to the states than the existent credit.\textsuperscript{19}

The credit for state taxes on estates (net estates before exemption) of less than $1.2 million would have been greater under the proposal than under present law. The credit allowed estates larger than this would have been less under the proposal than under present law. Table I, on page 211, illustrates this point.

The variation between the existent and the proposed credits illustrated in the table is due to the fact that the original rate schedule of the 1926 Act, against which the existent credit applies, allows a greater specific exemption and employs a different curve of progression than does the rate schedule of the 1935 Act, against which the proposed credit would have applied.

Although about ninety-eight per cent of the taxable federal returns show net estates (before allowance of the specific exemption) of less than $1.2 million,\textsuperscript{20} the 2 per cent of the returns showing net estates in excess of $1.2 million incur over half of the liability to the Federal Estate Tax.\textsuperscript{21} Nevertheless, because small and middle-sized estates are sufficiently more numerous in most states than estates in excess of

\begin{footnotes}
\item[17]Ibid.
\item[18]Ibid.
\item[19]\textit{Hearings before Committee on Finance on H. R. 9682, 75th Cong., 3d Sess. (1938)} 599-603.
\item[20]\textit{Statistics of Income for 1935} (Bureau of Internal Revenue, U. S. Treasury Department) pt. 1, 49-55.
\item[21]\textit{Id.} at 56-61.
\end{footnotes}
Table I. Comparison, by size of estate, of the existent and the proposed credit provisions.

<table>
<thead>
<tr>
<th>Net estate before allowance of the $40,000 specific exemption (000 omitted)</th>
<th>Credit allowed for state death taxes paid (Expressed as percentages of “net estate before exemption”)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Existent Credit (80 per cent of the tax imposed by the Revenue Act of 1926)</td>
</tr>
<tr>
<td>$50</td>
<td>—</td>
</tr>
<tr>
<td>100</td>
<td>—</td>
</tr>
<tr>
<td>200</td>
<td>0.6%</td>
</tr>
<tr>
<td>600</td>
<td>2.3</td>
</tr>
<tr>
<td>1,000</td>
<td>3.3</td>
</tr>
<tr>
<td>1,200</td>
<td>3.8</td>
</tr>
<tr>
<td>1,400</td>
<td>4.1</td>
</tr>
<tr>
<td>2,000</td>
<td>5.0</td>
</tr>
<tr>
<td>5,000</td>
<td>7.8</td>
</tr>
<tr>
<td>10,000</td>
<td>10.7</td>
</tr>
<tr>
<td>50,000</td>
<td>14.9</td>
</tr>
</tbody>
</table>

$1.2 million, a majority of the states would have benefited (according to the indications available from the statistics concerning federal estate tax returns filed during 1936) had the proposal become law. Table II, on page 212, indicates that, on the basis of returns filed during 1936, thirty-three states would have benefited had the proposed credit been adopted.

Although it is not possible to determine absolutely which states would stand to lose a portion of their vested interest in the credit provision were the proposed change adopted, the data compiled in the *Statistics of Income* for the years subsequent to the enactment of the additional estate tax afford some evidence helpful in determining which States would have been adversely affected under the change. These data indicate that, over a period of years, New York and Pennsylvania would have been adversely affected by the change, and that Colorado, Connecticut, Delaware, Florida, Illinois, Indiana, Maine, Massachusetts, Michigan, Montana, New Mexico, North Carolina, Rhode Island, and Wisconsin would have suffered in certain years under the change.22

22 In three out of the four years for which data are available the credits for state death duties allowed in New York and Pennsylvania estates stood in higher relation to the gross liability of such estates to the federal tax than did the credit allowed all estates to the
Table II. Existent credit for state death taxes expressed as a percentage of the gross liability to the federal tax, by states.\textsuperscript{23}
(Tabulation based upon returns filed during 1936)

<table>
<thead>
<tr>
<th>State</th>
<th>Ratio of credit to gross liability</th>
<th>State</th>
<th>Ratio of credit to gross liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>12.1</td>
<td>Nebraska</td>
<td>11.5</td>
</tr>
<tr>
<td>Arizona</td>
<td>10.4</td>
<td>Nevada</td>
<td>—</td>
</tr>
<tr>
<td>Arkansas</td>
<td>9.3</td>
<td>New Hampshire</td>
<td>14.8</td>
</tr>
<tr>
<td>California</td>
<td>13.7</td>
<td>New Jersey</td>
<td>17.0</td>
</tr>
<tr>
<td>Colorado</td>
<td>19.5</td>
<td>New Mexico</td>
<td>7.4</td>
</tr>
<tr>
<td>Connecticut</td>
<td>16.5</td>
<td>New York</td>
<td>19.2</td>
</tr>
<tr>
<td>Delaware</td>
<td>17.3</td>
<td>North Carolina</td>
<td>23.1</td>
</tr>
<tr>
<td>Florida</td>
<td>24.8</td>
<td>North Dakota</td>
<td>5.3</td>
</tr>
<tr>
<td>Georgia</td>
<td>11.7</td>
<td>Ohio</td>
<td>15.4</td>
</tr>
<tr>
<td>Idaho</td>
<td>12.6</td>
<td>Oklahoma</td>
<td>16.1</td>
</tr>
<tr>
<td>Illinois</td>
<td>14.6</td>
<td>Oregon</td>
<td>16.2</td>
</tr>
<tr>
<td>Indiana</td>
<td>9.8</td>
<td>Pennsylvania</td>
<td>21.2</td>
</tr>
<tr>
<td>Iowa</td>
<td>7.8</td>
<td>Rhode Island</td>
<td>16.7</td>
</tr>
<tr>
<td>Kansas</td>
<td>8.6</td>
<td>South Carolina</td>
<td>9.9</td>
</tr>
<tr>
<td>Kentucky</td>
<td>14.5</td>
<td>South Dakota</td>
<td>4.9</td>
</tr>
<tr>
<td>Louisiana</td>
<td>13.5</td>
<td>Tennessee</td>
<td>12.4</td>
</tr>
<tr>
<td>Maine</td>
<td>14.8</td>
<td>Texas</td>
<td>12.0</td>
</tr>
<tr>
<td>Maryland</td>
<td>16.7</td>
<td>Utah</td>
<td>12.0</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>17.0</td>
<td>Vermont</td>
<td>18.3</td>
</tr>
<tr>
<td>Michigan</td>
<td>21.2</td>
<td>Virginia</td>
<td>13.7</td>
</tr>
<tr>
<td>Minnesota</td>
<td>16.1</td>
<td>Washington</td>
<td>15.5</td>
</tr>
<tr>
<td>Mississippi</td>
<td>13.4</td>
<td>West Virginia</td>
<td>10.9</td>
</tr>
<tr>
<td>Missouri</td>
<td>16.2</td>
<td>Wisconsin</td>
<td>19.0</td>
</tr>
<tr>
<td>Montana</td>
<td>9.4</td>
<td>Wyoming</td>
<td>7.1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>18.6</strong></td>
</tr>
</tbody>
</table>

\footnotesize{\textsuperscript{23}Id. (1935) at 62-63.}
Governor Lehman of New York, acting as spokesman for the opposition of the states to the proposed 16.5 per cent credit, made the following statements the basis for a request that the proposed credit of 16.5 per cent be raised to at least 50 per cent:

"The extent to which the Federal Government has and is ignoring the rights of the States in the income (personal and corporate) and estate tax fields and virtually monopolizing those fields to the exclusion of the States is truly alarming."

A little further on Governor Lehman has this to say:

"The Federal [estate] tax fixes a ceiling for State taxes. The proposed Federal estate tax is graduated to 70 per cent, and in the case of the larger estates takes considerably more than one-half. In the lower brackets the percentage taken is as high, if not higher, than should reasonably be exacted. It is unthinkable that the States will superimpose upon the Federal tax still higher duties. To do so would be unfair and uneconomic."

In weighing these statements, it may be noted that an estate worth $80,000 consisting of $40,000 insurance and $40,000 in other assets pays no federal estate tax. A $100,000 net estate (before exemption) pays a federal tax that amounts to but 4.2 per cent of the value of the net estate (before exemption). New York's present death duty exceeds the credit allowed against the federal tax throughout the entire rate scale. So also do the death duties imposed by Arizona, Kentucky, Minnesota, North Dakota and Oregon (upon estates fairly typical in asset composition and in distribution to beneficiaries).

Representatives of New York, Delaware, Illinois, New Jersey, North Carolina, and Connecticut appeared before the Senate Committee on Finance to oppose adoption of the proposed credit. Statements made by the officials representing New York and New Jersey concerning the relationship between their respective states and the Federal Government under the existent credit indicate certain discrepancies between the statistics concerning this relationship relied on by the Federal Government and those relied on by these state officials. Tax Com-

---

25Id. at 591.
26Ibid.
27Tax Law of New York, §§ 249 m-s.
28The hypothetical estates upon which this statement is based contain life insurance payable to the widow of the decedent in the amount of 10 per cent of the value of the estates. The distributable portion of the estates goes 40 per cent to the widow, 25 per cent to a minor child of the decedent, 15 per cent to an adult child of the decedent, 10 per cent to a brother, and 10 per cent to a friend.
29Hearings before Committee on Finance on H. R. 9682, 75th Cong., 3d Sess. (1938) 592-603.
missioner Graves of New York advocated either expansion of the proposed 16.5 per cent credit to 50 per cent of the gross liability to federal tax or retention of the existent credit. Mr. Graves stated that the existent credit allowed by the Federal Government to New York estates for state death duties paid approximated 25 per cent of these estates' gross liability to the federal tax. The data compiled from federal returns filed during 1936 indicate that the credit allowed New York estates amounted to but 19.2 per cent of such estates' gross liability to the federal tax. Tax Commissioner Martin of New Jersey estimated that it would require in New Jersey a credit against gross liability of over 20 per cent and perhaps fully 25 per cent to produce the same amount of credit for New Jersey estates as the existent credit now produces. The data compiled from federal returns filed during 1936 indicate that the credit allowed New Jersey estates amounted to but 17 per cent. Assistant Attorney General Greene of Illinois appeared to support Mr. Graves' general statements, but, curiously enough, stated that it would be better for Illinois were the proposed 16.5 per cent credit to be adopted. On the basis of returns filed during 1936 this statement was correct, the existent credit for state taxes allowed Illinois estates amounting in that year to but 14.6 per cent of these estates' gross liability to the federal tax. Commissioner Maxwell of North Carolina argued for either retention of the existent credit or increase in the proposed credit to a percentage figure that would, with respect to the large estates, be the equivalent of the existent credit.

Tax Commissioner Long of Massachusetts wrote a letter to Senator Walsh in which he advocated (a) that the Federal Government retire from the death tax field; (b) if the Federal Government would not retire from the field, that a very substantial credit for state taxes be allowed; and (c) if the Federal Government would not withdraw, and if it would not allow a more substantial credit, that the 80 per cent credit provision against the 1926 rates be retained in the federal tax. In the course of the letter Mr. Long made the following statement: "The law as proposed seems to me to affect Massachusetts quite seriously and, of course, it is equally bad in relation to other States." As has been pointed out, the available data indicate that the change

---

80Id. at 592-7.
81Table II.
82Hearings before Committee on Finance on H. R. 9682, 75th Cong., 3d Sess. (1938) 599.
83Table II.
84Hearings before Committee on Finance on H. R. 9682, 75th Cong., 3d Sess. (1938) 597.
85Table II.
86Hearings before Committee on Finance on H. R. 9682, 75th Cong., 3d Sess. (1938) 601.
87Id. at 6521-2.
would have benefited the majority of the states. As to Massachusetts, the data available from federal returns filed during 1936 show that the credit allowed Massachusetts estates for state taxes paid amounted to 17 per cent of such estates' gross liability to the federal tax.

On the one hand, the proposed credit would have allowed a desirable simplification of the structure of the Federal Estate Tax, and, consequently, simplification in the computations involved in the determination of tax liability and in the statistical tabulations based upon the data contained in the estate tax returns. On the other hand, the elimination of the original rate schedule of the basic Federal Estate Tax would have required that statutory adjustments be made by the nineteen states whose enactments designed to take advantage of the federal credit have been inflexibly tied to the original rate schedule. The change would probably have rendered most difficult further tax interrelationship between the Federal Government and those states whose vested interests in the credit provision would have been reduced under the proposed credit.

The question that had to be decided was, would the advantages derived from the proposed simplification of the Federal Estate Tax outweigh the disadvantages inherent in the requisite reworking of state tax laws and the decreased possibility of further tax interrelationships between the Federal Government and certain of the states?

In weighing the advantages to be derived from the proposed simplification it should be borne in mind that the number of persons affected by the estate tax is relatively insignificant. The estate tax affects less than one-third of one per cent of the number of persons affected by the income tax. It has been estimated that less than one per cent of the adult decedents in the United States leave estates large enough to be subjected to the Federal Estate Tax. Furthermore, executors and

---

**Notes**

[29] Table II.

[30] Ibid.


tax administrators have had the benefit of six years of experience under the dual rate schedule.

No definite weight can be assigned to the damage that would have been done to federal-state relations as a result of the need for revising state tax laws, had the original rate schedule been eliminated. Nevertheless, it may be noted that the need for revising state law as a consequence of federal reconstruction has served to foster resentment on the part of some states even when such revisions have improved the fiscal position of such states.44

In an address before the Association of the Bar of the City of New York, former Under-Secretary of the Treasury Roswell Magill made the following statement:45

“Everyone recognizes that an approach should be made toward the integration of the Federal and State taxing systems. . . . The real problem is the formulation of an effective plan of procedure. . . . Perhaps the best mode of procedure would be the designation of some responsible commission with a national standing to spend a year in a thorough-going study of possible alternatives and then to propose an acceptable program.”

The opposition expressed by state officials to the attempted simplification of the Federal Estate Tax is strong factual support for the Under-Secretary’s tentative conclusion that changes in the tax structure of one level of government that affect the fiscal position of the other level should be made only after careful research by “. . . some responsible commission with a national standing . . .” rather than by one of the two parties in interest acting alone.

WILLARD C. MILLS

“In its act designed to take advantage of the credit provision the Federal Estates Tax, the Nebraska legislature made this antagonistic statement, Neb. Comp. Stat. (1929) § 77-2307: “This act is not a commitment of the legislature to the principle of the coercive features of the Federal Estate Tax. It is accepted in order to protect the temporary interests of the people of the State of Nebraska.”

44(1938) 24 A. B. A. J. 245.
MAY A CORPORATION PURCHASE ITS OWN STOCK OUT OF CAPITAL?—THE PROBLEM REVISITED

UNLESS prohibited by statute, it is the prevailing legal doctrine that a corporation has the authority to purchase shares of its own stock.1 Naturally, to protect the individual interests of creditors and shareholders, a limitation must be placed upon such authority. Therefore, it is generally stated that such authority may not be exercised with an intent to injure the creditors or so as to affect their rights adversely.2

However, in applying this limitation upon the corporate authority, the courts do go further than merely stating than an intent to injure creditors, or the doing of an act detrimental to their rights will make such a contract invalid. A norm or standard has been found necessary and the courts, aware of this necessity, have generally stated that the capital stock cannot be impaired by the existence of such agreements. In other words, the purchase may only be made out of "surplus".3

3 "The stock of a corporation is its only basis of credit, and it is of vital importance that it be rigidly guarded and protected. Courts have conceived it to be their duty to detect and defeat any scheme calculated in any way to place the fund beyond the reach of the creditors." In re Fechheimer Fishel Co., 212 Fed. 357, 365 (C. C. A. 2d, 1914). See, West Penn Chemical & Manufacturing Co. v. Prentice, 236 Fed. 891 (C. C. A. 3d, 1916); Topken, Loring and Schwartz, Inc. v. Schwartz, 249 N. Y. 206, 163 N. E. 735 (1928); aff'd, Melniker v. American Title & Guaranty Co., 253 App. Div. 570, 3 N. Y. S. (2d) 198 (2d Dep't 1938); McIntyre v. Bement's Sons, 146 Mich. 74, 109 N. W. 45 (1906); Cleveland v. Jencks Mfg. Co., 54 R. I. 218, 171 Atl. 917 (1934); Hoover Steel Ball Co. v. Shafer Ball Bearings Co., 90 N. J. Eq. 164, 106 Atl. 471 (1919); Fremont Carriage Co. v. Thomsen, 65 Neb. 370, 91 N. W. 376 (1902); Tierney v. Butler, 144
Surplus represents an accumulation of economic values in excess of the amount called for by the total outstanding book value of the capital stock.\textsuperscript{4} Ordinarily, the term “surplus” is used as an indication of “earned surplus”, that is, surplus that has arisen through corporate enterprise from year to year not distributed in dividends or specifically reserved for other purposes. However, “surplus” may also arise from another source; from transactions entirely unrelated to the regular business of the corporation. Such a surplus constitutes “capital surplus” and may arise in various ways; from the sale of stock at a premium, from the acquisition of stock of the corporation by the corporation itself for less than the par value and from the sale of capital assets for a sum greater than their stated value.\textsuperscript{5}

As yet, the courts have not found it necessary to distinguish between “earned surplus” and “capital surplus” in applying the rule which requires a “surplus” to exist. The law has not concerned itself with the economic distinctions, but has been satisfied with its general doctrine that a “surplus”, in its broadest sense, must exist in order to substantiate agreements whereby a corporation is to acquire shares of its own stock.\textsuperscript{6}

Keeping in mind the desire of the courts to protect the individual interests of creditors and shareholders, it is interesting to note the seemingly inconsistent attitude of at least three jurisdictions. In Massachusetts and Wisconsin the cases were decided in the absence of any statute governing the matter. In Colorado a similar doctrine was evolved as a result of judicial construction of a statute applicable to the situation.

In Barrett v. Webster Lumber Company,\textsuperscript{7} a leading Massachusetts case, a holder of preferred stock in the corporation, in attempting to avoid his obligation to sell stock to the corporation on the ground that a corporation cannot purchase its own stock except out of surplus profits, was denied relief, even though at the time of the purchase the liabilities of the corporation, including its capital stock, exceeded the fair value of its assets. The court held that such agreements to purchase need not be limited to purchase or redemption of stock out of surplus. The corporation was solvent at the time of the contract, and the stock purchased was kept in existence, ready to be sold and transferred to another party. Therefore, under such circumstances, it was held not

Iowa 553, 123 N. W. 213 (1909); In re International Radiator Co., 10 Del. Ch. 358, 92 Atl. 255 (1914).
\textsuperscript{4} Dewing, Financial Policy of Corporations (1937) 579.
\textsuperscript{5} Ibid.
\textsuperscript{6} See cases cited note 3, supra.
\textsuperscript{7} 275 Mass. 302, 175 N. E. 765 (1931).
necessarily *ultra vires* for a corporation to purchase its own stock when surplus profits were not available. ⁸

As far back as 1905,⁹ it was suggested that the purchase of shares of its capital stock by a street railway company was illegal, and that a note given in payment for such stock was void. The only question as to legality which was brought to the attention of the court arose from the fact that a note was given for capital stock of the corporation, which its officers thought it desirable to buy. Such a purchase was held not to be "a reduction of the capital stock within the meaning of Rev. Laws, c. 112, § 22, for the stock was kept in existence, ready to be sold and transferred to another party."¹⁰ "The stock was property, and it was then supposed to be of value. The mere fact that subsequently it proved to be worthless does not affect the validity of the note."¹¹

This contention was upheld in subsequent cases.¹² Finally, *Scriggins v. Dalby*,¹³ expressed what we shall term the "Massachusetts Rule". It was decided, "that a corporation, though not expressly authorized, if not forbidden by statute, may purchase shares of its own stock, and that an agreement to do this is enforceable, subject, at least, to the limitations that the purchase must be made in good faith and without prejudice to creditors and stockholders." Citing *Dustin v. Randall Faichney Corporation;¹⁴ Barrett v. Webster Lumber Company;¹⁵ and Cummins & Pierce Company v. Kidder Peabody Acceptance Corporation*,¹⁶ the court continued, "No decision here has added the further limitation, independent of these limitations, that such a purchase can be made legally only out of surplus."¹⁷

In Wisconsin, a similar, though somewhat less rigid rule has been established. The courts of this state agree that capital stock is in the nature of a trust fund out of which creditors are to be paid, and recognize the existence of a general rule stating that corporations have no right to purchase their own stock and thereby deplete this fund. How-

---

⁸*Id.* at 308, 175 N. E. at 768. "The contention of the plaintiff that a corporation cannot purchase its own stock except out of surplus profits cannot be sustained."


¹¹*Id.* at 358, 73 N. E. at 645.


¹³*290 Mass. 414, 195 N. E. 749 (1935).*

¹⁴*263 Mass. 99, 160 N. E. 528 (1928).*

¹⁵*275 Mass. 302, 175 N. E. 765 (1931).*

¹⁶*282 Mass. 367, 185 N. E. 383 (1933).*

¹⁷*290 Mass. 414, 416, 195 N. E. 749, 751 (1935).*
ever, the Wisconsin courts are not inclined to adhere to the general rule to the extent that they allow such a purchase if it does not operate to deplete the fund available to creditors to an extent that would prejudice their rights. A corporation may buy its own stock, so long as its assets are greater than its liabilities, and for such purpose, the capital stock of the corporation is not to be considered a liability.\(^{18}\)

A third example of this doctrine is found in Colorado as a result of the judicial interpretation of its statute, which provides that, "Every corporation may redeem shares of its capital stock . . . , Provided, That it shall not be lawful for such corporations, to use any of their funds for the purchase of stock in their own company or corporation, when such use would cause any impairment of the capital of the corporation."\(^{19}\) The courts of Colorado have given the statute a literal interpretation, holding in *Colorado Industrial Loan and Investment Company v. Clem*,\(^{20}\) that there is nothing in the statute limiting purchase or repurchase agreements to surplus funds. Speaking of the statute, the court said, "It reads that it shall not be lawful for a corporation to use any of its funds for such purpose if it will cause an impairment. This language of itself implies that it is not restricted to any fund of its own. If the intention of the legislature was to restrict the fund to surplus, it would not have indicated that the corporation might use any fund that it possessed for that purpose, so long as no impairment of capital resulted."\(^{21}\)

Contrary to the "Massachusetts Rule", and in conformity with the great majority of states requiring the purchase of stock to be made from surplus, New York has seen fit to embody such a provision in its general laws. This statute provides, "A director of a stock corporation, or any of them by which it is intended. . . . (5) To apply any portion of the funds of such corporation, except surplus profits, directly or indirectly, to purchase shares of its own stock, is guilty of a misdemeanor."\(^{22}\) No corporation in New York, therefore, can buy its own shares of stock out of its capital stock without making the officers voting

\(^{18}\)Shoemaker *v.* Washburn Lumber Co., 97 Wis. 585, 73 N. W. 333 (1897); Calteaux *v.* Mueller, 102 Wis. 525, 78 N. W. 1082 (1899); Marvin *v.* Anderson, 111 Wis. 387, 87 N. W. 226 (1901); Pabst *v.* Goodrich, 133 Wis. 43, 113 N. W. 398 (1907); Gilchrist *v.* Highfield, 140 Wis. 476, 123 N. W. 102 (1909); Atlanta & Walworth Ass'n *v.* Smith, 141 Wis. 377, 123 N. W. 106 (1909); Turner *v.* Turner Manufacturing Co., 184 Wis. 508, 199 N. W. 155 (1924); Rasmussen *v.* Roberge, 194 Wis. 362, 216 N. W. 481 (1927); Koeppler *v.* Crocker Chair Co., 200 Wis. 476, 228 N. W. 130 (1930).

\(^{19}\)COLO. COMP. LAWS (1921) § 2260.

\(^{20}\)82 Colo. 399, 260 Pac. 1019 (1927).

\(^{21}\)Id. at 405, 260 Pac. at 1021-1022.

\(^{22}\)Penal Law § 664.
for such purchases violators of this law. If the corporation has no surplus when the contract is to be enforced, it cannot legally assume its obligation. In the case of Richards v. Weiner Company, the court found that a corporation is bound to perform unless it shows as an affirmative defense that it has no surplus. Evidently, the contract may be avoided by the declaration of a dividend by the corporation. Yet, the possibility of avoiding the performance does not void the contract. This event, that is, lack of surplus, does not make the contract a mere nudum pactum, but only makes it unenforceable.

In Topken, Loring & Schwartz, Inc. v. Schwartz, the Loring Glove Company sold and transferred to Schwartz one hundred and fourteen shares of capital stock with an agreement to purchase more under certain conditions. Paragraph four of the agreement provided, "The party of the first part does hereby agree to purchase from the party of the second part, and the party of the second part does hereby agree to sell to the party of the first part, any and all shares of the capital stock of the first part which may be held by the party of the second part at the end of the period of employment of the party of the second part by the party of the first part." Upon an attempt to enforce the contract, it was held that the contract would have been impossible of performance at the time intended if there were no surplus then existent out of which the purchase could be made. Since this agreement could only be enforced if the company had a surplus from which to make payment, it might not be binding on the employer, and thus it lacked the consideration necessary for enforceability.

Again in Cross v. Beguelin, enforcement of a similar agreement was sought, but in this case there were no general creditors or unpaid claims, except claims for salaries of officers and directors, accruing subsequent to the contract of purchase. The court decided that the underlying reason for the statutory limitation is the protection of creditors who became such in reliance upon the corporate capital. If there are no such creditors whose rights are infringed, the reason for the statutory restriction fails. Therefore, the claim of the plaintiff is valid and he is

24Ibid.
25Ibid. at 65, 100 N. E. at 593. "If, when the time came, the defendant had a sufficient surplus, the contract would be enforceable. If it had not the contract could not be enforced." Therefore, the burden rested upon the defendant to show that there was no surplus and that it would thus be illegal to enforce the contract.
27249 N. Y. 206, 163 N. E. 735 (1928).
entitled to judgment, enabling him to participate pro-rata with the remaining creditors of the corporation.

Upon appeal, the judgment of the Appellate Division was affirmed, the court holding that the agreement was enforceable only if a surplus existed at the time of enforcement. Here, however, the claim is not against the corporation, but against assets in the hands of the creditors, the claimants rights being superior to those of subsequent creditors of the corporation who became such with notice of the purchase by the corporation of its own stock.

Thus in New York, the contract was considered enforceable in one case, a mere nudum pactum in another, and then held to be enforceable in the latest case decided by the Court of Appeals.

New York is not alone in seeking to protect the creditors of corporations by enacting such statutes. Among the states which have made this rule a part of their statutory law are Illinois, Louisiana Tennesee, and West Virginia, all of them providing that no corporation can purchase shares of its own stock except where there is a surplus available for such purchase.

In Delaware and Rhode Island, the statutory provisions as to purchase and repurchase agreements by a corporation are identical with those of Colorado. However, the courts in these two states, contrary to the Colorado decisions, interpret the words, "any impairment of the capital of the corporation" as limiting such corporate transactions to surplus funds.

_Cleveland v. Jencks Manufacturing Company_, a leading Rhode

---

222 The Georgetown Law Journal [Vol. 27

34Every corporation shall have the power . . . (g) to acquire hold, sell and transfer shares of its own stock: Provided, that no corporation shall use its own funds or property for the purchase of its own shares of capital stock when such use would cause any impairment of the capital of the corporation.
36Every corporation . . . shall have the power to purchase shares of its own stock; provided no such corporation shall use its funds or property for the purchase of its own shares of capital stock when such use would cause any impairment of the capital of the corporation.
3754 R. I, 218, 171 Atl. 917 (1934).
Island case, involved a suit to recover damages for breach of a contract to purchase stock, the corporation being insolvent at the date the contract was to be enforced, rights of creditors having intervened. The rule was laid down that such a contract is a valid obligation, but is enforceable only when the purchase would not impair the capital of the corporation to the detriment of creditors. Citing Adams v. New England Investment Company,39 and Garon v. Credit Foncier Corporation,40 the court said, "it is a fundamental principle of law that the capital of a corporation is a trust fund for its creditors and must not be depleted by allowing a claim arising through an agreement to purchase its own stock."41 This court expressly recognized the similarity of the Delaware and Rhode Island statutes, and agreed with the conclusion in the case of In re International Radiator Company,42 a leading Delaware case, wherein purchases were limited to corporate surplus.43

The rule that the purchase of stock must be made from "surplus" has been adopted by the courts in almost all of the states in which the point is not controlled by statute.44 Generally it is held, in the absence of statute, that no corporation can purchase its own stock with its capital to the injury of the creditors of the corporation. These states base their findings on the theory that capital is held in trust for the creditors, and that transactions leading to impairment of capital will not be enforced, or will be considered illegal if rights of creditors are affected. "The stock of a corporation is its only basis of credit, and it is of vital importance that it be rigidly guarded and protected. Courts have conceived it to be their duty to detect any scheme or device calculated in any way to place this fund beyond the reach of creditors."45

It has been said, as a summary of the majority rule, that,

---

33 R. I. 193, 80 Atl. 426 (1911).
37 R. I. 237, 92 Atl. 561 (1914).
54 R. I. 218, 221, 171 Atl. 917, 918 (1934).
10 Del. Ch. 358, 92 Atl. 255 (1914).
Id. at 360, 92 Atl. at 255. "The impairment of the 'capital' . . . means the reduction of the amount of the assets of the company below the amount represented by the aggregate outstanding shares. . . . A corporation may use only its surplus for the purchase of shares of its own capital stock when the value of its assets is less than the aggregate amount of all the shares of its capital stock. A use by a corporation of its assets to purchase shares of its own capital stock under such conditions impairs the capital of the company."

"On principle, a purchase by a corporation of its own stock from surplus should be upheld by the courts, (1) provided a legal and proper corporate object is advanced, (2) provided the condition of corporate affairs warrants it, (3) provided the transaction is designed and carried out in entire good faith, (4) provided the corporation received full and clear value, (5) provided there is not intended, and there results no undue advantage to a few favored stockholders at the expense of the remainder, (6) provided the rights of creditors are not jeopardized."46

CONCLUSION

In view of the express intention of all the courts in all the states to protect the interests of creditors of corporations, it is interesting to note the possible detrimental consequences that may result from an application of the "Massachusetts Rule".

In Wisconsin, a depletion of the capital stock is permitted, but the court must determine to what extent such a depletion is advisable. Though flexibility in other fields may be highly desirable, the uncertain situation here, where no specific standard is established, does not afford the creditors of the corporation the security to which they are entitled. Those who deal with corporations, and extend them credit, should be assured that the factors upon which they originally relied in extending credit, will not be varied as a result of the lack of an adequately defined standard.

The capital stock of a corporation is in the nature of a trust fund,47

46Wormser, Power of a Corporation to Acquire Its Own Stock (1914) 24 Yale L. J. 177, 188. See also, Wormser, Disregard of the Corporate Fiction and Allied Corporation Problems (1929) 120, 141.

47While it is true that the language has been frequently used to the effect that the assets of a corporation are a trust fund held by a corporation for the benefit of creditors, this has not been to convey the idea that there is a direct and express trust attached to the property.

"... The corporation is an entity distinct from its stockholders, as from its creditors. Solvent, it holds its property as any individual holds his, free from the touch of a creditor who has acquired no lien; free also from the touch of the stockholder who, though equitably interested in, has no legal right to, the property. Becoming insolvent, the equitable interest of the stockholders in the property, together with their conditional liability to creditors, places the property in a condition of trust, first for the creditors, and then for the stockholders. ... It is rather a trust in the administration of the assets, after possession by a court of equity than a trust attaching to the property as such, for the direct benefit of either creditor or stockholder." Hollins v. Brierfield Coal & Iron Co., 150 U. S. 371 (1893). See also, Ratcliff v., Clendenin, 232 Fed. 61, 66 (C. C. A. 8th, 1916).

In Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, 50 N. W. 1117 (1892), it was found that the capital of a corporation is not a trust for creditors except in the sense that there can be no distribution of it among stockholders without provisions being
and should not be reduced if the interests of the beneficiaries of the fund are to be preserved. The “Massachusetts Rule” presupposes that there would be no such impairment, since, the stock purchased is to be kept in existence, and ready to be transferred to another party at any time. What protection is afforded creditors should the corporation subsequently become insolvent? Under such circumstances the stock purchased has no value. Yet, it is this same stock which is supposedly protecting the creditor. Further, no one would seek to hold a corporation to its contract of purchase unless the value of the stock was reduced below the agreed purchase price. To enforce compliance with the contract would add nothing to the corporate assets, but would rather reduce the capital, and deprive creditors of funds primarily required for payment of corporate debts.

Reduction of the corporate capital in this manner could result in material injury to the credit of the corporation. Possible creditors might be reluctant to transact any business with a firm, knowing that shares of stock which might become of less, or of no value, have replaced definite assets as the capital stock of the corporation.

In view of the uncertainties and possible losses to which a creditor is subjected by the application of such a rule, it is not difficult to understand why the majority of the states have adopted a contrary doctrine.

DAVID HOROWITZ
GEORGE M. GOOD

It has often been said that assets of a corporation representing its capital stock constitutes a trust fund for the benefit of creditors. Mr. Justice Story first laid down this rule in 1824, (Wood v. Dummer, 3 Mason 308, Fed. Case No. 17, 944) but in that case the decision, “might well have been based, not upon the ground that the capital, stock or the money or property representing the same was in any sense a trust fund for the benefit of creditors, but upon the ground that the distribution of the assets among the stockholders was a fraud upon creditors; and this is true of many other cases in which the trust fund doctrine has been announced. The later cases, not only in most of the state courts, but also in the federal courts have repudiated or limited the theory. It is not true, however, that the capital of a corporation is held just as a natural person holds his property.” BALLENTINE, MANUAL OF CORPORATION LAW AND PRACTICE (1930) 719.

See also, Note (1936-1937) 25 GEorgetown LAW Journal 725.
RECENT DECISIONS

ADMINISTRATIVE LAW—N. L. R. B.—Procedure—Vacating Order

An employer, the Republic Steel Company, petitioned the Circuit Court of Appeals in the Third Circuit for a review of an order issued against it by the National Labor Relations Board. Meanwhile, an opinion of the Supreme Court [Morgan v. United States, 304 U. S. 1 (1938)] was interpreted as casting doubt on certain aspects of the procedure pursued by the Board in making its order, and the Board notified the Circuit Court of Appeals that it wished to vacate its order against the employer and change its procedure so as to remove doubts as to its validity. The Circuit Court, however, issued an order restraining the Board from vacating its order, and compelling it to file a certified transcript of the record of its proceedings against the employer. The Board petitioned the Supreme Court for a writ of mandamus ordering the Circuit Court of Appeals to vacate its injunction against the Board, and for a writ of prohibition against its exercise of jurisdiction over the petition of the employer to set aside the Board's order. Held, under § 10 (d) of the National Labor Relations Act, 49 Stat. 454, 29 U. S. C. §§ 151-166 (Supp. 1935), the Circuit Court of Appeals did not have jurisdiction of the cause until the Board filed with it a certified transcript of the record, and until then the Circuit Court was clearly without power to deny to the Board its right to modify or vacate its order. Since the Circuit Court of Appeals had indicated its willingness to abide by the ruling of the Supreme Court, no writs were issued. In the matter of the N. L. R. B., 58 Sup. Ct. 1001 (1938).

Writs of prohibition and mandamus are not issued against an inferior court unless the court is clearly without jurisdiction. Mere abuses of discretion cannot be remealed by such writs. In Re New York and Porto Rico S. S. Co., 155 U. S. 523 (1895); Ex Parte Oklahoma, 220 U. S. 191 (1911); Ex Parte Chicago, R. I. & P. Ry., 255 U. S. 273 (1921). See also Hughes & Brown, The Writ of Prohibition (1938) 26 Georgetown Law Journal 831. In the instant case, however, the writs prayed for were held to be appropriate in view of the clear absence of jurisdiction on the part of the Circuit Court of Appeals.

The Court held that § 10 (d) of the National Labor Relations Act, supra, in plain terms permits the Board to vacate or modify its orders before it files a transcript of the record with the Circuit Court of Appeals, and the Circuit Court is without power to prevent the Board from doing so. This power of the Board was compared to a like statutory authority permitting a master in chancery to modify or recall his report to a court after submission but before action by the Court, and "no one could successfully claim to be aggrieved in a legal sense by such a statutory provision . . .", and as the Court pointed out, the facts in the instant case clearly show how the employer could not be aggrieved. If the Circuit Court of Appeals had not restrained the Board, the Board would have vacated the order, and there would have been no order to aggrieve the employer. The employer could not in any sense be a "party aggrieved" within the meaning of § 10 (f), which permits an aggrieved party to seek relief in the courts. To allow the Circuit Court of Appeals to take jurisdiction would have given it power to pass upon an order which the Board did not wish to make.

While the opinion of the Court clarified § 10 (d) and § 10 (f) of the Act, an important question concerning § 10 (f) was nevertheless expressly left open. The opinion merely held that the Circuit Court of Appeals had no power to compel the Board to certify a transcript of the proceedings when the Board expressed its
intention to vacate or modify its order. It refused to decide the question as to whether the Circuit Court of Appeals would have jurisdiction under § 10 (f) where the Board merely refuses to certify the transcript without wishing to vacate or modify its order. The practical effect of this question is none the less important. A party aggrieved by an order of the Board can be one against whom an order is directed, or one who sought relief under the Act and was denied it by the Board. The first instance involves an affirmative order of the Board, the second involves a negative order of the Board. Where an affirmative order is issued, no real grievance arises until the Board seeks to enforce it by filing a transcript of the proceedings with the appropriate court, because the Board itself is without power to enforce its order, and no penalty accrues for disobeying it until the final order is enforced by the appropriate court. *Myers v. Bethlehem Shipbuilding Corp.*, 303 U. S. 41 (1938). The parties affected are, therefore, assured a judicial review of the order.

Judicial review of a negative order, that is, where a party is denied relief by the Board, is no less important. In the case of a negative order it would seem that the Board can be compelled under § 10 (f) to certify a transcript of the record with the proper court. To hold otherwise would render the entire § 10 (f) superfluous, a presumption in which one cannot indulge. *United States v. Butler*, 297 U. S. 1 (1936); *United States v. Wright*, 302 U. S. 583 (1938). The section seems to have been inserted into the Act for the very purpose of permitting judicial review of a negative order, since the Supreme Court had previously held that, in the absence of statutory authority, it lacked jurisdiction to review a negative order. *The Proctor & Gamble Co. v. United States*, 225 U. S. 282 (1912). No doubt, in most cases a negative order of the Board will involve only questions of fact, and therefore be not reviewable by a court, § 10 (e), but where questions of law are involved, the right to judicial review would seem to be assured by § 10 (f). However, the question has not been presented to any court.

PHILIP TREIBITCH.

CONFLICT OF LAWS—Divorce—Jurisdiction

On October 29, 1925, petitioner obtained a decree of divorce *a mensa et thoro* in the District of Columbia from respondent on the ground of cruelty. He then moved to Virginia where, after establishing a bona fide domicil, he obtained an absolute divorce on the ground of desertion, process of the Virginia court having been served on the respondent in person in the District of Columbia. Respondent appeared in the Virginia proceeding, filing a plea that she appeared "specially and for no other purpose than to file this plea to the jurisdiction of the court." After obtaining the Virginia decree the petitioner appeared before the District Court of the United States for the District of Columbia and prayed that it modify its decree of October 29, 1925, whereby it had required the petitioner to pay $300 per month to the respondent for her support and for the support of their daughter. The court denied the petition, holding the Virginia decree not entitled to full faith and credit. This was affirmed by the appellate court. *Davis v. Davis*, 61 App. D. C. 48, 57 F. (2d) 414 (1932). Meanwhile the petitioner's daughter married, and he, then conceiving that a change in conditions entitling him to modification of the decree had taken place, filed another petition for such modification based on this ground, again setting out the Virginia decree as a second ground. The court denied the petition holding that it was bound by "the law of the case"
as laid down by the appellate court in its decision on the first petition. The appellate court reversed the case however because of the failure of the trial court to consider the change in conditions occasioned by the marriage of the petitioner's daughter; but it reaffirmed its former decision that the Virginia decree was not entitled to full faith and credit. Davis v. Davis, 96 F. (2d) 512 (App. D. C. 1938). The Supreme Court of the United States granted certiorari, April 25, 1938, 58 Sup. Ct. 944. Held, reversed on the ground that the Virginia decree was entitled to full faith and credit, and must be recognized by the courts of the District of Columbia. Davis v. Davis, 59 Sup. Ct. 3 (1938).

Haddock v. Haddock, 201 U. S. 562 (1906), held that to be entitled to full faith and credit a divorce decree had either to be "granted at the last matrimonial domicil of the parties or, that, the wife be subjected to the jurisdiction of the court either by personal service within the state, or by voluntary appearance and participation in the suit." (italics supplied). The court of appeals recognized this rule as controlling but, according to the view taken by the Supreme Court, incorrectly applied it to the facts of the case, in erroneously assuming that the respondent had not been generally subject to the jurisdiction of the Virginia court.

Although the cases cited in the Supreme Court decision are principally divorce cases, the decision does not appear to be exclusively germane to the divorce field. It has a basis and standing in the broader field of jurisdiction.

Two main points were decided. The first of these was that an appearance entered by a defendant under the designation 'special appearance' made for the sole purpose of challenging jurisdiction, does not prevent the attaching of the court's general jurisdiction unless the conduct of the defendant under that plea was actually limited to the special purpose. The court said, "If the plea alone may not be held to amount to a general appearance, there arises the question whether by her participation in the litigation and acquiescence in the orders of the court relating to merits . . ., she submitted herself to jurisdiction for all purposes. Her plea and conduct are to be considered together," 59 Sup. Ct. 3, 7. The court then detailed facts showing that the respondent had by conduct gone beyond the scope of a special appearance and had submitted generally to the jurisdiction of the court.

The other point decided was that where a defendant appears and litigates the fact of jurisdiction and the fact of jurisdiction is determined adversely to him, that matter is res judicata. In this connection the court said, "As to petitioner's domicil for divorce and his standing to invoke jurisdiction of the Virginia court, its finding that he was a bona fide resident of that state for the required time is binding upon respondent in the courts of the District of Columbia. She may not say that he was not entitled to sue for divorce in the state court, for she appeared there and by plea put in issue his allegation as to domicil, introduced evidence to show it false, took exceptions to the commission's report, and sought to have the court sustain them and uphold her plea. Plainly, the determination of the decree upon that point is effective for all purposes in this litigation." Citing Baldwin v. Traveling Men's Ass'n., 283 U. S. 522 (1931).

It is interesting to observe that this case did not commit the court fully to the doctrine of the Restatement, Conflict of Laws (1934) § 113 as expounded by Professor Beale to the effect that the wrongful act of the one spouse which gives the other the right to obtain a divorce, and gives that spouse the right freely to go elsewhere to establish a domicil without being guilty of desertion also amounts to the granting of a consent by the injured spouse to the jurisdiction of the courts at the injured spouse's new domicil over him or her for purposes of divorce. As a matter of fact it would seem that the discussion of the effect of the alleged special
appearance and the binding effect of the litigation on jurisdictional grounds would have been rendered unnecessary if the court had been prepared to accept in full the doctrine of the Restatement. The same result would have been reached by deciding that since the district court had found Mrs. Davis guilty of cruelty in 1925, her husband freely acquired a new domicil in Virginia and that the 1925 District of Columbia decision precluded her from denying that she had not consented to the jurisdiction of the Virginia court over her interest in the marital res.

C. JONATHAN HAUCK, JR.

CONSTITUTIONAL LAW—Due Process—Price Fixing

Original application for writ of prohibition against a District Judge to restrain the defendant from taking further action in an injunction suit brought by the State Board of Barber Examiners against present plaintiffs. The point at issue is the validity of an Oklahoma Statute which provides for the fixing of minimum prices barbers may charge for their services. OKLA. STAT. ANN. (1937) tit. 59, §§ 91-105. Held, the establishment of minimum prices for barber work bears a reasonable and rational relationship to the preservation of the public health. Herrin et al. v. Arnold, District Judge, reharing denied, 82 P. (2d) 977 (Okl. 1938).

The legislature, here, after prescribing certain standards to be met, sanitary conditions to be maintained, found that the barber trade had been so permeated by unfair trading practices and unfair competition, that it had become impossible for the average barber to maintain reasonably safe and healthful barbering services for the public. As a means, therefore, of securing sanitary conditions in barber shops, § 102 of the Statute provides for the establishment of a State Board of Barber Examiners which “shall fix, by official order, the minimum price for all work usually performed in a barber shop.” In issuing an order, the Board must consider (1) “all conditions affecting the barber profession in its relation to the public health and safety,” and (2) the necessary costs incurred in the particular city or town . . . in maintaining a barber shop in a clean, healthful and sanitary condition.” Also the Board must ascertain that the minimum prices are just, and that they will “best protect the public health and safety by affording a sufficient minimum price . . . to enable the barbers to furnish modern and healthful service and appliances, so as to minimize the danger to public health incident to such work.”

Within the last two years appellate courts of four states have held similar statutes unconstitutional, while in one other state a similar statute has been held valid. While it is not unlikely that the conditions giving rise to this legislation were of the same nature in the several states, it is interesting to note the variety of objectives upon which the various legislatures based this exercise of the police power, and the varying degrees of success in the courts, measured in terms of the stated objectives of the legislation; also the intermixture of thought and precedent relied upon by the courts both in upholding and in striking down this kind of legislation.

An Iowa statute provided for municipal minimum price fixing for barber services for the purpose of preventing widespread unemployment and economic distress. In declaring the statute invalid as an undue restriction of freedom of contract under the due process clause of the 14th Amendment, Duncan v. City of Des Moines, 222 Iowa 218, 268 N. W. 547 (1936), the court relied upon Adkins v. Children’s Hospital, 261 U. S. 525 (1923), which invalidated an act of Congress fixing minimum wages for women in the District of Columbia, and also on decisions invalidat-
ing statutes fixing prices for industries not "affected with a public interest." Williams v. Standard Oil Co., 278 U. S. 235 (1929); Tyson v. Banton, 273 U. S. 418 (1927); also Wolff Packing Co. v. Court of Industrial Relations, 262 U. S. 522 (1923); and other cases. A similar ordinance in Alabama, passed under authority of a statute designed also to prevent widespread unemployment and economic distress, was held invalid on the ground that the question presented "has been set at rest" by the Adkins case; Wolff Packing Co. v. Court of Public Relations, supra; Williams v. Standard Oil Co., supra, and others. In deciding that the barber trade is not affected with a public interest sufficient to justify the fixing of minimum prices, however, the court commented that the fact that no legislature in Alabama has ever attempted to exercise this power, is a "persuasive argument that the power has never existed." City of Mobile v. Rouse, 233 Ala. 622, 173 So. 266, 267 (1937). In a Florida price fixing statute, the legislature found that unfair competition made it impossible for an average barber to support and maintain a family, and the main objective of the statute was to protect the health and well-being of the barbers and their families. While upon the phase of constitutionality under discussion, the court was evenly divided, the statute was held unconstitutional on the ground that under the terms of the statute, there could be no flexibility in the prices fixed, to reflect the varying costs of operation in the different cities and towns. Reliance was placed on the Adkins case, and the court distinguished the barber trade specifically from the milk industry, which, in Nebbia v. New York, 291 U. S. 502 (1934), was held to be closely connected with the public welfare. State v. Ives, 123 Fla. 401, 167 So. 394 (1936). In California, a city ordinance, enacted under a statute "to promote the general welfare," and not concerning itself with health or safety, was invalidated principally for the reason that the ordinance would help only 2% of the people and therefore did not constitute legislation "for the general welfare." The court distinguished the facts from West Coast Hotel Co. v. Parrish, 300 U. S. 379 (1937) (which had specifically overruled the Adkins case), on the ground that the West Coast case constituted "legislation for the general welfare of the race as well as for the good of a large proportion of our population." Ex Parte Kasas, 22 Cal. App. 161, 70 P. (2d) 962, 968 (1937).

In March, 1938, a Louisiana statute practically identical with the instant statute was declared invalid by the Supreme Court of that state, but on rehearing the statute was upheld. Chief reliance was placed on the Nebbia case, and, on the basis of Justice Roberts' statement in the majority opinion that "there is no closed class or category of business affected with a public interest," it was declared that "the operation of a barber shop is a business affecting the public health, safety, and welfare." Board of Barber Examiners v. Parker, 190 La. 214, 182 So. 485 (1938). In the instant case, the court cites the declaration by the legislature that there exists a relationship between prices and sanitary and health requirements, and quotes with approval the words of Mr. Justice Holmes, speaking of the labor regulation discussed in Lochner v. New York, 198 U. S. 45, 76 (1905) "A reasonable man might think it a proper measure on the score of health."

Thus it is that six state statutes providing for the establishment of minimum prices for barber services have recently been tested in appellate courts of the several states. Two of these statutes, in which the ultimate objective was the prevention of unemployment and economic distress, were held invalid; two, providing mainly for the health and sustenance of barbers and their families, were also held invalid; and two, providing for the preservation of the public health, and containing specific legislative findings appropriate to that objective were held valid.
But the question remains, referring to the precedents upon which all of these cases were decided, as to whether, with respect to constitutional restraints, there is any real distinction between price fixing statutes for particular service trades and minimum wage statutes of general application, i.e. whether there is a distinction in the fixing of prices for services as between employee and employer, and as between employer and the public. In the six cases discussed each of the appellate courts have placed some, and in certain of the cases, principal reliance upon decisions of the Supreme Court affecting the validity of minimum wage statutes, i.e., the Adkins case, and the West Coast Hotel case. Both in price-fixing and minimum wage statutes the source of the power invoked is the same, the police power; and in all, the constitutional limitation is the same, the due process clause of the 14th Amendment; and finally in all, the controversy has concerned the essence of the contract, the contract price.

The instant decision cites the West Coast Hotel case, as undermining the authority of three of the above four decisions invalidating price-fixing statutes, and points out that "with increasing economic complexities . . . it became evident that old guideposts must be repainted or their direction changed." And the question is asked, "How far in the new direction may we go before encountering the barriers of the Federal Constitution?"

Perhaps the most definitive answer to this question, if indeed there is occasion for the question, may be found in the dissenting words of Mr. Justice Brandeis, quoted with approval in the instant decision, "In my opinion, the true principle is that the State's power extends to every regulation of any business reasonably required and appropriate for the public protection." New State Ice Co. v. Liebmann, 285 U. S. 262, 302 (1932).

WILLIAM H. EDMONDS.

CONSTITUTIONAL LAW—Religious Liberty

Defendant School Board passed a regulation requiring pupils to salute the American Flag as a part of daily exercises in public schools, and providing that refusal so to do would be regarded as insubordination and dealt with accordingly. Plaintiffs, two minor children and their father, belonged to a religious body known as Jehovah's Witnesses and, following the tenets of that cult, sincerely and honestly were opposed to flag saluting on the ground that such action was a direct violation of the divine commandments. Acting on this conviction the minor plaintiffs refused to salute the flag and were dismissed from school. This action was brought to enjoin the School Board and its individual members from prohibiting the attendance of the minor plaintiffs at the public school because of their refusal to comply with the above regulation. Held, (1) the liberty guaranteed by the Fourteenth Amendment includes freedom in the exercise of religion; (2) the religious liberty thus guaranteed cannot be interfered with by the State except in connection with the police power purposes; (3) each individual may determine for himself the validity of his own religious beliefs. Gobitis v. Minersville School Dist., 24 F. Supp. 271 (E. D. Pa. 1938).

The first two grounds on which the decision is based are amply supported by authority. Myer v. Nebraska, 262 U. S. 390 (1923); Pierce v. Society of Sisters, 268 U. S. 510 (1925); Stromberg v. California, 283 U. S. 359 (1931); Near v. Minnesota, 283 U. S. 697 (1931); Hamilton v. Regents, 293 U. S. 245 (1934). The third contention, however, that neither judge nor other public official may decide for
the individual whether his particular belief and the action taken thereon may be classified as religious, is highly controversial.

The court bluntly asserted that the fundamental concept of religious liberty embraces the right of each man to decide for himself what is to him religious. No authority directly in point was cited, but rather the truth of the proposition was held to be an obvious and necessary deduction from the concept itself. In one of the land-mark cases on religious liberty, which held that a party's religious belief cannot be accepted as a justification for his committing an overt act, made criminal by the law of the land, the Supreme Court cited with approval and called particular attention to Thomas Jefferson's preamble to the early Virginia Act "For Establishing Religious Freedom" (12 HENING'S STAT. 84) in which he said: "... to suffer the civil magistrate to intrude his powers into the field of opinion, and to restrain the profession or propagation of principles on supposition of their ill tendency, is a dangerous fallacy which at once destroys all religious liberty, ... it is time enough for the rightful purposes of civil government for its officers to interfere when principles break out into overt acts against peace and good order". Reynolds v. United States, 98 U. S. 145, 163 (1878). See Meyer v. Nebraska, supra, at 399; Hamilton v. Regents, supra, at 262. It does not seem to be too broad an extension of Jefferson's idea to hold that even in restraining acts inimical to public interest the public officer shall deal with the acts alone and leave the belief from which they spring to the undisturbed custody of the offender.

This proposition, however obvious, has often either been ignored or inferentially disputed by many other decisions where the point was in issue. Mormon Church v. United States, 136 U. S. 1 (1890); New v. United States, 245 Fed. 710 (C. C. A. 9th, 1917), cert. denied 246 U. S. 665 (1918); Shapiro v. Lyle, 30 F. (2d) 971 (W. D. Wash. 1929); Smith v. People, 51 Colo. 270, 117 Pac. 612 (1911); McMasters v. State, 21 Okla. Cr. 318, 207 Pac. 566 (1922). In upholding an Idaho statute refusing bigamists the right to vote, the Supreme Court said "bigamy and polygamy are crimes by the laws of all civilized and Christian countries. ... To call their advocacy a tenet of religion is to offend the common sense of mankind". Davis v. Beason, 133 U. S. 333, 341 (1890). In refusing naturalization to a conscientious objector against war, the Supreme Court pointed out that he could not make his own interpretation of the will of God the decisive test, and instead substituted what it conceived to be the interpretation of the will of God a Christian Nation, which the United States was held to be. United States v. Maclntosh, 283 U. S. 605 (1931).

Three recent cases involving Jehovah's Witnesses and their objection to flag saluting and pledging allegiance which ran afoul of state statutes hold exactly contrary to the instant case. "The flag salute and pledge of allegiance herein in question do not in any just sense relate to religion. ... They are wholly patriotic in design and purpose." Nicholls v. Mayor and School Committee of Lynn, 7 N. E. (2d) 577, 580 (Mass. 1937), 110 A. L. R. 377. "The act of saluting a flag is by no stretch of reasonable imagination a religious rite." Leoles v. Landers, 192 S. E. 218, 222 (Ga. 1937). "A pledge of allegiance is by no means a religious rite. It is a patriotic ceremony. ..." John Hering v. State Board of Education, 117 N. J. L. 455, 456 (1937), aff'd., 118 N. J. L. 566 (1937). Typically enough, the Gobitis case and the three opposite holdings all cite Hamilton v. Regents, supra, for support. It is interesting to note in that case, however, that while the opinion of the court holds that conscientious objection to bearing arms is a valid religious objection, which must however be superseded by the State's paramount right to protection from aggression, the concurring opinion of Mr. Justice Cardozo, joined in by
Justices Brandeis and Stone, goes further and conveys the idea that the validity of religious beliefs must be weighed in the light of history and the concensus of the opinion of mankind.

Though in final analysis it may be just a matter of judicial technique, since the same result can be reached either by holding that the act in question is not religious in character and therefore does not come within the constitutional guarantee, or letting the individual himself decide as to its religious validity and holding that the State's police power is paramount thereto when exercised in its proper field, still much may be said for using the proper means to reach correct conclusions. Furthermore, it seems that the view taken by the court in the Gobitis case is more adapted to American viewpoint and tradition. In countries where opinion is definitely moulded into well defined channels, whether through unanimity of belief, tradition or governmental bludgeoning, it is perhaps more expedient to have hard and fast rules as to what is or what is not religious. Under our form of government, however, where independence of thought and opinion is of the essense of freedom, it may be more desirable to let the individual have the satisfaction of deciding this personal question for himself.

JAMES H. HYNES.

CONTRACTS—Infancy—Disaffirmance—Accountability for Consideration

Plaintiff, an infant twenty years old, entered into a contract under which he received instruction in aviation for which he paid $1,600. One year after attaining his majority, he brought this action to recover the sum he had paid, with interest, disaffirming his contract. The defendant maintained that, as the plaintiff could not return the consideration, he could not disaffirm the contract. Held, plaintiff may disaffirm and recover. Adamowski v. Curtiss-Wright Flying Service, Inc., 15 N. E. (2d) 467 (Mass. 1938).

The defendant's contention suggests a problem the solution of which has produced an appalling conflict in the decisions of the courts in this country. The prevailing rule is that the infant need restore only so much of the consideration as he has in his possession at the time of disaffirmance. Shutter v. Fudge, 108 Conn. 528, 143 Atl. 896 (1928). This rule recognizes the policy of the law in protecting the incautious and unwary infant who has wasted the effects of his contract. It accomplishes a just end by preventing the sophisticated infant from retaining the property received (in tangible form) and recovering the consideration paid therefor. More often, however, the doctrine works a gross injustice. To twist a figure of speech from Chancellor Kent, 2 Kent, Comm.* 240, it supplies the infant with a sword for his aggression rather than a shield for his protection. The rule fails to comprehend cases like the present in which the consideration is of an intangible nature, and consequently incapable of actual restoration. So the courts have indulged in the inept analogy to cases in which the infant lost, consumed, or squandered the subject-matter of his voidable contract. The fallacy of this method is more real than apparent. It permits the infant to reap substantial benefit and then deprive his benefactor of a due reward. Such a rule is contrary to natural justice, and should not be tolerated in the law.

In a minority of jurisdictions, rules have been adopted which succeed substantially in protecting the infant, yet securing the adult against fraudulent and corrupt practices. In Petit v. Liston, 97 Ore. 464, 191 Pac. 660 (1920), the plaintiff was refused the right to recover money paid without allowing the vendor a reasonable
compensation for the use and depreciation of the article while in his hands. Such is the law in *Rice Auto Co. v. Spillman*, 51 App. D. C. 378, 280 Fed. 452 (App. D. C. 1922). New Hampshire has the comprehensive rule that a person seeking to avoid an executed contract on the ground of infancy must account for what he has received under it, by restoring or paying the value of whatever remains in specie within his control, and allowing for the benefit derived from whatever cannot be restored. *Hall v. Butterfield*, 59 N. H. 354 (1879). Minnesota has adopted, in a case more in point than any suggested in the instant case, a policy similar to the one in New Hampshire. In *Johnson v. Northwestern Mutual Life Insurance Co.*, 56 Minn. 365, 378, 59 N. W. 992, 994 (1894), the court said: “Where the personal contract of an infant is fair and reasonable, and free from any fraud, over-reaching, or undue influence by the other party, and has been wholly or partly executed on both sides, so that the infant has enjoyed the benefits of it, but has parted with what he received, or the benefits are such that he cannot restore them, he cannot recover back what he has paid.” This was affirmed in *Berglund v. American Multigraph Sales Co.*, 135 Minn. 67, 160 N. W. 191 (1916).

These cases evince a tendency to increase the liabilities of the infant under his contracts. Whether or not the courts, in their effort to afford him protection against the improvidence of his kind and yet allow a minimum of injustice to be suffered, will go as far as the English courts in denying altogether the infant's right of disaffirmance when he cannot restore the consideration, is a matter purely of public policy. *Valentini v. Canali*, 24 Q. B. D. 166 (1889). It would seem that a universal adoption of the “benefit” rule of New Hampshire and Minnesota would, as Williston says, “prevent imposition upon the infant and also tend to prevent the infant from imposing to any serious degree upon others.” 1 WILLISTON, CONTRACTS (Rev. ed.) § 238.

JOSEPH W. KIERNAN.

CRIMINAL LAW—Lotteries—Bank Night

Demurrer to an information charging the operation of a lottery and setting out the following: Money was distributed by chance at the defendant theatre among persons holding coupons obtained either by purchasing a ticket to the theatre or free upon request without purchasing a ticket. The free participation was advertised. The holder of the winning coupon received the prize if he presented himself within five minutes after the announcement of the winner, which was made both in and outside of the theatre, and was admitted free to claim the prize if outside. *Held*, the information alleged facts from which a jury could find a valuable consideration paid by those who occupied the theatre for the chance to win the prize, and that the alleged fact that those who requested a chance obtained it free could be found by the jury a mere device to evade or circumvent the law. *State v. Schubert Theatre Players Co.*, 281 N. W. 369 (Minn. 1938).

Minn. Stat. (Mason, 1927) § 10209 defines a lottery as “a scheme for the distribution of property by chance, among persons who have paid or agreed to pay a valuable consideration for the chance”. This coincides with the standard definition of a lottery as it includes the three essentials: 1) a prize, 2) distribution by chance, and 3) consideration for the chance.

Under this definition, if it is necessary for each participant to purchase merchandise or pay for entertainment, the consideration is found in such payment although no additional payment is made for the chance.
The particular scheme in question is a form of the well-known "Bank Night", which attempts to avoid or evade the lottery laws by making participation equally open to those who do and those who do not purchase admission to the theatre and publicizing this fact. In spite of its newness, the adoption of this scheme has been so widespread that its legality has been questioned in reported cases from some nineteen states. In most of the cases the critical issue is whether the element of consideration exists to bring the operations within the laws prohibiting lotteries.

The prevailing view, where the enterprise is carried out as stated above, is that it is not a lottery. Since those who pay nothing have as good a chance to win as those who attend the show, it cannot be seen that those who attend pay for anything but entertainment, and therefore no consideration is received from any participant. *State v. Hundleby*, 220 Iowa 1369, 264 N. W. 608 (1936). According to this line of cases, additional revenue which the promoter receives from increased attendance is a motive for offering a prize, not a consideration for doing so, and the formalities of registration or asking for a free coupon and the act of waiting outside the theatre in order to receive the prize if one's number be drawn do not constitute valuable consideration. *Commonwealth v. Wall*, 3 N. E. (2d) 28 (Mass. 1936); *Briggs v. Miller*, 176 Wis. 321, 186 N. W. 163 (1932). This view was set out in a dissent in the principal case.

Decisions unfavorable to the legality of "Bank Night" schemes are slightly in the majority, but most are distinguishable from the principal case. Thus *State ex rel. Beck, Atty. Gen. v. Fox Kansas Theatre Co.*, 144 Kan. 687, 62 P. (2d) 929 (1936) and *State v. Dorau*, 124 Conn. 160, 198 Atl. 573 (1938) depend upon broad definitions of lotteries and related offenses in the state laws.

Other cases find that the free tickets were not widely advertised, and amounted to a mere subterfuge, as in *Wink v. Griffith Amusement Co.*, 100 S. W. (2d) 695 (Tex. 1936). In several cases it was found as a matter of fact that the time allowed within which the prize had to be claimed was so short that those who paid for admission had, or had reason to believe they had, a real advantage, for which consideration was found in the admission price. *Iris Amusement Corp. v. Kelly*, 366 Ill. 256, 8 N. E. (2d) 648 (1937).

There remain, however, several cases which clearly furnish precedent for the principal case, such as *State v. Danz*, 140 Wash. 546, 250 Pac. 37 (1926), and *Grimes v. State*, 235 Ala. 192, 178 So. 73 (1937). These opinions reason that the schemes are operated for a profit which comes from those who do purchase tickets, and this is sufficient consideration. As stated in the principal case "the moment some pay for the chance of participating in the drawing of the prize, it is a lottery under the law, no matter how many receive a chance to also participate free'.

It is submitted that the reasoning supporting this line of cases is not convincing, and one may well wonder if they would have been decided as they were but for a feeling on the part of the courts that the scheme involved is substantially the same as a lottery and just as undesirable. One can hardly quarrel with this view, but it would seem most proper for it to find expression through legislative action.

PAUL FITZPATRICK.

**EQUITY—Enjoining of Criminal Statutes**

Suit by Watch Tower Bible & Tract Society and individual members of the society before a statutory three-judge court against the City of Bristol and certain officials of the city for an injunction restraining defendants from enforcing or
otherwise proceeding against complainants to enforce a Connecticut Statute which provided a fine or imprisonment for persons who "shall write or print and publicly exhibit, post up or advertise, any offensive, indecent or abusive matter concerning any person." Conn. Gen. Stat. (1930) § 6194. Some of the individual complainants had been convicted for breach of the statute but no allegation was made that further or immediate prosecution was threatened. Held, no basis for equitable relief being established, the bill is dismissed. Watch Tower Bible & Tract Society v. City of Bristol, 24 F. Supp. 57 (D. Conn. 1938).

Section 266 of the Judicial Code, 36 Stat. 539, 557 (1910), 28 U. S. C. § 380 (1934), provides for a three-judge court with jurisdiction to consider suits to restrain, on constitutional grounds, the enforcement of a state statute by an officer of the state. On the application for interlocutory injunction the special court is not called upon to decide the merits of the case. McNaughton v. Johnson, 242 U. S. 344 (1917); Pacific Telephone & Telegraph Co. v. Cushman, 292 Fed. 930 (C. C. A. 9th, 1923), cert. denied, 263 U. S. 729 (1924). The court was, therefore, not concerned with whether the complainants had been properly convicted or whether the statute had been misapplied or misconstrued.

On authority of Spielman Motor Sales Co. v. Dodge, 295 U. S. 89 (1935), the court grounded its jurisdiction in a suit against city officials. The Spielman case held that where a statute embodies a policy of statewide concern, an officer, although chosen in a political subdivision, and acting within that limited territory, may be charged with the duty of enforcing the statute in the interest of the state and not simply in the interest of the locality in which he serves.

The court likewise had no great problem in deciding that the complainants had not established a right to equitable relief for it is a general principle of equity not to interfere to prevent the enforcement of a criminal statute, even though unconstitutional. In re Sawyer, 124 U. S. 200 (1888); Davis and Parnum Mfg. Co. v. Los Angeles, 189 U. S. 207 (1903); Hygrade Provision Co. v. Sherman, 266 U. S. 497 (1925).

The reason for the rule, that there is an adequate remedy at law to relieve the complainant, is stated by the Supreme Court in Fenner v. Boykin, 271 U. S. 240, 244 (1926): "The accused should first set up and rely upon his defense in the state courts, even though this involves a challenge of the validity of some statute, unless it plainly appears that this course would not afford adequate protection. The Judicial Code provides ample opportunity for ultimate review here in respect of Federal questions."

To justify equity's interference exceptional circumstances are needed and there must be a clear showing that the injunction is necessary to adequately protect constitutional rights. Terrace v. Thompson, 263 U. S. 197 (1923); Packard v. Banton, 264 U. S. 140 (1924); Tyson v. Banton, 273 U. S. 418 (1927); Cline v. Frink Dairy Co., 274 U. S. 445 (1927). Unless it is essential to safeguard rights of property and the danger of irreparable injury is great and immediate, the injunction will not be granted to restrain a criminal proceeding. Campbell v. Medalie, 71 F. (2d) 671 (C. C. A. 2d, 1934), cert. denied, 293 U. S. 592 (1934). But the injunction will issue to restrain the invasion of property rights by enforcement of an unconstitutional law, even if the effect is to restrain the institution or continuation of a criminal prosecution, Cline v. Frink Dairy Co., supra; State ex rel. Fry v. Superior Court of Lake County, 205 Ind. 355, 186 N. E. 310 (1933). The general rule against enjoining criminal prosecution is not changed by threats of arrest or of repeated arrest. Douglas v. South Georgia Grocery Co., 178 Ga. 657, 174 S. E. 127 (1934). The present case did not contain allegations that defendants threatened further or immediate prosecution of complainants.
The court thus followed the weight of many precedents in denying its relief to complainants on general equity principles. Complainants' contention that the statute abridges the constitutionally guaranteed rights of freedom of speech was not dignified by a reply by the court other than by the assertion that general police powers remained in the states and the statute here considered was not invalid on its face. Let it be observed that the holding in this case is not a retrenchment from the stand of the Supreme Court on civil liberties as set forth by *Near v. Minnesota*, 283 U. S. 697 (1931) and *Lovell v. Griffin*, 303 U. S. 444 (1938), for in those cases there was prior restraint on freedom of the press and of speech. The statute here under consideration did not create a prior restraint.

SIDNEY W. GOLDSTEIN.

INJUNCTION—Relief Against Taxation

The Regents of the University System of Georgia sought an injunction restraining the collection, by distraint, of a federal admissions tax in respect of athletic contests, in which the teams representing the University of Georgia and Georgia School of Technology participate, on the ground that the tax unconstitutionally burdens a governmental function of the State of Georgia. The petition challenged the Regents' ability to maintain a suit to enjoin the collection of the tax, on the strength of *Rev. Stat. § 3224* (1867), 26 U. S. C. § 1543 (1934) which provides: "No suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court". . . Held, the circumstances of the case, involving the question of whether the tax is an unconstitutional burden on a governmental function of the state, rendered the case one of equitable jurisdiction and took it out of the prohibition of the Statute. *Allen v. Regents of the University System of Georgia*, 304 U. S. 439 (1938).

This case forges another link in the chain of exceptions which have been made to the seemingly categorical prohibition of *Rev. Stat. § 3224* (1867), 26 U. S. C. § 1543 (1934). This statute was found constitutional in *Pullan v. Kissinger*, 2 Abb. 94, 20 Fed. Cas. No. 11, 463 (S. D. Ohio 1870). Despite the language of the Statute it has been found that its provisions are general enough to allow exceptions to be made to it. It does not apply to the maintenance by the stockholder of a corporation of a suit to restrain the corporation from voluntarily paying a tax claimed to be unconstitutional, if the constitutionality of such tax has not been decided. *Pollock v. Farmers' Loan and Trust Co.*, 157 U. S. 429 (1895); *Brushaber v. Union Pacific R. R.*, 240 U. S. 1 (1915). Then, in *Dodge v. Osborn*, 240 U. S. 118, 122 (1916), Chief Justice White intimated that such injunctive relief might be afforded where "... by some extraordinary and entirely exceptional circumstances its provisions are made inapplicable", although, in this particular case the injunction was denied. This view requires that, to give the court jurisdiction to grant this injunction, something more is necessary than the old equity rule demanded, viz., that there be no adequate remedy at law and irreparable damage. Substantially the same is *Dodge v. Brady*, 240 U. S. 122 (1916). This view was foreshadowed as early as 1878 in *Frayser v. Russell*, 9 Fed. Cas. No. 5067 (E. D. Va. 1878) and in *Kissinger v. Bean*, 14 Fed. Cas. No. 7853 (E. D. Wis. 1875), wherein it was held that the injunction would be granted where the collector's actions were so capricious that the imposition was a nullity. Note (1935) 49 Harv. L. Rev. 109. In *Lipke v. Lederer*, 259 U. S. 557 (1922) and *Regal Drug Co. v. Wardell*, 260 U. S. 386 (1922), which arose under the National Prohibition
Act, second situation was presented, in which an attempt to enforce penalties for violations of that act was held not to be covered by Rev. Stat. § 3224 (1867), 26 U. S. C. § 1543 (1934), since what was being collected was not a tax at all, but a penalty. Note (1935) 49 Harv. L. Rev. 109. *Hill v. Wallace*, 259 U. S. 44 (1922), was held to present a situation of "extraordinary and entirely exceptional circumstances" within the rule of *Dodge v. Osborn*, supra, and injunctive relief issued.

This march of exceptions was slowed up by *Graham v. Dupont*, 262 U. S. 234 (1923), in which the injunction was refused, the court retreating from the ground taken by *Hill v. Wallace*, supra, which it distinguished as involving a penalty rather than a tax, thus placing *Hill v. Wallace*, supra, with *Lipke v. Lederer*, supra. Note (1935) 49 Harv. L. Rev. 109. A hint at realignment with the forces of *Dodge v. Osborn*, supra, was made in *Bailey v. George*, 259 U. S. 16 (1922). But the storming of the walls of Rev. Stat. § 3224, 26 U. S. C. § 1543 (1934) was resumed in *Miller v. Standard Nut Margarine Co.*, 284 U. S. 498, 509 (1932). The Supreme Court, while adhering to the doctrine of extraordinary and exceptional circumstances, held that all that was required to remove a case from the operation of Rev. Stat. § 3224, 26 U. S. C. § 1543 (1934) was the presence of the requirements of the old equity rule. Mr. Justice Butler said: "Where, in addition to the illegality of exactation, in the guise of a tax, there are special and extraordinary circumstances sufficient to bring the case within some acknowledged head of equity jurisprudence, a suit may be maintained to enjoin the collector". Mr. Justice Stone registered a strong dissent, with Justices Cardozo and Brandeis concurring. In *Rickert Rice Mills v. Fontenot*, 297 U. S. 110, the Supreme Court, without stating any opinion, seems to follow the *Miller case*.

The instant case follows *Miller v. Standard Nut Margarine Co.*, supra, without indicating clearly what exceptional circumstances bring the case within that doctrine. Mr. Justice Roberts, in rendering the majority opinion, seems to indicate that the mere allegation of unconstitutionality by reason of being an unconstitutional burden on the governmental function of the State of Georgia (which suggestion was repudiated on its merits) is enough. Further on, however, he suggests that the position of the University, as a mere collecting agent for the Federal Government, rendered its chance of securing a refund of the tax so uncertain as to present sufficiently exceptional circumstances. Mr. Justice Reed concurred on the merits of the question of immunity from the tax, but differed from the majority in viewing the suit as barred by Rev. Stat. § 3224 (1867), 26 U. S. C. § 1543 (1934). In this view Mr. Justice Black concurred, as did Mr. Justice Stone, who, in a special concurrence, said: "... while I agree with the decision of the Court on the merits, I am not persuaded that this statute does not mean what it says, or that the suit is not one to restrain the collection of the tax. I can only conclude, as I did in *Miller v. Standard Nut Margarine Co.*, supra, that the statute deprived the district court of jurisdiction".

PETER J. BRENNAN, JR.

MONOPOLIES—Undue Restraint of Trade—Prevention of Double Feature Shows

The plaintiffs were the owners of two theatres, unaffiliated with a major producer. In order to compete with other local theatres it was necessary for them to show the so-called better class of motion pictures. For the purpose of securing a supply of these first grade pictures from the defendants, who were exclusive distributors, the plaintiffs were compelled to enter into contracts the contents
of which, as dictated by the defendants, contained a restrictive clause preventing
the plaintiffs from showing a double feature. This tended to reduce the feature
pictures purchased by the plaintiffs.

Suit was brought by the plaintiffs to have this particular clause in the contracts
declared illegal as a violation of the anti-trust laws and to enjoin the defendants
from further use of it. Under Section 16 of the Clayton Act, 38 STAT. 731 (1914),
15 U. S. C. § 16 (1934), individuals were authorized to bring suits in equity to
restrain violation of the anti-trust laws; prior to this time under the Sherman Act,
26 STAT. 209 (1890), 15 U. S. C. §§ 4, 5 (1934), only the Government could bring
such a suit. Held, the restrictive clause in question was in violation of the anti-trust
laws and plaintiffs were entitled to an injunction. Vitagraph, Inc. v. Perelman, 95 F.
(2d) 142 (C. C. A. 3d 1938).

There are generally three phases in the growth of the interpretation of the
statutes regarding the control of monopolies and monopolistic tendencies by means
of the Sherman Anti-Trust and the Clayton Acts. The first phase covers that period
of time from the passage of the Sherman Act in 1890 until about 1911. During
this period of time the law was construed strictly. All contracts or combinations
in restraint of trade (it did not matter whether or not they were reasonable or
unreasonable, or for the good of the particular business or industry) were held
to be a violation of the anti-trust laws. United States v. Trans-Missouri Freight
Association, 166 U. S. 290 (1897); United States v. Joint Traffic Association, 171
U. S. 505 (1898).

The second phase of this monopoly control was inaugurated by the "rule of
reason." In this instance the courts appreciated changing conditions and the rapid
expansion of industry and broadened their interpretation of the anti-trust laws
considerably. That is, a combination, even though somewhat in restraint of trade,
if reasonable, was not considered a violation of the acts. United States v. American
Tobacco Co., 221 U. S. 106 (1911).

In the leading case on this point, Standard Oil v. United States, 221 U. S. 160
(1910), Mr. Chief Justice White summed up the new outlook in the anti-trust
laws as follows, "... it was intended that the standard of reason which has been
applied at the common law and in this country in dealing with subjects of the
character embraced by the statute, was intended to be the measure used for the
purpose of determining whether in a given case a particular act had or had not
brought about the wrong against which the statute provided."

The third phase of the development of these anti-trust laws is of most interest
to us as it is more or less in a malleable state. The restrictions of the act are
not artificial or mechanical. The court says in Nash v. United States, 229 U. S.
373, 376 (1913), "that only such contracts and combinations are within the act
as, by reason of intent or the inherent nature of the contemplated acts, prejudice
the public interests by unduly restricting competition or unduly obstructing the
course of trade." See Standard Oil Co. v. United States, supra; United States v.
American Tobacco Co., supra; Chicago Board of Trade v. United States, 246 U. S.
231, 238 (1918); Window Glass Manufacturers v. United States, 263 U. S. 403, 412
(1923); Paramount Famous Lasky Corp. v. United States, 282 U. S. 30, 43 (1930);

Today, therefore, in looking for a test, the courts have come to look beyond
the statute and consider the industries objectively. After all, every agreement
between business men to combine tends to restrain free competition. Chicago
Board of Trade v. United States, supra. Carrying this new interpretation of the
anti-trust laws to its final point, the broad social and economic conditions are given
weight by the law. Distinction is made between monopoly in a district or area
and a complete monopoly which controls the entire market. In the former
instance even though there is a monopoly, and consequent restraint of trade, if
it can be shown that the leaders of the various businesses have furnished data
and facts, that lead to the belief that the combination is for the "good of the
industry", then the law holds such combination not to be in violation of the anti-

CHESTER HAMMOND.

TRADE MARKS—Infringement—Laches

In a cancellation proceeding filed in 1935 it was contended that the trade-
mark "Klad-ezee", which name was registered in 1928, was confusingly similar
to appellant's trade-mark "E-Z" which had been used by it and its predecessor since
1895, and which mark had been duly registered in the Patent Office long prior
to adoption and use of the mark "Klad-Ezee". The appellee denied confusing
similarity of the trade-marks, and alleged estoppel of appellant to bring this pro-
ceeding by reason of laches. *Held*, that if the marks of the parties were to be tested
by appearance alone they would not be confusingly similar, but when tested by
sound they would; and that mere laches may not be invoked against a petitioner in
a cancellation proceeding. *E-Z Mills, Inc. v. Martin Bros Co.*, 95 F. (2d) 269 (C.
C. P. A., 1938).

Trade-marks "... which so nearly resemble a registered or known trade-mark
owned and in use by another, and appropriated to merchandise of the same
descriptive properties, as to be likely to cause confusion or mistake in the mind
of the public, or to deceive purchasers, shall not be registered." 33 STAT. 725 (1905),
confusing similarity between trade-marks. *McKinnon & Co. v. HyVis Oils, Inc.,
24 C. C. P. A. (Patents) 1105, 88 F. (2d) 699 (1937); Chuett, Peabody & Co., Inc.,
v. Wright, 18 C. C. P. A. (Patents) 937, 46 F. (2d) 711 (1931). Since radio is an
important medium for advertising, sound is a necessary factor in considering the
question of confusing similarity in trade-marks. See *In re Dutch Maid Ice Cream

In disposing of appellee's defense of laches on account of appellant's seven-
year delay in bringing this proceeding, the court relied solely on the authority
of *Chuett, Peabody & Co., Inc. v. Hartogensis (Arrow Emblem Co., Inc., Substituted),
17 C. C. P. A. (Patents) 1166, 41 F. (2d) 94 (1930). In that case it was held
that the proper interpretation to be given to the phrase "at any time" in § 13 of
the Trade-Mark Act of 1905, 33 STAT. 728 (1905), 15 U. S. C. 93 (1934), where-
in it is provided "... whenever any person shall deem himself injured by the
registration of a trade-mark in the Patent Office he may at any time apply to the
Commissioner of Patents to cancel the registration thereof," should be that mere
laches could not be used as a defense in a proceeding under said section. This
holding was qualified by the statement "We think it appropriate to say in this
connection that this opinion should not be construed as implying that affirmative
acts of a prior owner and user of a trade-mark, relied upon by a registrant
to his injury, would not be a bar to the right of cancellation in a proceeding under
said § 13." *Id.* at 1172. The court then cited the cases of *McLean v. Fleming,
96 U. S. 245 (1877); Menendez v. Holt, 128 U. S. 514 (1888); and *Saxlehner v.
Eisner & Mendelson Co., 179 U. S. 19 (1900), in support of its contention. All these cases were decided prior to the Trade-Mark Act of 1905, supra.

Another authority cited in the Hartogensis case was Hanover Star Milling Co. v. Metcalf, 240 U. S. 403 (1915), which was decided long after the enactment of the Trade-Mark Act of 1905, supra. The passage of this case quoted in the Hartogensis case approving the cases decided prior to the Act, was merely dictum, however. This case actually decided that where a later user of a trade-mark in good faith and without notice of its use in another territory by an earlier user spends money and effort for good-will and in building up trade in a territory not entered by the earlier user until long afterwards, the earlier user is estopped from asserting infringement because, inferentially, of laches. Both the product used and the trade-mark were identical in the Hanover case.

Another case in which the doctrine of laches as laid down in the Hartogensis case was approved was Cluett, Peabody & Co., Inc. v. Wright, supra. The Commissioner of Patents had found that the appellant's right to extend its trade-mark "arrow" to bathing belts was lost by laches since the appellant had practically acquiesced to the exclusive use of the trade-mark "Air-O" on bathing belts from 1915 to 1926. The Commissioner cited France Milling Co., Inc. v. Washburn-Crosby Co., Inc., 7 F. (2d) 304 (C. C. A. 2d, 1925), and Victor Stove Co. v. Hall-Neal Furnace Co., 58 App. D. C. 65, 24 F. (2d) 893 (1928). The decision of the Commissioner was reversed, however, by the Court of Customs and Patent Appeals in spite of the fact that the appellant had not manufactured or sold bathing belts until eleven years after the appellee had been engaged in this business, and in spite of the fact that the only similarity the Court could find in the two trade-marks was in sound alone, which similarity it said was confusing. The Court distinguished the case at bar from the France Milling Co. case, but peculiarly enough omitted to comment on the Victor Stove Co. case.

The Victor Stove Co. case was decided in the Court of Appeals for the District of Columbia, which Court had appellate jurisdiction from decisions of the Commissioner of Patents prior to the creation of the Court of Customs and Patent Appeals in 1929. In this case plaintiff had used the trade-mark "Victor" on ranges and stoves since 1887, but not on furnaces until 1923. Defendant had used the identical mark on furnaces since 1895. On March 1, 1924, plaintiff was refused registration of the trade-mark to be applied to furnaces on the grounds of laches. The Commissioner of Patents found that the parties had sold their products in substantially the same territory, without a single instance of confusion. The Court in affirming the decision of the Commissioner of Patents was of the opinion that the plaintiff had practically acquiesced in the exclusive use of the trade-mark by the defendant with respect to furnaces, during which time defendant had built up a market and good-will for its product under the name "Victor". Such an appropriation, i.e., the use of its trade-mark on furnaces, by the plaintiff would be clearly inequitable in the estimation of the Court.

It is to be noted that in this case, as in the Hanover case, the trade-marks were not merely confusingly similar in sound, but were identical. It is also pointed out that in each case the Court commented on the development of good-will and market by the later user, thus indicating their appreciation of the equities involved.

It is also stated in the instant case "There is no evidence in the record that appellant ever acquiesced in the use of the mark 'Klad-ezee' by appellee". This statement appears to affirm the doctrine of the Hartogensis case in regard to
laches which calls for *affirmative* acts of acquiescence by the prior user, and not merely *practical* acquiescence, the standard used in the *Victor Stove Co. case*.

According to the *Hartogensis case* the defense of laches as viewed by the Court of Customs and Patent Appeals is predicated upon a statutory construction of the words "at any time" in § 13 of the Trade-Mark Act of 1905, *supra*. This view evidently is a much narrower one than has been held by the regular judicial courts in cases involving infringement based upon prior use of a trade-mark. *Chase Brass & Copper Co. v. Chase Metalcraft Corp.*, 19 F. Supp. 966 (S. D. N. Y. 1937); *Valvoline Oil Co. v. Havoline Oil Co.*, 211 F. 189 (S. D. N. Y. 1913). These cases held that laches could be used as a defense where complainant merely had knowledge of the infringement. In *Quigley Pub. Co., Inc. v. Showmen's Round Table, Inc.*, 7 F. Supp. 410 (S. D. N. Y. 1934), the court went so far as to say that ten months' delay without adequate explanation would constitute laches.

AUSTIN P. SULLIVAN.
BOOK REVIEWS


Professor Johnson in his Preface disclaims the idea that this study is "a definitive treatment of the subject." His purpose is rather "to assemble some of the historic arguments in support of the bicameral system, to present criticisms against it and consider some of the remedies, with special attention to the unicameral form." His book, therefore, contains a brief historical review of the evolution of the British Parliament, of the tendency toward centralization of legislative power in the House of Commons; an account of the development of the legislature in France, with its shift between one and two chambers; and short descriptions of the practice in other countries varying between unicameralism and bicameralism. More in detail is the treatment of early legislatures in the United States, with a description of the unicameral state legislatures in the early constitutions of Georgia, Pennsylvania and Vermont. He especially dwells on the unicameral legislature of Vermont which lasted from 1777 to 1836, and which the author, citing Professor Daniel B. Carroll, believes gave at least as good results as the bicameral system which has existed from 1836 to the present. He concludes that usage and tradition made bicameralism an established institution in the United States, which is only recently being shaken by the advocates of unicameralism, especially since that system was adopted by Nebraska in 1934.

The author gives a brief comment on the first session, which opened on January 5, 1937, calling attention to some of its achievements, notably cutting down the number of standing committees to 15, which, with a committee on committees and a committee on rules, made a total of 17, in contrast with 32 in the Senate and 36 in the House—a total of 68 in the preceding legislature. Another really important innovation provided for by the rules was the public hearing on every bill while in committee. Reports on the work of the legislature insist on the effectiveness of these hearings and the fairness with which they were conducted. Perhaps one of the worst features of the ordinary state legislature is the ineffectiveness of public hearings—a contrast with the full hearings and enormous amount of information laid before the committees of both houses of the Congress of the United States.1

Another important change in committee procedure and one that is the beginning of an important function, was the requirement of the

†Executive Dean, Union College.

1P. 139.
filing of a report of committee action on every bill. This, it may be hoped, will lead finally to a reasoned committee report on important bills, such as is the regular practice in Congress and has been recommended for the legislature in New York.²

It is not possible to pass definitely on the success of the unicameral legislature as the result of one session; but the reviewer agrees with the author in his generally favorable opinion as to the results of the session and in the conclusion expressed, as the author says, by one of the Nebraska Senators, that changes in the future "will not be reversion to the two-house system but improvement of the one-house plan."³

The reviewer thinks that one of the great improvements of the single chamber system will be the result of the use of the legislative council.⁴ If the council develops as is hoped, it will be an organ for the study and preparation of projects of legislation operating in the interim between sessions, a forum before which different interests, economic, social and political, may appear and develop their arguments with more time and publicity than is possible during the short legislative session, no matter how good the legislative committee system may be. The council will do the work which in other states is done by interim legislative committees, but if it has a trained nonpartisan personnel and if its membership is kept on the high order of the present council, it may perhaps prove to be one of the most significant accomplishments of the Nebraska experiment. For the council does not only study proposals and draft bills; it is hoped that it will arrange proposals in the order of importance, so that it will present a definite legislative program to the people at the time of the election of the Senators, or before the assembling of each session, which will permit a general popular discussion, based, not on suggestions, but on definite proposals in the form of bills. If the people respond, the result may be very close to a popular referendum on the council's bills and its program, perhaps showing approval of some and disapproval of others and perhaps forcing the modification of the original program. Thus, a real opportunity will be presented to the people of Nebraska to express their will in regard to legislative proposals and their relative importance.

Nebraska seems to the reviewer an ideal state for the unicameral experiment. There is no serious difficulty in regard to the rural-urban problem, so important in other states. Representation of the city of Omaha does not bulk large in Nebraska, as would be the case of cities in California⁵ or Ohio,⁶ or in such states as New York, with its great

---

²P. 88.
³P. 161.
⁴Pp. 116-117.
⁵P. 148.
⁶P. 121.

urban vote, or Maryland, where Baltimore contains more than half the total population of the state. Nebraska is predominantly agricultural, and even in its smaller cities, the interests of the population are often more with the farming than with the industrial community, so that the contention between the industrial and the rural areas does not exist as a serious situation. Taxation, furthermore, is not complicated, but the state still depends largely on the land tax. Nor is the demand for social legislation and industrial legislation in Nebraska as insistent as in great manufacturing and rural states.

In his excellent discussion of the advantages and disadvantages of the bicameral system as against the unicameral, the author has suggested the ancient bases for bicameralism, that it was justifiable only when each house represented a different interest or when one by length of service of its members could act as a check on the other, and doubts their validity today, even though he points out the persistence of these bases and suggests that the first may be met by an adjustment of membership in a single chamber. It seems to the reviewer that the author does not quite sufficiently insist on the real difference between a system of two houses, one controlled by urban and one by rural districts, and the system in which there might be some adjustment by which the many rural counties would elect a larger proportion of members than their population would warrant as against the representation from the cities.\footnote{Pp. 127-128.} In the latter, while this arrangement recognizes that the difference in interest warrants representation on another basis than that of voting strength or of population, it does not give the same check as the system of the two houses, for there will be in the single house either an urban or a rural majority which can impose its will on the minority in case of a clash. This, however, emphasizes the point that a single house will be more apt to take action and cannot "pass the buck" between houses.

The chart of the proposals for unicameral legislatures in different states is very interesting. In the states in which the urban-rural question is important, it shows universal efforts to meet this situation by giving an advantage to the minority rural interest. It is interesting to note that the proposals do not suggest proportional representation as a means of electing representatives, but that they incline to the single district and that the dependence on the county as a unit is still strong in many states.

Nonpartisan elections, joined to the consequences of the work of the legislative council, should focus the attention of Nebraska legislators on the merits of proposals free from the pressure of party machines, and the responsibility of the council and the single chamber make unnecessary
the responsibility of the party in control for the work of each session and the value of criticism by the minority party especially in financial and important social questions is minimized. A campaign on the basis of the council's proposals, may be an excellent substitute for a campaign on the basis of a party platform.

Professor Johnson has packed into a short volume a surprisingly large and well arranged amount of material. He has brought out clearly the worst defects in our American legislative system; his book provides an exceptional basis for discussion, and his thoughtful guidance through the mazes of various legislative difficulties is most helpful.

JOSEPH P. CHAMBERLAIN*


In the reviewer's opinion the authors have selected too narrow a title for this informing, though brief, book. A broader one, such as, perhaps, "The Adolescent Offender," would have been more suggestive of the range of the contents. Their initial premise is that adolescence represents a particularly difficult period of adjustment, with problems of rapidly increasing complexity, yet that this period is given little or no special attention by our common law criminal procedure. This inattention is the more surprising in view of the fact that the civil law still regards the adolescent as incapable of mature and ripe handling of his own affairs, when the criminal law proclaims him an adult merely by passing beyond the juvenile court age. Such inattention, they continue, is all the more short-sighted because of the fact that today the largest proportion of crimes is committed by this "forgotten group" of offenders between the ages of sixteen and twenty-one. From this starting point the authors proceed to examine the factors making for adolescent delinquency.

As is to be expected, they reject the one-time, but now outworn, notion that there is any single explanation of delinquent or criminal conduct, whether inherited criminal tendency, mental defect, or what have you. Instead it is the effect of many factors, a large number of which are summed up in the word, "environment." There is nothing

*Professor of Public Law, Columbia University School of Law.

†Member of the Bar of New York; City Magistrate, New York City.
‡Acting Dean, School of Education, New York University.
1The maximum age for the Borstol institution (viz., places for adolescent incarceration) in England has been raised recently from twenty-one to twenty-three.
startling in their conclusion that "slums and blighted areas are an expensive luxury." This preliminary material, showing what the problem of the adolescent is and how serious is our present failure to solve it, takes up the first two-thirds of the book.

The remainder deals with the setting up of a specialized adolescents' court. The authors are strongly opposed to meeting the situation merely by raising the juvenile court age limit. This would not only be harmful to the juveniles, so brought into contact with older offenders, but would also result in lessened emphasis on the separate and largely different problems of the latter group. A separate court is needed, in these writers' opinion, with its own machinery for the proper socialized treatment of its human material, such as segregation from other age groups, supervision from contaminating contacts inside their own group while awaiting court action, mental examination where needed, proper case investigation prior to trial, etc. The adolescents' courts as they are now functioning in Chicago, Philadelphia and (most recently) Brooklyn are then examined and compared, to the advantage, incidentally, of each in one respect or another. As is to be expected, that in Brooklyn, which is so largely a result of Chicago and Philadelphia experience, makes the best overall showing, although one innovation in it is hard to understand, viz., the rotation of judges after service of two weeks in the court. With many cases kept active for a long time for the admitted purpose of continuing supervision by a judge informed of all its developments, the purpose of such rotation is hard to see. The authors offer no comment on this point. A typical day in the Brooklyn court forms part of the concluding chapter.

The book is almost free from printer's errors. The English used is of a clarity and excellence that deserves special mention. In only two matters did the reviewer find evidence of possible haste which, presumably, greater care would have discovered and corrected. There is not, and, so far as the reviewer knows, there never has been a Judge John Gutnick in Chicago.\(^2\) Presumably the reference is to Judge John Gutknecht, who has been active in boys' court matters in that city. Particularly to be regretted is the complete absence of an index. This work deserved better treatment than that.

E. W. PUTTKAMMER*

---

\(^2\)P. 181.

*Professor of Law, The University of Chicago Law School.

Mr. Kirsh, who was for some years Special Assistant to the United States Attorney in New York in the prosecution of Anti-Trust cases, published in 1927 and 1928 a series of thoughtful and suggestive law review articles on the legal problems faced by trade associations, with particular reference to difficulties arising under the Anti-Trust laws. These articles were presented in book form in Trade Associations: The Legal Aspects.¹ That volume has been of great value to those interested in trade associations, and particularly to attorneys practicing in that field.

Trade Associations in Law and Business is a revision of the earlier work, and covers the same general subject matter, although the arrangement has in some respects been changed. The chapters on Foreign Trade Functions in Trade Associations, Credit Bureau Functions, Uniform Cost Accounting Methods, and Standardization by Trade Associations are reproduced with little change other than to supply references to some of the more recent authorities. The chapter on Statistical Reporting Service of Trade Associations has been expanded so as to include an analysis of the Sugar Institute case.² The chapter on Trade Relations of Trade Associations has been almost completely rewritten, with a view to presenting a picture of the steps which business is now permitted to take in the direction of self-discipline. This chapter, which is potentially one of the most interesting and valuable in the book, raises the issues involved and points the attorney to the governing authorities, but its usefulness would be greatly enhanced by closer and more explicit analysis and a better organized arrangement of problems and conclusions. The chapter in the earlier book entitled Restricting Channels of Distribution has been given the heading Boycotts and Defensive Combinations, and has been expanded to include an extended discussion of such cases as Federal Trade Commission v. Wallace,³ United States v. American Livestock Commission Co.,⁴ Paramount Famous Lasky Corporation v. United States,⁵ Wm. Filene’s Sons Co. v. Fashion Originators’ Guild of America, Inc.,⁶ and Arnold v. Burgess.⁷ A discussion of the Gasoline

†Member of the Bar of New York.
‡Member of the Bar of New York.
¹Central Book Company, New York, 1928.
²Sugar Institute, Inc. v. United States, 297 U. S. 553 (1936).
³75 F. (2d) 733 (C. C. A. 8th, 1935).
⁴279 U. S. 435 (1929).
⁵282 U. S. 30 (1930).
⁶90 F. (2d) 556 (C. C. A. 1st, 1937).
⁷241 App. Div. 364, 272 N. Y. Supp. 534 (1st Dep’t 1934) aff’d without opinion, 269
Cracking case\textsuperscript{8} and Lynch v. Magnavox Co.,\textsuperscript{9} has been added to the chapter on Patent Interchange and Cross-License Agreements, together with a survey of some of the practical problems confronting the practitioner in this field. The material on Uniform Basing Point Systems of Trade Associations has been extensively revised, and contains a valuable summary of recent developments in the steel industry and in the cast-iron pipe industry. The chapter on Collective Purchasing Functions of Trade Associations has been rewritten in the light of the Robinson-Patman Act,\textsuperscript{10} as well as of the Appalachian Coals case,\textsuperscript{11} and other recent decisions.

There is no attempt to deal with the mechanical details of forming a trade association or keeping it in smooth operation. The book will not serve, and doubtless was not intended to serve, as a ready guide in meeting many of the administrative problems faced by an active association, though it is full of practical suggestions to association members and their counsel. The approach of the author and his collaborator is at all times thoughtful and scholarly, as well as practical. Mr. Kirsh's first book, however, was somewhat lacking in coordination, doubtless by reason of the fact that it was a collection of articles, and the opportunity presented by a second edition might well have been used to knit the material together in a somewhat more integrated fashion. The present volume, however, does not represent a very decided improvement over the first edition in this respect. For example, on page 327 of the book under review, at which Mr. Kirsh is discussing foreign trade functions of trade associations, he refers to some of the economic advantages of trade associations and states: "These subjects have been treated in greater detail elsewhere", citing his law review articles rather than making cross references to other portions of the work in hand. It is also to be remarked that relatively little emphasis is given to the activities of the Federal Trade Commission with respect to trade associations. The attitude of the Commission regarding a given trade association activity, as reflected in the Commission's complaints and orders, can have, after all, a good deal of practical importance to the parties concerned, and greater use of this material might profitably have been made.

Though the book is primarily concerned with legal rather than economic problems the amount of non-legal material presented is considerable. This supplies a valuable background to the trade association

\textsuperscript{8}Standard Oil Co. v. United States, 283 U. S. 163 (1931).
\textsuperscript{9}94 F. (2d) 883 (C. C. A. 9th, 1938).
\textsuperscript{11}Appalachian Coals, Inc. v. United States, 288 U. S. 344 (1933).
attorney and seldom interferes with the clarity or validity of the author’s discussion of the related legal questions. It is clear that Mr. Kirsh recognizes that so long as the Sherman and Clayton Acts remain on the statute books the courts must continue to condemn certain lines of business conduct irrespective of the economic benefit which such conduct might confer on the community in a particular case, and, further, that the courts must continue to look at the practical result of all of the activities of an association, rather than the effect of each activity taken singly. If the reader will study the book as a whole, or a given chapter as a whole, the economic arguments presented will not create misleading impressions as to the existing state of the law.

Mr. Kirsh’s introductory chapter is interesting and suggestive. Pointing out the comparative powerlessness of any trade association “to overcome the disintegrating efforts [effects?] of the activities of recalcitrant minorities during an era of economic stress”12, he looks to the forthcoming Monopoly Inquiry to investigate the issues and suggest a solution. He no doubt hopes for such a revision of the law as will encourage the further development of trade associations, but he makes no concrete proposals, nor does he suggest that future legislation should draw distinctions between the various types of association. Yet it seems clear that an organization of the type involved in the Sugar Institute case is very different in its functions, and in its potential dangers and advantages to the community, from a loosely knit association of many thousands of retail dealers. It would seem that any solution of the problem which is to be more than temporary must be grounded on a thorough investigation of factors such as these.

GEORGE T. WASHINGTON*


Peculiarly appropriate to an election year is Matthew Josephson’s The Politicos. Of course it is not intended that a work of such proportions as this should be passed over lightly with the cavalier comment that its message is well-timed but of only ephemeral importance. It is a lesson well to be minded by the electorate this year and two years hence, and thereafter with each recurrent election period, that good government is much more a matter of careful selection of personalities than

12P. 32.

*Assistant Professor of Law in the Cornell Law School.

†Author of The Robber Barons (1931).
astigmatic adherence to political parties and faith in platform promises. It is high time that heed was given to the view, not many times realized since Washington occupied the office, that the presidency (and other high elective positions) should be reserved not for the party wheel-horse, but for the man, whatever his party affiliation, believed best fitted of all men available to receive a trust of such dignity and responsibility. Far from promoting this ideal the party system has stifled it quite completely. It comes as no news to us today that the raison d'etre of the system—to give the electorate a choice between clean-cut issues and principles—has to no appreciable extent been fulfilled within the memory of men now living. As news to some may come the lesson taught by The Politicos, that from the Civil War to the turn of the century it was the same; that changes in administrations meant merely that the ten fingers of one political party were greedily snatched from the patronage pie to make room for ten even more predatory. Issues of reconstruction, paper money, protective tariff, civil service reform, and free silver were raised as smoke screens to delude the public that it would make an important difference whether the Democrat succeeded the Republican, whether Justice Bradley cast the die in 1877 toward Rutherford Hayes or Samuel Tilden. But the Robber Barons behind the scenes filled the coffers of both parties, knowing full well that however matters fell theirs would be the ultimate victory. Surface scratched with coin Democrat and Republican showed up the same—politicos, "mouthing one set of ideals or doctrines, for which they show the warmest attachment, and even traditional reverence (e.g., Liberty or Justice), while at the same time they are plainly seen to be pursuing ends or interests wholly at variance with their professions of faith."

The author projects his thesis against a background made familiar by him in his earlier work The Robber Barons. There the players were the financial tycoons of the period, Morgan, Gould, Belmont, Huntington, Cooke, Whitney, Havemyer, Carnegie, Hill, and the rest. Here he peoples the same scenery with a chorus of the nominal party leaders, Grant, Hayes, Garfield, Arthur, Cleveland, Harrison, and Cleveland again, but the real protagonists are the wire pullers and public purse string looseners, Thad Stevens, Roscoe Conkling, Ben Butler, Simon Cameron, Zach Chandler, Tom Platt, Matt Quay, with solo specialties by the likes of Charles Sumner, Thomas B. Reed, Carl Schurz, James Blaine, William McKinley—Mark Hanna (the Gold Dust twins), and William Jennings Bryan, on whose 1896 dénouement the curtain falls.

The author builds on the principle that repetition is the surest tool of sound pedagogy. It may be, but the sameness of treatment with

\[P. ix.\]
which the administration of Hayes succeeds that of Grant, and those of Garfield and Arthur on that of Hayes, and so on, packs a burden of monotony that is at times almost too heavy. More interesting than any of the others are the chapters dealing with the Cleveland Administrations, particularly the second, (1893-1897), when occurred conflicts on many fronts between the “haves” and the “have-nots”, largely engendered by the panic of 1893. Cleveland himself is shrunken in stature to fit the mould cast for him by Woodrow Wilson, when in 1913 Wilson said: “You may think Cleveland’s administration was Democratic. It was not. Cleveland was a conservative Republican.”

The author’s most mordant excoriations are directed not at Cleveland, however, but at his Attorney-General, Richard Olney of Massachusetts. In detail the author pictures the critical Pullman Strike of 1894 at Chicago to throw Olney’s part, in moving the President to dispatch Federal troops, into strong contrast with the position of Governor John Altgeld of Illinois, who thought the state authorities altogether competent to cope with the situation. (For Altgeld alone, of all the personages portrayed, the author drops a pen of critical analysis and employs the brush of the hero painter.) Not content with throwing the power of the National Guard at the back of the railroad owners, Olney labored zealously to add the infinitely greater weight of the courts with their telling weapon of the labor injunction. His triumph in the Debs case is contrasted with his abject failure in the Anti-Trust Law case where, the author suggests, Olney deliberately let the government down, content, once having freed interstate commerce of the “interruptions” of Debs and his coterie, to see it far more effectively plugged by the Beef Trust of Armour and the Sugar Trust of Havemyer. To complete the record, the Attorney-General is described as having argued the Income Tax case of 1895 with “dead heart”, leaving the scarey Justice Field easy prey to the class legislation hobgoblins of that all too able defender of vested interests, Joseph Choate. The Debs, Knight, and Pollock deci-

---

3P. 392.

4Eugene V. Debs, leader of the strikers, was jailed for violation of the injunction issued by the federal court in Chicago. His imprisonment was sustained by the United States Supreme Court in habeas corpus proceedings entitled In re Debs, 158 U. S. 564 (1895). This decision, the author comments, “represented not only a complete vindication for Olney and Cleveland, but as Cooley, the famous jurist who was to enter the Supreme Court later (?), remarked, ‘a great and valuable lesson in constitutional construction . . . settled for all time.’” At p. 606.

5United States v. E. C. Knight Co., 156 U. S. 1 (1895) (The Knight Company was a subsidiary of the American Sugar Refining Company).

6P. 608.


8P. 610.
ions, coming so closely on the heels of one another, the author views as a "kind of legal 'revolution' or coup d'etat", giving to the Supreme Court "the commanding role in our Government." Against the view of many commentators that these decisions plummeted the Court to an all time low in public esteem, the author attributes to them "much of the religious reverence which now attaches to the Supreme Court forty years later."

In view of the space devoted to the contribution made by the Court to this part of the period covered, it seems odd and somewhat disappointing that the author should ignore the Legal Tender decisions9 of the Grant Administration as a fruitful source of material mirroring the trend of that era. Even more tantalizing is the mere hint that the author shares the opinion of Charles A. Beard et al. that the cryptic ambiguity of the Fourteenth Amendment was deliberately planned by the Joint Committee of Fifteen on Reconstruction in charge of its drafting.11 Surely the author's research into the life of Roscoe Conkling of New York, one of the Senate representatives on the Committee, must have disclosed something to illuminate the part played by Conkling12 in bringing the Court (the chief justiceship of which he had refused in 1873, and an associate justiceship in 1882) to the conviction13 that the people, in adopting the Fourteenth Amendment intended to bring under its protecting aegis not the black man alone but the corporation too.14 Perhaps attention to such matters would have made an already longish

1P. 605.  2Ibid.
3Hepburn v. Griswold, 8 Wall. 603 (U. S. 1870), overruled in Knox v. Lee, 12 Wall. 457 (1870). These cases are mentioned but once by the author, and then only a brief, non-discursive footnote (at p. 605).
4See Graham, The "Conspiracy Theory" of the Fourteenth Amendment (1938) 47 Yale L. J. 371.
6The point was decided for the first time four years after Conkling's argument in a case similar to the San Mateo case, viz., Santa Clara County v. Southern Pacific R.R., 118 U. S. 394, 396 (1886).
7Argument concerning the validity of the Court's conclusion has been rendered somewhat less academic by the position assumed by Mr. Justice Black in his dissenting opinion in Connecticut General Life Ins. Co. v. Johnson, 58 Sup. Ct. 436 (1938): "I do not believe the word 'person' in the Fourteenth Amendment includes corporations. . . . A secret purpose on the part of the members of the committee, even if such be the fact, however, would not be sufficient to justify any such construction. The history of the amendment proves that the people were told that its purpose was to protect weak and helpless human beings and were not told that it was intended to remove corporations in any fashion from the control of state governments. . . . I believe this Court should now overrule previous decisions which interpreted the Fourteenth Amendment to include corporations." (At pp. 440, 441. Italics supplied).
book over-lengthy. Yet they can hardly be called foreign to the author's thesis. In this day it seems almost banal to suggest that our highest bench has known the presence of some of the greatest politico-craftsmen of our history. Without proportionate discussion of their contribution no depiction of the political development of any period may well be called complete. Perhaps now that we have the politicos hung in the gallery along by the Robber Barons we may soon have the group completed with a portrayal of the judiciary of the era.

F. C. NASH*


In this day of economic and legal boundary leveling, the thought of large-scale, interstate operations, being vitally affected by and dependent upon state legislation, becomes almost incongruous. The inevitable question that rises is whether or not some federal law does not overrule and supersede the state acts. Thus, when a book is published entitled The Delaware Corporation, the reflex reaction is one of doubt as to its value except from an academic and historical viewpoint.

But strangely enough the corporate form, together with all of its incidents was still, as of 1932, a sphere almost wholly regulated and prescribed by the states. True, anti-trust legislation had blunted somewhat the power of the state legislatures, but the essence of the corporation, and the power to grant—and choke off—its existence remained in the palms of the several states. The early days of the New Deal foreshadowed a change in this, as in other particular fields previously under exclusive, local control. Today the Securities and Exchange Commission and the various federal acts regulating the type of corporations which may exist and decreeing the manner in which their securities may be offered to the public, have greatly enlarged the scope of federal control in the corporate field, as they have similarly diminished the power of the states. However, as of today, there is still no law providing for incorporation of inter-state business under federal laws although such legislation has been proposed and is pending in the Congress at present. Further, it seems unlikely that such legislation will be enacted during the next year or two.

Hence, it is that the thoroughgoing nationalist will pause and realize that perhaps there is some sound basis, other than as a record, for

*Professor of Law in the Georgetown University Law School; former Editor of this Journal.

†Department of Economics, Massachusetts State College.
posterity in the publication of the present work. One who wishes to form a corporation, still must do it locally under the guidance of state law though he must in addition conform to certain federal standards and requirements.

The book is small—179 pages of text—and it is written by an economist. Hence, it is to be expected that it would not be—as it is not—a learned legal or juristic treatise. Rather it deals briefly with the historical phases of the present Delaware law, tracing the steps leading up to the present day statute and contrasting and comparing the laws of other states with those of Delaware. The book is a unit (No. 25 of a New Series) of the Johns Hopkins University Studies in Historical and Political Science. The table of contents gives a very good picture of the plan of the book. This plan will be followed in outlining the scope of Professor Larcom's work.

Chapter One is entitled The Adoption of the Corporation Law of 1899. The principal conclusion that can be drawn from this chapter which outlines the evolution of the original Delaware Act, is that Delaware has rather consistently waited for other states to act and then deliberately has gone further in its concessions to corporate promoters and directors. New Jersey, until the intrusion of Delaware into the field, was the state in which new incorporations were most prolific. Hence, the franchise and other tax rates in the Delaware law closely resemble components of a "low bid" contract, with Delaware in every case underbidding her sister state.

In Chapter Two is portrayed the evolution of the Certificate of Incorporation under Delaware law. There is a particularly timely discussion of the rights, or rather lack of rights, of preferred stockholders under that law. Mr. Larcom points out, however, that the courts have persisted in protecting accumulated unpaid dividends under certain circumstances. It may be observed here that throughout the book the author insists that the only safeguard to the liberal laws of Delaware has been a sane and soundly grounded court in that state.

Chapter Three, The Power to Hold Stock in Other Corporations, contains a good discussion of consolidation and reorganization laws, especially as they affect the formation and use of subsidiary and interlocking corporations. The author's conclusion is that "... the subsidiary will remain an important, if temporary, method of organizing the business of an individual corporation."1

The Issue and Payment of Capital Stock, forms the theme of Chapter Four. Since Delaware was, as in other phases of the law, partly the pioneer and greatly the imitator and perfecter of the issuance and use

1 P. 72.
of "no-par" stock, the discussion is particularly interesting in this field.
Although New York and Maryland tested the concept first, Delaware
improved upon it and made it a popular vehicle for escaping many
previous practical difficulties with regard to valuation of capital stock
and also with regard to the payment of promoters and others for services
rendered and property sold to the infant corporation. It brought about
"Blue Sky" legislation which culminated in that portion of the Securities
Act of 1933 under which "protection has been afforded [the public]
by direct interference with the operation of the state laws regulating
the issue and payment of stock... While these valuations [of the stock
by promoters—overthrown by the Securities and Exchange Commission]
are of the type which the Delaware courts might not have upheld in the
interpretation of the statute, the importance of the Securities Commis-
sion's policy from the point of view of the investor lies in the fact that
protection is afforded before an amendment is made."2 It might have
been well had the author added that even such protection as that
afforded by the S. E. C. is not going to stop incautious and careless
"investors" from "taking a plunge" on unsound and ill-advised "tips".
Again in Chapter Five, Corporate Capital, there is an intelligent
discussion of an evolutionary process. It involves the rules and
restrictions relative to the payment of dividends, and shows the extent
to which Delaware has gone—surpassed in this only by California—in
allowing dividends to be paid out of so called "capital". To the author
these laws, and their near counterparts in a few other states, represent
bad accounting practice. However, he believes that the S. E. C. will
be able "to preserve sound accounting methods"3 in spite of bad state
legislation.
In Chapter Six, The Exercise of Corporate Powers, the author's theme
is again taken up to the effect that the tendency is to withdraw all
limitations on corporate powers, and to center power in a reasonably
flexible board of directors, rather than in the more unwieldy group of
individual stockholders. Once more he reiterates that the theory behind
the Delaware legislation is that the good balance of the courts will pre-
serve the rights of the minorities. And again the statement is made
that the trouble with this theory is, that most of the injustice done, for
one reason or another, will never reach the courtroom.
The final chapter is a statistical summary showing graphically, and
with various tables of figures, that Delaware's goal, expanded revenues
through liberal incorporation laws, has certainly been attained.
The reader experiences reasonable disappointment that the economis-
author, with such an interesting and timely subject, and with such worth-
while material, does not dwell longer upon the economic aspects of Delaware corporation law. Mr. Larcom seldom draws conclusions; and where he might easily and profitably expand a point, he simply allows the reader to formulate his own conclusions. The work would have been greatly improved had his efforts been greater to bring into relief the relationship between the economic and legal aspects of the liberal corporation policy in the State of Delaware, and their importance in relation to the depression of 1929 and the present "recession".

The book should be of interest to a student rounding out a law school course in Corporation Law. For the lawyer in general practice, or for the specialist in corporate practice, it is valuable only to the extent that it refreshes the memory as to the chronology of the present law. For the teacher of a course in Corporation Law, it should prove a valuable handbook. It is not, of course, of any value as a text book or reference work on corporation law—nor has Mr. Larcom intended it to be so.

J. NICHOLAS SHRIVER, JR.*

*Member of the bars of Maryland and the District of Columbia; former Associate Editor of this JOURNAL.
BOOKS RECEIVED

A number of the books listed below will be reviewed in the January issue of the Journal


