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Recent Cases

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RECENT CASES

Administrative Law—Freedom of Information Act—Unclassified Docnments Physically Connected with Classified Documents May Not Be Withheld Under the National Secnrity and Foreign Affairs Secrets Exemption

Appellants brought suit under the Freedom of Information Act (FOIA)[1] to obtain several documents[2] pertaining to an underground nuclear test explosion scheduled to take place off Amchitka Island, Alaska. Appellee, the Environmental Protection Agency, had refused to produce the documents, which included an attached, but unclassified, memorandum from the Council on Environmental Equality concerning the probable environmental consequences of the planned test. Appellants maintained that the national defense and foreign affairs secrets exemption to the FOIA[3] requires that each document an agency wishes to withhold be classified by a separate executive order. Appellee argued that, under Executive Order No. 10,501,[4] a group of physically connected documents should be classified no lower than the most highly classified document therein. Accepting appellee's argument, the district court refused to compel disclosure.[5] On appeal to the United States

1. 5 U.S.C. § 552 (1970). The Act requires federal agencies to make information available to any person, unless the information falls within one of the 9 enumerated exemptions specified in the Act.

2. The documents—which dealt with the environmental, national defense, and foreign relatims consequences of the planned test—were prepared by a special committee established by the President on January 20, 1969, as part of the National Security Council system. The Committee was established to review the annual underground nuclear test program. Representative Patsy T. Mink of Hawaii asked the White House for copies of the report. When her request was denied, Representative Mink and 32 other members of Congress brought this suit.

3. 5 U.S.C. § 552(b)(1) permits the withholding of information if it is: "specifically required by Executive order to be kept secret in the interest of national defense or foreign policy . . . ."

4. 3 C.F.R. § 292 (Supp. 1971). Paragraph (b) of § 3 of Executive Order No. 10,501 provides: "The classification of a file or group of physically connected documents shall be at least as high as that of the most highly classified document therein."

5. The district court concluded that all the documents were within the national security and foreign affairs exemption and that the documents also were covered by the inter-agency memoranda exemption. 5 U.S.C. § 552(b)(5) (1970) permits withholding matters if they are "inter-agency or intra-agency memoranda or letters which would not be available by law to a party other than an agency in litigation with the agency . . . ." Such internal governmental communications were first recognized as privileged in United States v. Morgan, 313 U.S. 409 (1940). In Kaiser Aluminum & Chem. Corp. v. United States, 157 F. Supp. 939, 946 (Ct. Cl. 1958), protection was said to focus

Court of Appeals for the District of Columbia Circuit, *held*, reversed and remanded. Documents that are associated with separately classified papers, but that are not independently classified as secret do not qualify for the national defense and foreign affairs secrets exemption. *Mink v. Environmental Protection Agency*, No. 17-1708 (D.C. Cir. Oct. 15, 1971).

Throughout the history of our government, the judiciary has been confronted with the task of achieving a socially desirable balance between the individual's right of access to government-held information and the government's legitimate interest in the nondisclosure of such information. As early as 1875, in *Totten v. United States*,[6] the Supreme Court refused to grant an individual the enforcement of a secret government service contract on the grounds that the existence of a contract of that nature is itself a fact not to be disclosed and that disclosure of the service contracted for might compromise or embarrass the Government in performing its public duties or in engaging in foreign relations.[7] This early judicial recognition that the executive may withhold information the disclosure of which would endanger the national security or obstruct the Government's conduct of foreign affairs has been followed repeatedly in subsequent cases.[8] The Supreme Court, however, has acknowl-

on the "consultative functions of government." From the view that the privilege was intended to protect the administrator's mental processes, the courts restricted the common-law privilege to inter-agency or intra-agency memoranda containing opinions or recommendations that are part of the decision-making process, but the privilege has been held not to apply to memoranda that are mere factual reports. *See, e.g.*, Machin v. Zuckert, 316 F.2d 336 (D.C. Cir. 1963) (accident report by Air Force concerning airplane crash); Boeing Airplane Co. v. Coggeshall, 280 F.2d 654 (D.C. Cir. 1960) (documents of Renegotiation Board). This distinction has received congressional sanction in exemption 5 of the FOIA. *See, e.g.*, Soucie v. David, 448 F.2d 1067 (D.C. Cir. April 13, 1971) (document evaluating Government's program for developing a supersonic transport aircraft); Bristol-Meyers Co. v. FTC, 424 F.2d 935 (D.C. Cir. 1970) (FTC staff investigative reports); Ackerly v. Ley, 420 F.2d 1336 (D.C. Cir. 1969) (document held by Commissioner of Food and Drugs relating to hazard of carbon tetrachloride); American Mail Line, Ltd. v. Gulick, 411 F.2d 696 (D.C. Cir. 1969) (staff memorandum of Maritime Subsidy Board for Department of Commerce); Freeman v. Seligson, 405 F.2d 1326 (D.C. Cir. 1968) (documents held by Secretary of Agriculture). In the instant case, the court stated that, while this exemption protects the decisional processes of the President and other officials, it does not prevent disclosure of factual information, unless it is inextricably intertwined with the policy-making processes. Under the circuit court's remand order, the district court will examine the documents in question *in camera* and can deny disclosure under this exemption only for those documents that involve internal communications of advice or opinions that are a part of the policy-making process.

6. 92 U.S. 105 (1875) (individual made contract with President Lincoln to do clandestine work in the South during the Civil War).

7. *Id.* at 106.

8. *See, e.g.*, Cresmer v. United States, 9 F.R.D. 203 (E.D.N.Y. 1949) (report is privileged if disclosure would reveal a military secret or constitute a threat to the national security); Pollen v. Ford Instrument Co., 26 F. Supp. 583 (E.D.N.Y. 1939) (secrecy required concerning invention of military device); Firth Sterling Steel Co. v. Bethlehem Steel Co., 199 F. 353 (E.D. Pa. 1912) (subject matter of information contained in drawings is privileged as government secret in military matter).

edged that, although there exists an executive privilege to protect military and state secrets, the judiciary cannot wholly abdicate its control over the evidence in a case and over what information permissibly may be withheld to the discretion of executive officers.[9] In *United States v. Reynolds*,[10] the Court identified the problem as essentially one of the court's determining the appropriateness of the Government's claim of privilege in a manner that will not force disclosure of the very thing that the privilege is designed to protect. In assessing this request for secrecy, the Supreme Court held that it is the duty of the trial court to look at all the circumstances of the case to ascertain whether there is a reasonable danger that disclosure of the evidence would expose matters that, in the interest of national security, should not be divulged. If the trial court finds the existence of such danger, the Government's claim of privilege must be upheld without further judicial inquiry. The Court concluded that the extent to which the trial court should probe to determine whether disclosure of certain materials presents a reasonable danger to the national security depends upon the strength of the showing of necessity for disclosure. Even a strong showing of necessity, however, would make no difference if the court were satisfied that military secrets were involved.[11] In response to these judicial decisions, Congress, in 1946, enacted section 3 of the Administrative Procedure Act (APA), which was intended to increase public disclosure of administrative action.[12] Nevertheless, certain broad exceptions to the general policy compelling disclosure that were included in the Act when secrecy is required "in the public interest" or when information is designated as confidential "for good cause"[13] allowed the Act to be used as an effective instrument through which officials in the executive branch could justify nondisclosure of a large variety of material.[14] Executive Order No. 10,501, issued by President Eisenhower in November 1953, furnished further justification for nondisclosure practices and permitted blanket nondisclosure by providing that "[t]he classification of a file or group of physically connected documents shall be at least as high as that of the

9. United States v. Reynolds, 345 U.S. 1 (1953) (report resulting from investigation of crash of military aircraft in flight to test secret electronic equipment held privileged).

10. *Id.* at 8.

11. *Id.* at 10-11.

12. Administrative Procedure Act § 3, ch. 324, § 3, 60 Stat. 238 (1946), *as amended*, 5 U.S.C. § 552 (1970).

13. *Id.*

14. *See* Editorial Note, *The Freedom of Information Act: A Critical Review*, 38 GEO. WASH. L. REV. 150 (1969).

most highly classified document therein."[15] Thirteen years later, Congress, perceived the need to reassert the announced policy of full public disclosure, and bolstered it by amending section 3 of the APA with the enactment of the Freedom of Information Act.[16] This Act grants to any person a cause of action to obtain any identifiable record of a government agency that is improperly withheld. The Act vests the federal district courts with jurisdiction to conduct trials de novo in cases concerning the propriety of refusals to disclose and places the burden of proof on the agency to show that nondisclosure is justified under one of the nine exemptions specifically provided for in the Act.[17] One of these exemptions, subsection 552(b)(1),[18] is the statutory recognition of the executive privilege to withhold information relating to national defense and foreign policy. The Senate committee report described the change from the broad "in the public interest" standard for exemption under old section 3 to the national defense and foreign affairs secrets exemption of subsection (b)(1) as an attempt "both to delimit more narrowly the exception and to give it a more precise definition."[19] The House committee report referred to the exemption as covering those "categories of information which the President has determined must be kept secret to protect the national defense or to advance foreign policy, such as matters classified pursuant to Executive Order 10,501."[20] The Attorney General's office interpreted the reference in the House report to Executive Order No. 10,501 as an indication that no great degree of specificity is required in identifying matters to be covered by this exemption.[21] In 1970, the Ninth Circuit in *Epstein v. Resor*[22] accepted the interpretations placed upon the national security and foreign affairs secrets exemption by the House committee report and the Attorney General's memorandum. The court found that under subsection (b)(1), the legislature had expressly assigned to the executive the function of determining whether secrecy is required in the national interest. Furthermore, the court concluded that judicial review was limited to the question whether an appropriate executive

15. 3 C.F.R. § 292 (Supp. 1971).

16. 5 U.S.C. § 552 (1970).

17. *Id.*; *see* 83 HARV. L. REV. 928 (1970).

18. 5 U.S.C. § 552(b)(1) (1970) (permits withholding information under executive order "in the interest of national defense or foreign policy . . . .").

19. S. REP. No. 813, 89th Cong., 1st Sess. 8 (1965).

20. H.R. REP. No. 1497, 89th Cong., 2d Sess. 9-10 (1966).

21. DEP'T OF JUSTICE, ATTORNEY GENERAL'S MEMORANDUM ON THE PUBLIC INFORMATION SECTION OF THE ADMINISTRATIVE PROCEDURE ACT 30 (1967).

22. 421 F.2d 930 (9th Cir. 1970) (suit by historian to obtain Army file dealing with forced repatriation of Soviet citizens following World War II).

order invoking nondisclosure under the foreign affairs and national security secrets exemption had been promulgated on the material in question; judicial review of the factual basis for the administrative determination to classify certain documents as secret was precluded as constituting a political decision on matters not appropriately within the province of the courts.[23] The court in *Epstein* limited the scope of judicial inquiry under subsection (b)(1) to a determination whether the agency decision to withhold information was clearly arbitrary or capricious. This inquiry, in turn, was limited by the court to an investigation of the origin of the file contents and the surrounding circumstances, thus precluding any *in camera* examination of the file.[24]

In the instant case, the court initially recognized that the purpose of Congress in enacting the FOIA was to require federal agencies to make information available to any person, unless the information sought is withheld for a purpose enumerated in the nine exemptions to the disclosure rule. Although the legislative history of the Act does not define clearly the relationship between Executive Order No. 10,501 and the national security and foreign affairs secrets exemption, the court acknowledged that Executive Order No. 10,501 consistently has been the authority for classification of matters relating to national defense. Since it could find no rational basis for withholding on security grounds a document that had no independent need for classification and that was included in a file or was physically connected with classified documents,[25] the court determined that such attached, but unclassified documents are not included within the national security and foreign affairs secrets exemption. The court declared that this determination was made, even though it was inconsistent with Executive Order No. 10,501, because the terms and purposes of the FOIA, which was enacted subsequent to the Executive Order, demanded such a finding. The court emphasized that the congressional policy against secrecy by association manifested in the FOIA dictates that, if the nonsecret components of a file are separable from the secret remainder and may be read separately without distortion of meaning, these nonclassified items must be disclosed.[26]

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23. *Id.* at 933.

24. *Id.*

25. The court pointed out that this is not the type of case in which mere disclosure of the fact of the inquiry is itself impermissible.

26. Regarding the inter-agency or intra-agency memoranda exemption, the court merely stated that it would follow the interpretation it had recently placed upon the exemption in Soucie v. David, 448 F.2d 1067 (D.C. Cir., 1971), when it held that the exemption does not prevent the disclosure of factual information, unless that information is inextricably intertwined with the policy-making process.

The decision in the instant case marks a departure from the restrictive interpretation placed upon the FOIA by the House report,[27] the Attorney General's memorandum,[28] and the Ninth Circuit's decision in *Epstein*.[29] By accepting the Senate committee's interpretation[30] that the purpose of the FOIA is to enable the public to obtain access to the information necessary for it to deal effectively and upon an equal footing with federal agencies,[31] the instant court reasoned that the national security and foreign affairs secrets exemption is to be afforded a narrow and precise construction. The *Epstein* decision, by limiting judicial review of agency classifications to the question whether the agency acted arbitrarily or capriciously, severely undermined the effectiveness of the FOIA and increased the agencies' broad discretionary powers regarding disclosure.[32] In this case, however, the court recognized that it was congressional disapproval of broad agency discretion that led Congress to provide for de novo court review of agency determinations to withhold information; therefore the court limited agency discretion by construing the grant of de novo jurisdiction as encompassing the authority to resolve the issue whether an exemption applies under a particular factual setting. In exercising this jurisdiction, the court rendered the physically connected documents provision of Executive Order No. 10,501[33] a nullity by concluding that it was superseded and overruled by the FOIA. This action removes a significant basis upon which administrative officials have been able in the past to obtain blanket nondisclosure of a variety of matters under the national security and foreign affairs secrets exemption and is in keeping with the congressional attitude that the FOIA is not a withholding statute but rather a disclosure statute.[34]

The decision in the instant case is socially desirable because it encourages a policy of full public disclosure that serves to check possible administrative abuses of power. The court's analysis, however, failed to establish a structural approach that could be utilized by administrative officials and courts for evaluating future requests for disclosure of information which arguably could come within the national security and foreign affairs secrets exemption. The court did firmly establish that

27. H.R. REP. No. 1497, *supra* note 20.
28. DEP'T OF JUSTICE, *supra* note 21, at 30.
29. 421 F.2d 930 (9th Cir. 1970).
30. S. REP. No. 813, *supra* note 19.
31. *See* Davis, *The Information Act: A Preliminary Analysis*, 34 U. CHI. L. REV. 761 (1967).
32. Hoerster, *The 1966 Freedom of Information Act—Early Judicial Interpretations*, 44 WASH. L. REV. 641 (1969).
33. 3 C.F.R. § 292 (Supp. 1971).
34. *See* S. REP. No. 813, *supra* note 19.

unclassified documents physically connected to classified documents may not be withheld, but failed to decide the more difficult question whether and to what extent courts may question the classification and withholding of information under an executive order requesting that specific material be kept secret in the interest of national security or foreign policy. If the grant of de novo jurisdiction to federal district courts is to be truly significant, it must incorporate the unrestricted power to evaluate whether a particular exemption, including the national security exemption, may be invoked appropriately in a given situation. Rather than adhere to a technical interpretation of the wording of the nine exemptions, as has been done heretofore, the courts should evaluate administrative decisions that refuse disclosure by balancing the interest of the individual and the public at large in acquiring the information against the interest of the government in nondisclosure.[35] In conducting such an evaluation, the courts should consider the particular nature of the agency concerned, the mischief to which the exemption is directed, the specific record involved, and the fact that the FOIA places the burden of proving that nondisclosure is appropriate on the agency.[36] Few individual citizens have the financial resources and time to file suit against an agency under the FOIA; consequently, unless the judiciary, the executive, and the legislative branches cooperate to create an atmosphere of openness throughout the government,[37] most bureaucrats simply will ignore the disclosure requirements of the FOIA when dealing with individual citizens. Although this decision supports and strengthens the policy of full disclosure, the goal of a truly free and knowledgeable electorate will not be attained while the executive has the unfettered discretion to deny disclosure whenever such action is believed to be in the interest of the national security.

35. *See* Davis, *supra* note 31, at 765.

36. *See* Hoerster, *supra* note 32.

37. Nader, *Freedom From Information: The Act and the Agencies*, 5 HARV. CIV. RIGHTS—CIV. LIB. L. REV. 1 (1970).

Antitrust—Treble Damage Class Actions—Privity with Defendant Required To Maintain Suit

Plaintiff, City of Denver, alleging that defendant asphalt manufacturers had conspired to overprice asphalt, brought a class action seeking treble damages[1] for violation of section 1 of the Sherman Act.[2] Plaintiff purported to represent a class composed of itself and all other governmental entities in the State of Colorado that either directly or indirectly had purchased asphalt from defendants. Defendants argued that the Supreme Court's recent rejection of the passing-on defense[3] implied a requirement of privity between the complainant and the alleged conspirators before an action for antitrust violations could be maintained. Because only a small number of the proposed class members possessed this privity,[4] defendants contended that joinder of these remaining parties would be more practicable than maintenance of the suit as a class action.[5] Pursuant to Federal Rule 23(c),[6] the District Court for the District of Colorado, *held*, judgment for defendants. The abolition of the passing-on defense creates a requirement that privity exist between the plaintiff and the alleged antitrust violator before an action for treble damages may be maintained under section 4 of the Clayton Act. *City & County of Denver v. American Oil Co.*, 53 F.R.D. 620 (D. Colo. 1971).

Section 4 of the Clayton Act[7] provides a treble damage remedy for those injured as a result of any violation of the antitrust laws. Because the language and the legislative history of the Act suggests that the only

1. "Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue . . . and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee." Clayton Act § 4, 15 U.S.C. § 15 (1970), *formerly* Sherman Act § 7, ch. 647, § 7, 26 Stat. 210 (1890).

2. "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States . . . is declared to be illegal . . . ." Sherman Act § 1, 15 U.S.C. § 1 (1970).

3. *See* Hanover Shoe, Inc. v. United Shoe Mach. Corp., 392 U.S. 481 (1968). *See also* text accompanying notes 16-20 *infra*.

4. The proposed class was to include 126 governmental agencies, of which it was estimated that less than 10 had purchased asphalt directly from the named defendants.

5. FED. R. CIV. P. 23(a)(1) requires that "the class [be] so numerous that joinder of all members is impracticable." FED. R. CIV. P. 23(b)(3) also was relevant to the defendants' argument. This rule requires that before an action may be maintained as a class action, it must appear "that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy."

6. "As soon as practicable after the commencement of an action brought as a class action, the court shall determine whether it is to be so maintained." FED. R. CIV. P. 23(c)(1).

7. 15 U.S.C. § 15 (1970). For the text of § 4 see note 1 *supra*.

prerequisite to the maintenance of this private action is a showing that an injury has been sustained,[8] the courts have had the burden of determining what will constitute a recognizable injury.[9] This task has been particularly difficult when the courts have had to treat multi-tiered transactions in which a seller, in violation of the antitrust laws, sells to an original purchaser, who in turn conveys the merchandise to a subsequent purchaser. These transactions raise the question of which purchaser has sustained the injury necessary to invoke section 4. Although early Senate debate emphasized the treble damage action as a remedy designed primarily for the ultimate consumer,[10] early Supreme Court pronouncements declared that, when an illegally excessive price was exacted, it was the immediate purchaser who sustained injury under the Act; that his claim accrued at the moment of the overcharge; and that the law did not reach into subsequent dispositions of the acquired property.[11] This position was somewhat modified, however, in the *Oil Jobber*

8. *See* 21 CONG. REC. 1767 (1890) (remarks of Senator George on the private remedy proposed in § 7 of the original Sherman bill); *id.* at 2615 (remarks of Senator Coke). Nowhere in the legislative history is the term "injury" defined. *Cf.* Pollock, *Standing To Sue, Remoteness of Injury, and the Passing-On Doctrine*, 32 A.B.A. ANTITRUST L.J. 5, 8-9 (1966); Comment, *Should "Injury" in Treble Damage Suits Be Redefined?*, 51 NW. U.L. REV. 141, 142 (1956). The Supreme Court has acknowledged the all-inclusive nature of the language of § 4: "The statute does not confine its protection to consumers, or to purchasers, or to competitors or to sellers. Nor does it immunize the outlawed acts because they are done by any of these. The Act is comprehensive in its terms and coverage, *protecting all who are made victims of the forbidden practices by whomever they may be perpetrated.*" Mandeville Island Farms, Inc. v. American Crystal Sugar Co., 334 U.S. 219, 236 (1948) (emphasis added; citations omitted). *See also* Radiant Burners, Inc. v. Peoples Gas Light & Coke Co., 364 U.S. 656, 660 (1961): "[T]o state a claim upon which relief can be granted under [§ 4], allegations adequate to show a violation and . . . that plaintiff was damaged thereby are all the law requires."

9. For a discussion of the closely related problem of standing in antitrust actions generally see Klingsberg, *Bull's Eyes and Carom Shots: Complications and Conflicts on Standing To Sue and Causation Under Section 4 of the Clayton Act*, 16 ANTITRUST BULL. 351 (1971); McGuire, *The Passing-On Defense and the Right of Remote Purchasers To Recover Treble Damages Under Hanover Shoe*, 33 U. PITT. L. REV. 177, 179-83 (1971); Pollock, *supra* note 8.

10. "An advance in price to the middlemen is not mentioned in the bill, for the obvious reason that no such advance would damnify them; it would rather be a benefit . . . . [W]hatever [price] he pays he receives when he sells, together with a profit on his investment . . . . The consumer, therefore . . . is the party necessarily damnified or injured." 21 CONG. REC. 1767 (1890) (remarks of Senator George). In determining the legislative intent behind the treble damage remedy in the Clayton Act, emphasis must be focused on the enactment of the Sherman Act, which was the first statute prescribing such a remedy. Although the language of § 4 of the Clayton Act differs from that used in § 7 of the Sherman Act, no change in the purpose of the remedy was intended in the second statute. *Cf.* 51 CONG. REC. 9164 (1914). *See also* H.R. REP. NO. 627, 63d Cong., 2d Sess., pt. 1, at 14 (1914) (dealing with § 5 of the later Act).

11. *E.g.*, Thomsen v. Cayser, 243 U.S. 66 (1917) (discriminatory rate structure in foreign shipping); Chattanooga Foundry & Pipe Works v. City of Atlanta, 203 U.S. 390 (1906) (excessive prices for iron pipes which were needed by city for its waterworks system). *See also* Adams v. Mills, 286 U.S. 397 (1932) (excessive charges for unloading railroad stock cars); Southern Pac. Co. v.

Cases,[12] which were a series of lower federal court decisions that denied recovery to immediate purchasers on the theory that a middleman who recoups his losses resulting from the alleged violation by exacting a higher price from his customers has not incurred injury within the meaning of section 4. This rationale became the basis of the "passing-on" defense, the theory being that a plaintiff is not injured when he has "passed-on" the allegedly excessive prices to the ultimate consumer. Shifting the emphasis from the compensatory effect to the deterrent effect of treble damage litigation on future violators,[13] subsequent decisions refused to follow the passing-on doctrine when no alternative right of action vested in the ultimate consumer.[14] Underlying these decisions was the apprehension that, if followed in these circumstances, the passing-on doctrine would effectively immunize the antitrust offender from the legal consequences of his violations. Moreover, the courts reasoned that if a windfall were to result, it was preferable for it to accrue to an innocent plaintiff than a guilty defendant.[15] Judicial dissatisfaction

Darnell-Taenzer Lumber Co., 245 U.S. 531 (1918) (reparation for excessive freight rates on hardwood lumber).

12. *See, e.g.*, Clark Oil Co. v. Phillips Petroleum Co., 148 F.2d 580 (8th Cir.), *cert. denied*, 326 U.S. 734 (1945) (margin of profit maintained by "passing-on" higher prices to customers); Northwestern Oil Co. v. Socony-Vacuum Oil Co., 138 F.2d 967 (7th Cir. 1943), *cert. denied*, 321 U.S. 792 (1944) (transfer of excessive prices inferred); Twin Ports Oil Co. v. Pure Oil Co., 119 F.2d 747 (8th Cir.), *cert. denied*, 314 U.S. 644 (1941) (failure to prove lessened profit margins). *See also* Miller Motors, Inc. v. Ford Motor Co., 252 F.2d 441 (4th Cir. 1958) (dicta); Wolfe v. National Lead Co., 225 F.2d 427 (9th Cir.), *cert. denied*, 350 U.S. 915 (1955) (dicta).

13. *See, e.g.*, Perma Life Mufflers, Inc. v. International Parts Corp., 392 U.S. 134, 136 (1968) ("a vital means for enforcing the antitrust policy of the United States"); Quemos Theatre Co. v. Warner Bros. Pictures, Inc., 35 F. Supp. 949, 950 (D.N.J. 1940) ("ancillary force of private investigators to supplement the Department of Justice"). *See also* Comment, *Proof Requirements in Anti-Trust Suits: The Obstacles to Treble Damage Recovery*, 18 U. CHI. L. REV. 130, 138 (1950). *But see* Parker, *Treble Damage Actions—A Financial Deterrent to Antitrust Violations?*, 16 ANTITRUST BULL. 483 (1971); Vold, *Are Threefold Damages Under the Anti-Trust Act Penal or Compensatory?*, 28 KY. L.J. 117 (1940). A maximum criminal penalty of $5,000 for each antitrust violation is provided in 15 U.S.C. § 21(*l*). There has been some advocacy for major increases in the fine so as to reduce reliance on § 4 as a deterrent to future violations. *Cf.* Pollock, *supra* note 8, at 38.

14. In Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co., 335 F.2d 203 (7th Cir. 1964), public utilities were permitted to recover for price fixing by manufacturers of electrical equipment, despite defendants' charges that these prices had been passed-on to the customers of the plaintiffs. An earlier decision, Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co., 315 F.2d 564 (7th Cir.), *cert. denied*, 375 U.S. 834 (1963), had denied the ultimate consumers of electricity standing to intervene in this action on the theory that the proximate cause of the consumers' injury was not the antitrust violation but the intervening actions of the public utilities. *Accord*, Atlantic City Elec. Co. v. General Elec. Co., 226 F. Supp. 59 (S.D.N.Y.), *interlocutory appeal denied*, 337 F.2d 844 (2d Cir. 1964).

15. *E.g.*, Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co., 335 F.2d 203, 209 (7th Cir. 1964).

with the doctrine culminated with *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*,[16] in which the Supreme Court held that, to have a prima facie case of injury, a buyer must show only that he has been charged an illegally excessive price and that he can identify the amount of the overcharge; when both of these are satisfied, a buyer can maintain a suit for treble damages under the antitrust laws. The Court reasoned that a suit by the merchandiser was the only practical means of preventing a guilty manufacturer from enjoying the "fruits of his illegality,"[17] because the ultimate consumers of retailed merchandise, although possibly vested with a legal cause of action, had little incentive to institute a lawsuit.[18] From this seemingly broad denunciation of the passing-on defense, the Court excepted those situations in which it can be shown that the direct purchaser resold the merchandise in issue at a predetermined percentage of profit, on a "cost-plus" basis.[19] Although *Hanover* helped to clarify the legal positions of immediate purchasers, the decision left unclear whether the presumption against the applicability of the passing-on defense creates the inverse presumption that, except in those limited "cost-plus" situations, the ultimate consumer has no enforceable claim against the same manufacturer. Addressing this issue in *Philadelphia Housing Authority v. American Radiator & Standard Sanitary Corp.*,[20] a federal district court held that in order to prevent multiple liability of the defendant, the presumption created by *Hanover* against passing-on by an immediate purchaser required a similar presumption that an ultimate consumer has not sustained the injury necessary to bring suit under section 4.[21] Accordingly, the court denied standing to individual homeowners in an action against the manufacturers of plumbing fixtures installed in plaintiffs' homes. In further support of its holding, the court reasoned that because of the number of transactions between the actual sale of the fixtures and the subsequent purchase of

16. 392 U.S. 481 (1968).

17. *Id.* at 489.

18. *Id.* at 494. It was reasoned further that to allow the defense would require the insuperable task of determining the extent of an alleged pass-on. *Id.* at 492-93.

19. This "cost-plus exception" was applied in West Virginia v. Chas. Pfizer & Co., 440 F.2d 1079 (2d Cir. 1971), in which the court held that retail and wholesale druggists resold antibiotics which had been illegally overpriced by the manufacturers at a fixed margin of profit, and, as such, the passing-on doctrine could be invoked in allocating a settlement award between druggists and consumers.

20. 50 F.R.D. 13 (E.D. Pa. 1970), *aff'd sub nom.*, Mangano v. American Radiator & Standard Sanitary Corp., 438 F.2d 1187 (3d Cir. 1971). *See also* Philadelphia Housing Authority v. American Radiator & Standard Sanitary Corp., 323 F. Supp. 381 (E.D. Pa. 1970) (public housing authority denied standing to sue on the same grounds).

21. 50 F.R.D. at 30.

the homes, it would be impossible to trace the excess charges to the ultimate purchasers.[22]

The instant court initially analyzed the prerequisites for the maintenance of a class action and determined that the practicability of maintaining the suit as a class action depended on a finding that questions of law and fact common to the proposed class predominate over any questions peculiar to individual class members.[23] To make a conclusive determination on this issue, the court reasoned that it was first necessary to ascertain defendants' section 4 liability to the proposed class members.[24] Addressing the question of liability, the court interpreted *Hanover* to mean that, whenever a direct purchaser brings suit under section 4, he will recover for his injuries so long as it cannot readily be shown that he has recouped his additional cost by passing it on to his customers on a cost-plus basis. The court recognized that to permit recovery by the ultimate consumer in non-cost-plus situations could result in multiple treble liability.[25] Moreover, the court expressed great concern for the difficulty of tracing an allegedly excessive price through a series of transactions to the ultimate consumer and for the immense burden such a process would place on the courts.[26] Accordingly, the court felt that certain limitations must be prescribed and, therefore, reasoned that *Hanover* not only created a presumption against use of the passing-on defense in suits instituted by direct purchasers, but that it also estab-

22. *Id.* at 25-26.

23. *See* materials cited note 5 *supra*.

24. "We do not disagree that the ultimate decision as to the standing/remoteness/pass-on issues must await development of the facts, but we believe that at least where the apparent facts are such as here exist, the factual differences among potential class members—differences affecting liability—should be recognized before a case is determined to be a class action. . . . Appropriate use of the discovery procedures should establish the essential facts as to the passing-on of the alleged improper charges, and the issue as to most potential class members may well become ripe for decision on motion for summary judgment. If a class action were to be determined to be appropriate at this time, the summary judgment route will be effectively barricaded before the court has a fair chance to look at a problem which may be dispositive of the case as to many members of the proposed class." 53 F.R.D. at 633.

25. "If the 'passing-on' defense is available to a defendant, he would be excused from liability to the first purchaser, and there would be no risk of double liability trebled, but if that defense is not available, to permit recovery by one who bought only indirectly would subject the manufacturer to possible multiple liahility trebled, and this we think goes beyond the policy of Congress in enacting the antitrust laws." *Id.* at 631.

26. "The difficulty in tracing any overcharge for asphalt into a completed job will vary from job to job. . . . [T]he claims of the class members and their right to recover will vary from potential class member to potential class member dependent upon the type of contract entered into by them—not contracts entered into with countless contractors whose bidding formulae will all be different. To try this case as a class action might be an accountant's paradise, but it would be a court's purgatory." *Id.* at 636-37.

lished a similar presumption that ultimate consumers had no standing to sue for excessive prices further up the chain of distribution. The court completed its treatment of *Hanover* by holding that the case implicitly set forth a requirement of privity of contract between the plaintiff and the antitrust violator before a suit for treble damages under section 4 of the Clayton Act could be maintained, except in the limited cost-plus situations. Turning back to the propriety of the instant class action, the court concluded that, since only a small number of the proposed class possessed the requisite privity with the alleged violators, maintenance of a class action would be less practicable procedurally than a joinder of the injured parties.[27]

The private cause of action created by section 4 of the Clayton Act serves two pronounced functions: the redress of injury and the enforcement of the antitrust provisions. The instant court's insistence on privity between a purchaser of overpriced goods and the antitrust violator raises a number of questions relating to the furtherance of each of these two functions. By imposing the requirement of privity before a suit may be entertained under section 4, the court has obscured a major policy recognized by court decisions, including *Hanover*, since the inception of the Act: the need to promote private treble damage actions as an effective supplement to the Justice Department's enforcement of the antitrust laws of the United States.[28] The importance of this enforcement facet of the private remedy is suggested by the unprecedented growth of treble damage actions during the decade of the 1960's.[29] Imposition of a privity requirement effectively forecloses most ultimate consumers from bringing suit under section 4 and increases the opportunities for the antitrust offender to avoid civil liability. The possibility that such violations will not be legally scrutinized is greatly enhanced by the likelihood that many immediate purchasers—those possessing the requisite privity—may feel compelled to forego their claims in order to avoid jeopardizing long-standing, and often quite valuable, business relations with the defendant.[30] Thus, reliance on the broad concept of privity of contract must

27. The court designed "a rather loose intervention procedure" to afford those indirect purchasers claiming under a cost-plus purchasing agreement to intervene individually in the suit. The direct purchasers, of course, were joined automatically.

28. *See* cases and materials cited note 13 *supra*.

29. The number of private suits filed under § 4—excluding the electrical equipment industry cases—have been reported by year as follows: 1960, 228; 1961, 341; 1962, 266; 1963, 283; 1964, 317; 1965, 443; 1966, 444; 1967, 536; 1968, 659; 1969, 740. Parker, *supra* note 13, at 483 n.3. Parker suggests that the increase may reflect an increase in the number of violations rather than any increased awareness of relief through private antitrust litigation. *Id.* at 484.

30. 547 BNA ANTITRUST & TRADE REG. REP., No. 547, at B-3 (Jan. 25, 1972) (analysis of instant case).

be limited severely, or preferably disallowed on the appellate level, in order to promote the enforcement function of section 4. Moreover, the conclusion that a requirement of privity was implicit in *Hanover* is untenable and violative of the spirit of that decision. Admittedly, the High Court did express concern for the difficulty of tracing illegally excessive prices to the ultimate consumer, a position with which the instant court appears to be obsessed, but it must be recognized that it did so in the context of preventing a defendant from escaping liability by his arguing that the excessive prices injured more remote purchasers than the plaintiff. When this fact is examined along with the *Hanover* Court's express doubts that the ultimate consumers would bring suit, it becomes apparent that the Court was concerned primarily with preventing the alleged violator from profiting from his illegal activity without bearing the attendant legal consequences.[31] Furthermore, it cannot be overlooked that section 4 had the additional purpose of remunerating those injured.[32] To believe that the ultimate consumer is never injured, except in those situations involving a cost-plus operation, is an exercise in fiction. By adopting such an attitude, the instant court is dealing with extremes—discounting the probability that many pass-on situations are not complete, with both parties absorbing a share of defendant's injurious practices. Thus reason and policy considerations dictate that the cost-plus situation not be interpreted as the exclusive exception to *Hanover* but merely as an example of those instances in which proof of a partial or complete pass-on would not be overly taxing.[33] Also, the fact that *Hanover* did not expressly preclude a suit by the ultimate consumer, but merely elicited doubt that such an action would be maintained, intimates that the Court recognized that such an action could be brought. Moreover, this disbelief that a suit by the ultimate purchasers would be instituted has been dissipated greatly by the growth of consumer actions since the decision in *Hanover*,[34] and could be dissipated even more by a liberal allowance of *parens patriae* suits by the states on behalf of their consuming citizenry.[35] Thus rather than prescribing a

31. *See* text accompanying notes 17-18 *supra*.

32. *See* materials cited note 8 *supra*.

33. "[T]here might be situations—for instance, when an overcharged buyer has a pre-existing 'cost-plus' contract *thus making it easy to prove that he has not been damaged*—when the considerations requiring that the passing-on defense not be permitted . . . would not be present." Hanover Shoe, Inc. v. United Shoe Mach. Corp., 392 U.S. 481, 494 (1968) (emphasis added).

34. *Cf.* Handler, *The Shift from Substantive to Procedural Innovations in Antitrust Suits—The Twenty-Third Annual Antitrust Review*, 71 COLUM. L. REV. 1, 6 (1971).

35. McGuire, *supra* note 9, at 196 & n.63. The *parens patriae* action has not met with a favorable response. *See, e.g.*, Hawaii v. Standard Oil Co., 301 F. Supp. 982, 986, 988 (D. Hawaii

conclusive rule that lacks the flexibility needed for the courts to adjudicate fairly the many diversified factual situations presented by antitrust actions, a far better rule would be to decide this question on a case-by-case basis, with some discretionary power vested in the district court to determine when the problem of ascertaining the ultimate consumers' injuries becomes so insurmountable that no section 4 suit should be maintained.[36] To the extent that the instant decision involved such a finding, it is palatable; it is the privity language with its far-reaching effects that is a source of concern. Finally, the instant court's compromise of the deterrent and retributive functions of private treble damage actions in order to eliminate a defendant's risk of multiple liability, although understandable in light of the general confusion of substantive and procedural law that besets the courts' decisions in this area,[37] was unnecessary, for the threat of multiple liability can be diminished greatly through the proper employment of procedural devices. One such mechanism would be for the antitrust defendant to move to join both the immediate and subsequent purchasers in the same action under Federal Rule 19 as indispensable parties.[38] Of course, the feasibility of this procedure will depend on whether the parties to be joined are subject to service of process by the court and whether such a joinder would deprive the court of subject matter jurisdiction.[39] An alternative method would be for the defendant to consolidate the claims of all the parties into a single action by means of interpleader.[40] This method, however, is not without

1969), *rev'd on other grounds*, 431 F.2d 1282 (9th Cir. 1970), *aff'd*, 40 U.S.L.W. 4246 (U.S. Mar. 1, 1972); Philadelphia Housing Authority v. American Radiator & Standard Sanitary Corp., 309 F. Supp. 1057, 1061 (E.D. Pa. 1969). *But cf.* West Virginia v. Chas. Pfizer & Co., 440 F.2d 1079, 1089 (2d Cir. 1971) (dicta). For a general discussion of the need for more *parens patriae* suits under the antitrust laws see Comment, *Wrongs Without Remedy: The Concept of Parens Patriae Suits for Treble Damages Under the Antitrust Laws*, 43 S. CAL. L. REV. 570, 592-93 (1970).

36. *Cf.* McGuire, *supra* note 9, at 203.

37. *See* materials cited note 9 *supra*.

38. McGuire, *supra* note 9, at 201-02.

39. FED. R. CIV. P. 19(a) provides: "A person who is subject to service of process and whose joinder will not deprive the court of jurisdiction over the subject matter of the action shall be joined as a party in the action if (1) in his absence complete relief cannot be accorded among those already parties, or (2) he claims an interest relating to the subject of the action and is so situated that the disposition of the action in his absence may (i) as a practical matter impair or impede his ability to protect that interest or (ii) leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of his claimed interest. . . ."

40. McGuire, *supra* note 9, at 197-98; Comment, *The "Passing-On" Defense in Treble Damage Antitrust Suits*, 1969 U. ILL. L.F. 377, 387; Note, *The Defense of "Passing-On" in Treble Damage Suits Under the Antitrust Laws*, 70 YALE L.J. 469, 479 n.66 (1961). Because FED. R. CIV. P. 22 requires complete diversity before the interpleader can be used, it would have minimal application in this area. As a result, courts would need to rely most often on statutory inter-

its drawbacks since the defendant may not be willing or able to deposit with the courts the large stakes generally associated with section 4 actions;[41] furthermore, such a move may be tantamount to an admission of liability by the moving defendant.[42] A final method could be for the courts to hold any award in escrow, under a modified constructive trust theory, for a statutorily determined length of time, with the award subject to diminution by the claims of interested parties who were absent in the litigation against the antitrust defendant.[43] Admittedly, none of these suggestions is without its flaws, but the adoption of this type of procedural framework would have the advantage of preventing multiple liability *without* sacrificing the ultimate consumers' right to be compensated for any injuries they have sustained as a result of a defendant's antitrust violation, and *without* diminishing the enforcement benefits inherent in section 4 litigation.

Constitutional Law—Eqnal Protection—State Probate Code Discriminating in Favor of Males Violates Equal Protection Clanse

Appellant and appellee, respectively mother and father of the deceased minor, filed competing petitions in county probate court, each seeking appointment as administrator of the child's estate. The probate court awarded letters of administration to the father pursuant to a provision of the Idaho probate code[1] that gave a mandatory preference to men over women when members of the same entitlement class apply for appointment as administrator of a decedent's estate.[2] Appellant con-

pleader—28 U.S.C. § 1335 (1970). Complete diversity was abolished as a requirement for statutory interpleader by the Supreme Court in State Farm Fire & Cas. Co. v. Tashire, 386 U.S. 523 (1967).

41. McGuire, *supra* note 9, at 197-98; Note, *supra* note 40, at 479 n.66.

42. Note, *supra* note 40, at 479 n.66.

43. "A constructive trust arises when a person who holds title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it." 5 A. SCOTT, LAW OF TRUSTS § 462 (3d ed. 1967).

1. IDAHO CODE § 15-312 (1947) designates the persons who are entitled to administer an intestate's estate by means of a priority ranking based upon relationship to the deceased. The third group listed is the "father or mother." Section 15-314 further provides that "[o]f several persons claiming and equally entitled [under § 15-312] to administer, males must be preferred to females, and relatives of the whole to those of the half blood."

2. On March 12, 1971, the Idaho Legislature adopted the Uniform Probate Code, effective July 1, 1972. Once the new code is in effect §§ 15-312 and 15-314 of the present code effectively will be repealed; no provision in the new legislation gives a mandatory preference to males over females as administrators of estates.

tended that the statutory provision favoring men over women violated the equal protection clause of the fourteenth amendment. Agreeing with appellant, the state district court held that the challenged section unconstitutionally discriminated against women and was therefore void. The Idaho Supreme Court reversed the district court and reinstated the original order naming the father as administrator of the estate. On appeal to the Supreme Court of the United States, *held*, reversed. The granting of a mandatory preference to men over women, when both are members of the same entitlement group applying for appointment as administrator of a decedent's estate, violates the equal protection clause of the fourteenth amendment. *Reed v. Reed*, 404 U.S. 71 (1971).

In recognition of the respective roles historically performed by man and woman within the family, English common law merged many of the procedural and substantive rights of the wife into those of the husband.[3] The resulting female disabilities, like other vestiges of the common law, frequently were assimilated into the laws of this country and persist today in many fields.[4] Changes in the style of life resulting from modern technology, communication, and education, however, have caused a re-

3. 1 W. BLACKSTONE, COMMENTARIES 445.

4. A March 1970 memorandum of the Citizens' Advisory Council on the Status of Women lists 15 specific areas of sex discrimination:

"1. State laws placing special restrictions on women with respect to hours of work and weightlifting on the job;

2. State laws prohibiting women from working in certain occupations;

3. Laws or practices operating to exclude women from State colleges and universities (including higher standards required for women applicants to institutions of higher learning and in the administration of scholarship programs);

4. Discrimination in employment by State and local governments;

5. Dual pay schedules for men and women public school teachers;

6. State laws providing for alimony to be awarded, under certain circumstances, to ex-wives but not to ex-husbands;

7. State laws placing special restrictions on the legal capacity of married women or their capacity to establish a legal domicile;

8. State laws that require married women but not married men to go through formal procedure and obtain court approval before they may engage in an independent business;

9. Social Security and other social benefits legislation which give greater benefits to one sex than the other;

10. Discriminatory preferences, based on sex, in child custody cases;

11. State laws providing that the *father* is the natural guardian of minor children;

12. Different ages for males and females in (a) child labor laws, (b) age for marriage, (c) cutoff of the right to parental support, and (d) juvenile court jurisdiction;

13. Exclusion of women from the requirements of the Military Selective Service Act of 1967;

14. Special sex-based exemptions for women in selection of State juries;

15. Heavier criminal penalties for female offenders than for male offenders committing the same crime."

116 CONG. REC. 9685 (1970). *See also* Note, *Sex, Discrimination, and the Constitution*, 2 STAN. L. REV. 691 (1950).

evaluation of the societal roles traditionally attributed to man and woman. Laws that discriminate on the basis of sex are now regarded by many as anachronistic barriers, depriving women of the free exercise of certain rights enjoyed by men.[5] Although the advent of female suffrage[6] and the inclusion of sex as an equal employment opportunity classification under Title VII of the 1964 Civil Rights Act[7] represent significant legislative progress in the quest for the legal equality of women, the courts have remained unwilling to proclaim the absolute equality of the sexes.[8] Early decisions reveal underlying social and legal attitudes that continue to constitute the basis for judicial reluctance. Concurring in an 1872 Supreme Court decision[9] denying a license to practice law to a woman, Justice Bradley stated that the "constitution of the family organization, which is founded in the divine ordinance, as well as in the nature of things, indicates the domestic sphere as that which properly belongs to the domain and functions of womanhood."[10] In *Muller v. Oregon*,[11] the High Court in 1908 brought this early social position into a legal context and in dicta established the principle that sex is a valid basis for classification.[12] Subsequent judicial reliance upon this language without regard for the purpose of the statute in question or the reasonableness of the classification has substantially stymied challenges of sex-based discrimination on equal protection grounds.[13] Although the fourteenth amendment prohibits arbitrary, unreasonable discrimination, a

5. *See* L. KANOWITZ, WOMEN AND THE LAW (1969); Brown, Emerson, Falk, & Freedman, *The Equal Rights Amendment: A Constitutional Basis for Equal Rights for Women*, 80 YALE L.J. 871 (1971); Cavanaugh, *"A Little Dearer Than His Horse:" Legal Stereotypes and the Feminine Personality*, 6 HARV. CIV. RIGHTS-CIV. LIB. L. REV. 260 (1971); Crozier, *Constitutionality of Discrimination Based on Sex*, 15 B.U.L. REV. 723 (1935); Gilbertson, *Women and the Equal Protection Clause*, 20 CLEV. ST. L. REV. 351 (1971); Johnston & Knapp, *Sex Discrimination by Law: A Study in Judicial Perspective*, 46 N.Y.U.L. REV. 675 (1971); Kanowitz, *Constitutional Aspects of Sex-Based Discrimination in American Law*, 48 NEB. L. REV. 131 (1968); Murray & Eastwood, *Jane Crow and the Law: Sex Discrimination and Title VII*, 34 GEO. WASH. L. REV. 232 (1965); Seidenberg, *The Submissive Majority: Modern Trends in the Law Concerning Women's Rights*, 55 CORNELL L. REV. 262 (1970); *Developments in the Law—Employment Discrimination and Title VII of the Civil Rights Act of 1964*, 84 HARV. L. REV. 1109 (1971); Note, *Sex Discrimination and Equal Protection: Do We Need a Constitutional Amendment?*, 84 HARV. L. REV. 1499 (1971); Note, *Sex, Discrimination, and the Constitution*, 2 STAN. L. REV. 691 (1950).

6. U.S. CONST. amend. XIX.

7. Civil Rights Act of 1964, §§ 701-16, 42 U.S.C. §§ 2000e to -15 (1970).

8. *See* Johnston & Knapp, *supra* note 5.

9. Bradwell v. Illinois, 83 U.S. (16 Wall.) 130 (1872).

10. *Id.* at 141 (Bradley, J., concurring).

11. 208 U.S. 412 (1908) (upheld statute limiting work by women to 10 hours a day).

12. *See id.* at 421-23.

13. *See, e.g.*, Goesaert v. Cleary, 335 U.S. 464 (1948) (upheld statute denying women a bartender's license).

state ordinarily can support the constitutionality of a classificatory statute by showing that the divisions created bear a "rational relationship" to a legitimate state objective.[14] When "suspect classifications" such as race[15] or national ancestry,[16] or "fundamental interests" such as voting[17] or procreation[18] are involved, however, much stricter judicial scrutiny is imposed. In such cases, the burden is placed upon the state to show a compelling state interest in support of the discriminatory statute.[19] Although sex-based classifications have been held invalid under the equal protection clause by several state and federal courts,[20] the progress in overcoming the broad language in *Muller* has been slow. The less demanding rational connection test was applied in most of these cases, but at least two decisions[21] have held that sex is a suspect classification and have imposed the stricter compelling state interest standard. Despite this activity by lower courts, the Supreme Court has never held any form of sex discrimination to violate the equal protection guarantee. In fact, the Court in a recent decision summarily upheld, against an equal protection challenge, South Carolina's right to operate a sex-segregated college.[22] The Court's continued willingness to examine the problem of sex-based discrimination, however, was evidenced by its agreement to hear several cases in which the issue was directly presented.[23]

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14. *See, e.g.*, McGowan v. Maryland, 366 U.S. 420 (1961) (upheld statute prohibiting the sale of certain articles on Sunday); Goesaert v. Cleary, 335 U.S. 464 (1948) (upheld statute denying women a bartender's license).

15. *E.g.*, McLaughlin v. Florida, 379 U.S. 184 (1964) (invalidated statute prohibiting cohabitation by an unmarried interracial couple).

16. *E.g.*, Korematsu v. United States, 323 U.S. 214 (1944) (imposed strict scrutiny on order relocating Japanese-Americans during World War II).

17. *E.g.*, Harper v. Virginia Bd. of Elections, 383 U.S. 663 (1966) (held Virginia's poll tax unconstitutional).

18. *E.g.*, Skinner v. Oklahoma *ex rel.* Williamson, 316 U.S. 535, 541 (1942) (invalidated statute providing for sterilization of habitual criminals).

19. *See Developments in the Law—Equal Protection*, 82 HARV. L. REV. 1065, 1087 (1969). For a critical appraisal of the expanding application of the compelling state interest standard see Shapiro v. Thompson, 394 U.S. 618, 655 (1969) (Harlan, J., dissenting). *See generally* Tussman & tenBroek, *The Equal Protection of the Laws*, 37 CAL. L. REV. 341 (1949).

20. *See, e.g.*, Kirstein v. University of Va., 309 F. Supp. 184 (E.D. Va. 1970) (recognized right of women to attend University of Virginia at Charlottesville); Seidenberg v. McSorleys' Old Ale House, Inc., 308 F. Supp. 1253 (S.D.N.Y. 1969) (upheld right of women to patronize bar formerly catering only to men); Commonwealth v. Daniel, 430 Pa. 642, 243 A.2d 400 (1968) (struck down unequal criminal sentencing for men and women).

21. United States *ex rel.* Robinson v. York, 281 F. Supp. 8 (D. Conn. 1968) (applied strict scrutiny to difference in criminal sentencing based upon sex); Sail'er Inn, Inc. v. Kirby, 5 Cal. 3d 1, 485 P.2d 529, 95 Cal. Rptr. 329 (1971) (upheld hiring of women bartenders at state-licensed bars).

22. Williams v. McNair, 316 F. Supp. 134 (D.S.C. 1970), *aff'd mem.*, 401 U.S. 951 (1971).

23. In addition to the present case, the Supreme Court recently has granted certiorari in 2 other state court cases involving sex discrimination: *In re* Stanley, 45 Ill. 2d 132, 256 N.E.2d 814

In the instant case, the Supreme Court observed that the provision of the Idaho probate code according different treatment to potential administrators on the basis of sex established a classification subject to inspection under the equal protection clause.[24] Writing for a unanimous Court, Chief Justice Burger noted that the fourteenth amendment does not deny states the power to treat different classes of persons in different ways. The classification, however, must be reasonable, not arbitrary, and must be based upon some difference that has a substantial relation to the purpose of the legislation. Recognizing that the reduction of the workload of probate courts is a legitimate state objective, the Court nevertheless ruled that persons within a given entitlement class are similarly situated with respect to that objective, regardless of sex. The High Court further announced that the difference in sex of competing applicants for letters of administration did not bear a rational relationship to the state purpose that was sought to be advanced. The Court, therefore, concluded that a statute which gives preference to men over women when persons of the same entitlement class apply for appointment as administrator of a decedent's estate is based solely on an arbitrary discrimination prohibited by the equal protection clause of the fourteenth amendment.

The instant decision, as the first case in which the Supreme Court squarely has held that sex-based discrimination violates the equal protection clause, is a significant landmark in the developing interpretation of the fourteenth amendment. In some respects, however, the ruling represents only a qualified victory for proponents of legal equality between the sexes. The opponents of the proposed equal rights amendment,[25] for example, can use the decision as support for their contention that the guarantee embodied in the equal protection clause makes such an amendment unncessary. More important is the Court's failure to include sex as a suspect classification. Choosing to apply the less demanding rational connection test, the Court declined to afford sex-based discrimi-

(1970), *cert. granted sub nom.* Stanley v. Illinois, 400 U.S. 1020 (1971) (involving alleged discrimination against the male parent in awarding custody of illegitimate children); State v. Alexander, 255 La. 941, 233 So. 2d 891 (1970), *cert. granted*, 401 U.S. 936 (1971) (involving a claim that females were systematically excluded from the grand jury which returned a rape indictment against defendant, a male Negro).

24. The application of the equal protection clause to instances of statutory classification is thoroughly examined by Tussman & tenBroek, *supra* note 19.

25. A version of the proposed amendment ensures that equality of rights under the law shall not be denied or abridged by the United States or by any state on account of sex. H.R.J. Res. 11, 89th Cong., 1st Sess. § 1 (1965); S.J. Res. 85, 89th Cong., 1st Sess. § 1 (1965). For a discussion of the proposed amendment see Brown, Emerson, Falk, & Freedman, *supra* note 5; Note, *Sex Discrimination and Equal Protection: Do We Need a Constitutional Amendment?*, *supra* note 5.

nation equal status with discrimination based upon race. A comparison between sex and race as a criterion for classification, however, reveals similarities that support the inclusion of sex as a suspect classification. Both sex and race define large, readily identifiable classes whose members are immutably determined by accident of birth. Both classes are subject to certain group stereotypes drawn from imputed characteristics that, although inapplicable to many individual members of the group, nonetheless have been employed to endorse discriminatory treatment for the entire class. The falsity of certain racial stereotypes has been widely recognized in recent years, and women similarly have demonstrated that many of the characteristics attributed to females as a class are without basis in fact. To the extent that women perform maternal functions, they are physiologically different from men and society has an obvious interest in the protection of this vital role. Nevertheless, courts have been reluctant to recognize that many women choose not to become wives and mothers[26] and, more importantly, that neither the status of "wife" nor the status of "mother" has a functional basis after the birth of the child. Individuals should not be denied equal opportunity for personal achievement by overbroad laws based upon a stereotyped conception of "womanhood." An expanded application of the equal protection clause or a constitutional amendment prohibiting sex-based discrimination would not preclude legislative protection of woman's role as childbearer, as some opponents contend. Either, however, would require a shift of emphasis from the class attributes of womanhood to the *functional* attributes of individuals.[27] Laws recognizing functions, *if being performed*, rather than sex per se would permit legal protection of mothers and homemakers while granting equal professional and personal opportunity to women who choose careers outside the home. Even if no constitutional change is ratified, a reappraisal of sex discrimination under the fourteenth amendment resulting in a judicial inclusion of sex as a suspect classification undoubtedly would affect various existing laws. Alimony based upon sex would not be permitted, but instead would be determined by an examination of the relative income of the two parties. State labor standards would have to apply equally to men and women. Both sexes also would be subject to compulsory military service and jury duty, but exemptions could be made for certain activities, such as child care and parenthood, if based on performance of the function rather than sex. In

26. Women made up 38% of the labor force in 1971. U.S. DEP'T OF LABOR, WOMEN WORKERS TODAY 1 (1971).

27. For a discussion of the functional aspect of classification see Murray & Eastwood, *supra* note 5, at 239.

this respect, the present decision represents the initial step toward recognition by the Supreme Court that the equal protection clause authorizes classification by sex only when inherent sexual attributes bear a rational functional relationship to the state objective.

Constitutional Law—Federal Pre-emption—Atomic Euergy Act Requires Exclusive Federal Regulation of Radioactive Discharges from Nuclear Power Plauts

Plaintiff, a nuclear power producer located in Minnesota, sought a declaratory judgment that defendant, the state of Minnesota, had no authority to regulate the release of radioactive waste materials from plaintiff's nuclear power plant.[1] Minnesota's regulations were more stringent than those imposed by the federal government, and plaintiff contended that the development and utilization of atomic power demanded uniform policies and controls that could not be accomplished without exclusive federal regulation.[2] Plaintiff further maintained that Congress intended the Atomic Energy Act[3] to vest, and that the Act did in fact vest, exclusive control over the construction and operation of nuclear facilities in the Atomic Energy Commission (AEC). Minnesota asserted, however, that the Act did not pre-empt a state's authority to regulate the discharge of radioactive waste materials within its own borders. Relying on the tenth amendment to the Constitution,[4] Minne-

1. Both parties agreed that there were no disputed factual issues and stipulated the following facts: (a) the Atomic Energy Commission issued a provisional permit to plaintiff in June, 1967, pursuant to 42 U.S.C. § 2134(b) (1970) and the regulations contained in 10 C.F.R. § 50 (1971), authorizing construction of a nuclear power plant located on the Mississippi River near Monticello, Minnesota; (b) the Minnesota Pollution Control Agency issued a waste disposal permit on May 20, 1969, subject to state controls regulating the radioactive level of liquid and gaseous discharges; (c) on January 19, 1971, the AEC issued to plaintiff a provisional operating license under which the Monticello plant is currently operating; (d) plaintiff is acting in compliance with all federal laws and requirements and it is not physicially impossible to comply with both state and federal regulations. The Minnesota regulations, although embracing the same area as the federal regulations, are substantially more stringent; and (e) the Governor of Minnesota and the AEC have not entered into any agreement pursuant to 42 U.S.C. § 2021(b) (1970) that would allow Minnesota to assume regulatory powers in controlling atomic energy.

2. Plaintiff also contended that any state regulation could lead to abuse and be detrimental to the efforts of the AEC to promote the construction and operation of nuclear power plants. As an overly protective reaction against the dangers presented by atomic energy utilization, states might enact extremely strict regulations in order to preclude the use of nuclear reactors.

3. 68 Stat. 921-61 (1954), *as amended*, 42 U.S.C. §§ 2011-2296 (1970).

4. "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." U.S. CONST. amend. X.

sota urged that, since pollution control is essential to the health and safety of its citizens, Minnesota should have authority to regulate such pollution under its police powers. The federal district court concluded that federal legislation pre-empted even concomitant state regulation,[5] and on appeal, the Eighth Circuit Court of Appeals, *held*, affirmed. The Atomic Energy Commission has exclusive power to regulate radioactive waste releases from nuclear power plants. *Northern States Power Co. v. Minnesota*, 447 F.2d 1143 (8th Cir. 1971).

Before Congress can pre-empt a state from exercising authority over a field of regulation and grant exclusive regulatory control to the federal government, the power to so act must be specifically delegated to Congress by the Constitution.[6] In the absence of an express constitutional delegation, the tenth amendment reserves to the states the power to regulate.[7] Notwithstanding these clear guidelines, conflicts have arisen when both state and federal governments assert jurisdiction over the same subject matter based upon separate and distinct acts of sovereignty.[8] The Atomic Energy Act of 1946,[9] for example, authorized complete federal pre-emption of the nuclear energy field by granting the AEC exclusive control over the production and use of fissionable materials.[10] States have also sought to regulate, as necessary to the health and safety of their citizens, the intrastate discharge of pollutants.[11] Although the

5. Northern States Power Co. v. Minnesota, 320 F. Supp. 172 (D. Minn. 1970).

6. Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 229-30 (1947). *See also* Helman, *Pre-emption: Approaching Federal-State Conflict over Licensing Nuclear Power Plants*, 51 MARQ. L. REV. 43 (1967).

7. U.S. CONST. amend. X. When there is a specific delegation, however, the supremacy clause of the Constitution is the basis for federal pre-emption. The supremacy clause provides: "This Constitution and the Laws of the United States which shall be made in Pursuance thereof; and all treaties made, or which shall be made, under authority of the United States, shall be the supreme law of the Land, and the Judges in every state shall be bound thereby, anything in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. CONST. art. VI, § 2. *See* Estep, *Federal Control of Health and Safety Standards in Peacetime Private Atomic Energy Activities*, 52 MICH. L. REV. 333 (1954).

8. *See, e.g.*, Huron Portland Cement Co. v. City of Detroit, 362 U.S. 440 (1960) (municipality's regulation of smoke emission from ships engaged in interstate commerce to protect health and welfare of its citizens challenged on basis of federal pre-emption of regulating interstate commerce); South Carolina State Highway Dep't v. Barnwell Bros., 303 U.S. 177 (1938) (regulation of weight of vehicles using state highways as an exercise of police power to protect state roads challenged by interstate truckers on basis that only Congress could regulate interstate commerce).

9. Act of Aug. 1, 1946, ch. 1073, 60 Stat. 755.

10. The AEC controlled the mining of certain radioactive source material, and owned all of the facilities that produced fissionable materials and all of the radioactive material produced. Atomic Energy Act of 1946, ch. 1073, §§ 5(a)(1), 5(a)(2), 5(b)(1), 60 Stat. 755.

11. *See, e.g.*, ALA. CODE tit. 22, §§ 346-51 (Supp. 1969) (Solid Waste Disposal Act); CONN. GEN. STAT. ANN. §§ 19-505 to -522 (Supp. 1969) (Connecticut Air Pollution Control Act); MISS. CODE ANN. §§ 7106:111-:136, :141-:144 (Supp. 1971) (Mississippi Air and Water Pollution Control Act); R.I. GEN. LAWS ANN. §§ 23-25-1 to -22 (1968) (Rhode Island Clean Air Act).

Supreme Court has acknowledged that it is the function of the judiciary to resolve disputes arising out of such overlapping regulation,[12] no single formula has been found appropriate for all cases. In *Florida Lime and Avocado Growers v. Paul*,[13] the Court held that, when the state enactment was inconsistent with federal objectives, a state could only act up to the point of actual conflict with federal authority. In other cases,[14] the Court recognized an express congressional declaration that the authority conferred would be exclusive as pre-emptive of any state concomitant or supplementary regulatory power. Even in the absence of an express prohibition against dual regulation, however, some cases have implied federal pre-emption.[15] In determining the propriety of implied pre-emption, courts have examined the aim and intent of the statute in question,[16] the pervasiveness of the regulatory scheme[17] and the need to achieve uniformity,[18] and the state law's position as a possible obstacle to the purposes and objectives of Congress.[19]

In recent years, the conflict between federal and state control of nuclear power production has become increasingly difficult to resolve. The AEC periodically has relinquished parts of its absolute control over the operation of nuclear facilities, and states have become more actively

12. Hines v. Davidowitz, 312 U.S. 52, 67 (1941) (a court's function is to determine and implement the full purpose and objectives of Congress).

13. 373 U.S. 132 (1963).

14. Campbell v. Hussey, 368 U.S. 297, 302 (1961) (state and federal concomitant regulation of tobacco grades prohibited by Congress' declaring that control should be left to the federal government); Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 235-36 (1947) (concomitant regulation of grain warehouses rejected by finding contrary congressional intent).

15. Bethlehem Steel Co. v. New York State Labor Relations Bd., 330 U.S. 767, 772 (1947) (dual state and federal regulation of labor dispute denied). *See also* Napier v. Atlantic Coast Line R.R., 272 U.S. 605, 613 (1926) (Federal Boiler Inspection Act precluded concomitant state regulation in that field).

16. *See, e.g.*, Florida Lime & Avocado Growers v. Paul, 373 U.S. 132, 147-50 (1963) (Agricultural Adjustment Act's legislative history did not preclude concomitant state regulation); Campbell v. Hussey, 368 U.S. 297, 301-02 (1961) (Federal Tobacco Inspection Act's legislative history precluded any state regulation of the industry). The Supreme Court traditionally has placed special reliance upon legislative history in determining whether federal pre-emption should be implied.

17. *See, e.g.*, Pennsylvania v. Nelson, 350 U.S. 497, 502-04 (1956) (Communist Control Act of 1954 completely covers that field of regulation to the exclusion of state control); Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947) (federal legislation exclusively covers the field of grain warehouse regulation); Bethlehem Steel Co. v. New York State Labor Relations Bd., 330 U.S. 767, 774 (1947) (federal legislation prohibits state regulation of labor disputes through its pervasiveness).

18. *See, e.g.*, Florida Lime & Avocado Growers v. Paul, 373 U.S. 132, 143-44 (1963) (state regulation of avocadoes upheld as not being an obstacle to uniformity of regulation in the field); San Diego Bldg. Trades Council v. Garmon, 359 U.S. 236, 241-44 (1959) (dual federal and state regulation regarding labor/management disputes no obstacle to uniformity in the field).

19. *See, e.g.*, Hines v. Davidowitz, 312 U.S. 52, 67 (1941) (state legislation that stood as an obstacle to federal regulation held invalid).

concerned with environmental protection. In 1954, for example, Congress amended the Atomic Energy Act to allow limited private ownership and operation of utilization facilities,[20] with the owners still being required to comply with strict AEC licensing requirements.[21] In 1959, the Act was amended again to provide procedures that authorized the AEC to relinquish certain of its regulatory responsibilities to the states.[22] The 1959 amendments, however, specifically prohibited the Commission from discontinuing its authority and responsibility over the construction and operation of nuclear production and utilization facilities.[23] Because of the special hazards involved, the Act seemed to mandate continued federal supervision over nuclear power plants and the discharge of radioactive effluents therefrom.[24] Along with these amendments, Congress more recently has extended the states' power to regulate in the closely related, yet formerly pre-empted, area of environmental protection.[25] In cases involving analogous concomitant state and federal regulation, courts have been reluctant to find federal pre-emption when states have acted under the authority of their police powers.[26] *Calvert Cliffs' Coordinating Committee, Inc. v. United States Atomic Energy Commission*,[27]

20. Act of Aug. 30, 1954, ch. 1073, § 81, 68 Stat. 935 (codified at 42 U.S.C. § 2111 (1970)). The amendment authorized private ownership of byproduct materials and leasing of special nuclear materials.

21. *Id.* For an analysis of the detailed licensing procedures see Power Reactor Dev. Co. v. International Union of Elec. Workers, 367 U.S. 396 (1961).

22. Act of Sept. 23, 1959, Pub. L. No. 86-373, 73 Stat. 688 (codified at 42 U.S.C. § 2021 (1970)). Section 2021(b) (1970) allows discontinuance of AEC authority only when the Governor of a state and the AEC enter into an agreement to that effect. The Joint Committee on Atomic Energy, however, found that "[l]icensing and regulation of more dangerous activities—such as nuclear reactors—will remain the exclusive responsibility of the Commission. Thus a line is drawn between types of activities deemed appropriate for regulation by individual States at this time, and other activities where continued AEC regulation is necessary." S. REP. NO. 870, 86th Cong., 1st Sess. 2872, 2879 (1959).

23. 42 U.S.C. § 2021(c) (1970).

24. 42 U.S.C. § 2021(k) (1970) provides that "[n]othing in this section shall be construed to affect the authority of any State or local agency to regulate activities for purposes other than protection against radiation hazards."

25. *See, e.g.*, Water Pollution Control Act Amendments of 1956, 33 U.S.C. §§ 1151-75 (1970); Clean Air Act, 42 U.S.C. §§ 1857-57(1) (1970); National Environmental Policy Act of 1969, 42 U.S.C. 4321-47 (1970); Environmental Quality Improvement Act of 1970, 42 U.S.C. §§ 4371-74 (1970).

26. *See, e.g.*, Textile Workers Union v. Lincoln Mills, 353 U.S. 448 (1957) (state law, if compatible with the Labor Management Relations Act, may be resorted to in order to find the rule best suited to effectuate policy of Act); Dickinson v. First Nat'l Bank, 400 F.2d 548 (5th Cir. 1968), *aff'd.*, 396 U.S. 122 (1969) (upheld state law imposing restrictions on federal definition of "branch bank").

27. 449 F.2d 1109 (D.C. Cir. 1971). For a discussion of this case see 25 VAND. L. REV. 258 (1972).

for example, acknowledged that Congress, through various environmental control acts, had recognized a significant state interest in protecting the environment. Moreover, the court in *Calvert Cliffs'* noted that the AEC has acknowledged this interest. Certain regulations proposed by the Commission subsequent to the 1969 enactment of the National Environmental Policy Act would obligate holders of nuclear construction permits to observe all applicable environmental standards imposed by either federal or state law.[28]

The instant court initially found that Congress had not exceeded the scope of its constitutionally delegated authority[29] by enacting the Atomic Energy Act and then proceeded to consider whether the Act precluded the state regulation in question. After concluding that the Act did not expressly pre-empt state regulation and that compliance with both the state and federal regulations was not impossible, the court looked to the legislative history of the Act and to the amendments to the Act to determine whether pre-emption could be implied on those bases. Although the 1954 amendments somewhat diminished federal control over the development of atomic energy,[30] the court noted that the pervasive licensing procedures that had been established effectively retained federal pre-emption of the field. Similarly, although the 1959 amendments enabled the AEC to transfer some regulatory functions to the states, the court found that the modifications were not intended to permit state regulation of radioactive wastes from nuclear power plants.[31] Moreover, the court observed that there would be no need for such formalized transfer procedures unless the AEC otherwise had exclusive regulatory jurisdiction. By closely examining the precise language of these amendments, the court found a clear congressional intent to pre-empt the field of controlling radioactive waste releases from nuclear power plants.[32] As additional support for this conclusion, the court noted that state regulation could present the possibility of overly protective action by the states. Finally, the court reasoned that, since such national interests as common defense, the security of the nation, and the free-flow of interstate and

28. 449 F.2d at 1116.

29. For a discussion of the constitutional basis for congressional regulation of public health and safety standards see Estep & Adleman, *State Control of Radiation Hazards: An Intergovernmental Relations Problem*, 60 MICH. L. REV. 41 (1961); Estep, *supra* note 7.

30. *See* Act of Aug. 30, 1954, ch. 1073, § 1, 53, 81, 68 Stat. 921, 930, 935 (codified at 42 U.S.C. §§ 2011, 2073, 2111 (1970)).

31. *See* Act of Sept. 23, 1959, Pub. L. No. 86-373, § 1, 73 Stat. 688 (codified at 42 U.S.C. § 2021(b) (1970)).

32. *See* Act of Sept. 23, 1959, Pub. L. No. 86-373, § 1, 73 Stat. 688 (codified at 42 U.S.C. § 2021(k) (1970)). For the text of 2021(k) see note 24 *supra*.

foreign commerce could be jeopardized by individual state action, federal pre-emption was necessary and should be implied.

Although the instant court's analysis of the Atomic Energy Act was sound, the court evidenced a myopic view in reaching its decision. First, the court's finding of implied federal preemption to the exclusion of state police power is contrary to the test established by the Supreme Court in *Florida Lime & Avocado Growers v. Paul*[33]—"whether both regulations could be enforced without impairing the federal superintendence of the field."[34] In the instant case, the court failed to determine whether the State regulations were unreasonable or burdensome. The Supreme Court also has held that state police powers should not be superseded unless an intent to pre-empt is clearly manifested by Congress,[35] or unless Congress has unambiguously mandated pre-emption.[36] The Eighth Circuit in the instant case, however, resorted to legislative history that was neither clear nor unambiguous in reaching its decision. Secondly, this court disregarded the proposed regulations of the AEC,[37] which provide that atomic energy plants must conform to both state and federal regulations in order to be licensed. The AEC promulgated these regulations under authority conferred by the 1969 National Environmental Policy Act,[38] which encourages federal agencies to share their regulatory authority with the states. Nevertheless, two sections[39] of the Atomic Energy Act seem to preclude the AEC's delegating such regulatory authority to the states; therefore the acts conflict. Although an administrative agency's interpretation of an act is not controlling, the AEC must have had good reason to propose this state regulation, and the instant court should have considered these reasons in reaching its decision. Finally, and most significantly, the instant court failed to recognize either the express language or the congressional intent behind recently enacted environmental protection acts.[40] In each of these acts, Congress recognized the need for more control of environmental pollution, stressed the necessity of greater state and federal cooperation, and used language broad enough to reach a variety of environmental problems—including radioactive waste disposal. Consequently, it is not unexpected that sections of the environ-

33. 373 U.S. 132 (1963).
34. 373 U.S. at 142.
35. Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947).
36. 373 U.S. at 147.
37. 10 C.F.R. § 50, app. D (1971). At the time the instant case was decided, these regulations were proposed but not adopted.
38. 42 U.S.C. §§ 4321-47 (1970).
39. 42 U.S.C. §§ 2021(k), (m) (1970).
40. *See, e.g.*, National Environmental Policy Act of 1969, 42 U.S.C. §§ 4321-47 (1970).

mental acts and the Atomic Energy Act are inconsistent.[41] Courts, therefore, should concern themselves not with ignoring, but with resolving the conflicting sections by balancing federal and state interests. The federal government has an interest in controlling atomic energy resources in order to preserve national defense capabilities and to provide national uniformity in the use of atomic energy. The AEC, through its specialization and expertise, can provide necessary leadership in the development and management of nuclear power plants.[42] On the other hand, states have a pressing and legitimate interest in protecting the health and safety of their citizens. Moreover, effective policing of a regulatory scheme may be accomplished more efficiently on the state level, since a state may be more responsive to local problems than a large, federal bureaucracy. Finally, a state may choose to forego some of the salutary effects of increased electric power in order to offer its citizens a cleaner environment. Obviously there is merit to both sides—enough merit to warrant a closer scrutiny than the instant court provided. The problems raised by this case are indicative of future conflicts between pre-emptive authority and remedial legislation. Congress may intentionally use broad language in drafting remedial legislation to enhance an act's chances of reaching a variety of related problems. Congress also should be aware that even a well intentioned ambiguity may have uncomfortable side effects. It should be left to Congress to cure interpretative problems that arise, since without congressional action each problem will be litigated separately with possibly inconsistent results. Although the judiciary eventually may reach a solution, Congress should exercise legislative power to circumvent the time-consuming judicial process by amending conflicting legislation to clarify present congressional intent and the allowable means to accomplish its purpose.[43]

41. *Compare* 42 U.S.C. § 2021(k) (1970) (restricting concomitant state and federal regulation), *with* 42 U.S.C. § 4321 (1970) (encouraging dual regulation).

42. One area in which federal assistance is vitally needed is in the production of electricity by atomic energy; witbout this help, the current energy crisis will be much more difficult to resolve. For an account of the energy crisis as well as proposals for its solution see Special Project, *The Energy Crisis: The Need for Antitrust Action and Federal Regulation*, 24 VAND. L. REV. 705 (1971).

43. Since the preparation of tbis Comment, the United States Supreme Court has affirmed the instant decision without opinion, Justices Stewart and Douglas dissenting. Northern States Power Co. v. Minnesota, 40 USLW 3479 (Apr. 4, 1972).

Corporations—Shareholder Suits—Shareholder May Iuspect Corporate Records Only for Proper Purpose Germane to his Economic Interest As Shareholder, Not Merely To Further his Owu Social and Political Beliefs

Petitioner shareholder,[1] who strongly opposed American military involvement in Vietnam, requested respondent Honeywell, Inc., to permit him to inspect its shareholder list so that he could communicate with other shareholders about halting Honeywell's production of war materials. Petitioner had purchased respondent's stock solely to gain a voice in Honeywell's affairs and thereby effectuate a change in the board of directors that would lead to a reduction in the manufacture of war materials.[2] When Honeywell refused to allow the requested inspection, petitioner sought a writ of mandamus to compel disclosure.[3] Petitioner contended that proxy solicitation and communication with other shareholders are in themselves proper purposes justifying inspection of the shareholder ledger. Honeywell maintained that proper purposes must focus on concern for investment returns and that petitioner, therefore, had not set forth a proper purpose. The trial court dismissed the petition and concluded that petitioner had not met the common-law prerequisite to inspection of setting forth a proper purpose germane to his interest as a shareholder.[4] On appeal to the Supreme Court of Minnesota, *held,* affirmed. A shareholder does not have the right to inspect shareholder lists in order to communicate with other shareholders or to solicit prox-

1. In July 1969, after learning about Honeywell's involvement in the production of war materials, petitioner ordered his agent to purchase 100 shares of Honeywell stock. The agent, however, unaware of petitioner's purpose, bought the stock in the name of a family nominee. Later, petitioner learned that he had a contingent beneficial interest in 242 shares of Honeywell stock through a trust formed for his benefit by his grandmother. Finally, on August 11, 1969, petitioner bought one share of stock in his own name.

2. Petitioner attended the July 3, 1969, meeting of the "Honeywell Project," an antiwar group that sought to stop Honeywell's manufacture of munitions. Petitioner first learned about Honeywell's government contracts for antipersonnel bombs at this time and decided to try to stop Honeywell's participation in these activities.

3. The petition for writ of mandamus was filed on November 24, 1969. Petitioner also sought to inspect Honeywell's records specifically relating to the manufacture of war materials in order to familiarize himself with the extent of Honeywell's involvement so he could make stronger arguments to other shareholders. These records were not, however, the focus of attention; the primary issue concerned the shareholder ledger containing names and addresses.

4. Honeywell is a Delaware corporation doing business in Minnesota. On appeal, both parties argued the question of applicable state law. The trial court applied Delaware law. DEL. CODE ANN. tit. 8, § 220 (Supp. 1968). The instant court found that the test derived from common law and was applicable in Minnesota under the authority of Sanders v. Pacific Gamble Robinson Co., 250 Minn. 265, 84 N.W.2d 919 (1957). Thus the common-law test was properly used.

ies for a board of directors election when the shareholder's sole purpose is to advance his own social and political beliefs without regard to economic effects. State *ex rel.* Pillsbury v. Honeywell, Inc., 191 N.W.2d 406 (Minn. 1971).

At common law, company shareholders have a right to inspect corporate records in order to protect their interests as owners of the corporation.[5] Enforcement of this right against recalcitrant management is by writ of mandamus.[6] Mandamus, however, is a discretionary remedy, and courts require the shareholder to justify its use by showing a proper purpose for the inspection, in order to prevent the corporate disruption that would be created by a shareholder roaming at will through company records merely to satisfy some personal motive.[7] The court, therefore, must inquire into the objectives sought by a shareholder's request to examine corporate records.[8] Early state statutes embodied the common-law principles but extended them to make the inspection right virtually absolute.[9] Because the remedy for denial of this statutory right continued to be mandamus, however, the courts continued to rely on the discretionary nature of the remedy to enforce a shareholder's inspection demand only upon demonstration of a proper pur-

5. *See, e.g.*, Guthrie v. Harkness, 199 U.S. 148, 155 (1905) (bank shareholders cannot be denied access to books and accounts by bank officers); State *ex rel.* G.M. Gustafson Co. v. Crookston Trust Co., 222 Minn. 17, 22 N.W.2d 911 (1946) (bank shareholders had right to inspect the books for proper purposes); 5 W. FLETCHER, PRIVATE CORPORATIONS § 2214 (perm. ed. rev. repl. 1967); H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES 396-97 (2d ed. 1970); ABA MODEL BUS. CORP. ACT ANN. § 52, Comment (2d ed. 1971); Note, *"Proper Purpose" for Inspection of Corporate Stock Ledger*, 1970 DUKE L.J. 393, 394-95.

6. 5 W. FLETCHER, *supra* note 5, § 2214; Note, *supra* note 5, at 394 n.9, 395.

7. *See, e.g.*, Cooke v. Outland, 265 N.C. 601, 611, 144 S.E.2d 835, 842 (1965). In *Cooke*, a proper purpose was exhibited by a demand to examine bank records to determine the value of the stock equity and the bank's financial condition and to determine whether the bank was managed efficiently. Proper purpose has been shown in other instances. *See* cases cited note 12 *infra*. Courts have denied mandamus when petitioner did not show a proper purpose. *See* cases cited note 13 *infra*.

8. In most instances, courts have gone beyond petitioner's demand to inspect corporate records in order to determine the purpose behind the demand. *See, e.g.*, State *ex rel.* Miller v. Loft, Inc., 34 Del. 538, 156 A. 170 (1931) (although shareholder is equitable owner of corporate assets, inspection will be allowed only when the facts, in the exercise of sound judicial discretion, justify it); Sawers v. American Phenolic Corp., 404 Ill. 440, 89 N.E.2d 374 (1949) (shareholder must show that he has some interest at stake or some beneficial reason for desiring the examination); State *ex rel.* G.M. Gustafson Co. v. Crookston Trust Co., 222 Minn. 17, 22 N.W.2d 911 (1946) (trust company shareholder's inspection demand must be germane to his interest as shareholder).

9. *E.g.*, Law of Mar. 22, 1929, ch. 135, § 29, [1929] Del. Laws 391 (the stock ledger containing the names, addresses, and share ownership of all shareholders "shall . . . be open to the examination of every stockholder"); Law of May 7, 1897, ch. 384, § 53, [1897] N.Y. Laws 314. For an in-depth discussion of the early "absolute" inspection right statutes see Newman, *Inspection of Stock Ledgers and Voting Lists*, 16 Sw. L.J. 439, 442-46 (1962).

pose.[10] More recent statutes have settled this dilemma by incorporating the common-law proper purpose concept into the statutory language.[11] This common-law standard has been interpreted by the courts to mean that a shareholder, acting in good faith, has a legal right to inspect corporate records for a specific legal purpose if that purpose is not contrary to the interests of the corporation and is germane to the petitioner's interest as a corporate shareholder.[12] On this basis, when the shareholder merely wanted to satisfy an idle curiosity, to harass the company, or to obtain the information, such as shareholder lists, for his individual business or speculative use, courts traditionally have found the purpose to be improper.[13] In *McMahon v. Dispatch Printing Co.*,

10. The development of judicial application of the law in Delaware is a typical example. *See* State *ex rel.* Cochran v. Penn-Beaver Oil Co., 34 Del. 81, 143 A. 257 (1926); Note, *supra* note 5, at 394-97. *See also* Henry v. Babcock & Wilcox Co., 196 N.Y. 302, 89 N.E. 942 (1909).

11. Note, *supra* note 5, at 397. For an analysis of the different state statutes see ABA MODEL BUS. CORP. ACT ANN. § 52, ¶ ¶ 3.02-.03 (2d ed. 1971). *See also* DEL. CODE ANN. tit. 8, § 220 (Supp. 1968) (any "stockholder . . . shall upon written demand under oath stating the purpose thereof, have the right . . . to inspect for any proper purpose the corporation's stock ledger . . . . A proper purpose shall mean a purpose reasonably related to such person's interest as a stockholder"); N.Y. BUS. CORP. LAW § 624(c) (McKinney 1963) (inspection may be denied if it is not for a "purpose which is in the interest of a business"); *id.* § 624(f) ("Nothing herein contained shall impair the power of the courts to compel the production for examination of the books and records of a corporation"); 5 W. FLETCHER, *supra* note 5, § 2215.1.

12. An analysis of the cases indicates that this is a fair summary of the common-law rule. Proper purposes generally can be listed under either investigation of corporate affairs and management or proposed communication with other shareholders. For a discussion of the former category see Sanders v. Pacific Gamble Robinson Co., 250 Minn. 265, 84 N.W.2d 919 (1957) (inspection of corporate records by shareholder to determine remuneration and other benefits received by corporate officers upheld as proper purpose), *noted in* 11 VAND. L. REV. 609 (1958); State *ex rel.* G.M. Gustafson Co. v. Crookston Trust Co., 222 Minn. 17, 22 N.W.2d 911 (1946) (trust company shareholder's inspection demand must be germane to his interest as shareholder); Durr v. Paragon Trading Corp., 270 N.Y. 464, 1 N.E.2d 967 (1936) (demand by shareholders to inspect corporate records to determine whether the officers are properly managing the corporate affairs is a sufficiently proper purpose as a matter of law); Cooke v. Outland, 265 N.C. 601, 144 S.E.2d 835 (1965) (proper purpose was exhibited by a demand to examine bank records to determine value of the stock equity and the bank's financial condition and to determine whether the bank was efficiently managed). For a discussion of the latter category see NVF Co. v. Sharon Steel Corp., 294 F. Supp. 1091 (W.D. Pa. 1969) (inspection of shareholder list in order to make offer to purchase equity stock of other shareholders upheld as a proper purpose); General Time Corp. v. Talley Indus., Inc., 43 Del. Ch. 531, 240 A.2d 755 (Sup. Ct. 1968); *see* text accompanying note 18 *infra;* cases cited note 15 *infra.*

13. *See, e.g.*, State *ex rel.* Thiele v. Cities Serv. Co., 31 Del. 514, 115 A. 773 (1922) (owner of one share of stock sought the shareholder list to sell for his own profit); Sawers v. American Phenolic Corp., 404 Ill. 440, 89 N.E.2d 374 (1949) (shareholder's purpose in requesting list was merely to satisfy curiosity because he had not attended shareholder meetings and had not accepted the company's offer allowing him to examine its books); Charles A. Day & Co. v. Booth, 123 Me. 443, 123 A. 557 (1924) (shareholder securities dealer bought single share of stock of several companies solely to obtain shareholder lists to use in his business); Albee v. Lamson & Hubbard Corp., 320 Mass. 421, 69 N.E.2d 811 (1946) (petitioning shareholder failed to establish his good faith in seeking the list). *See also* H. HENN, *supra* note 5, at 396-97.

for example, mandamus was denied when petitioner, lacking good faith and interest as a shareholder and consciously disregarding potential damage to the corporation's credit, desired to enforce his right of inspection merely to prosecute a personal feud.[14] Facilitation of proxy solicitation and communication with other shareholders, however, are the traditional reasons for seeking information that have been held to be proper purposes.[15] In recent cases, a conflict has arisen over whether communication with other shareholders is a proper purpose in itself, or whether the court can inquire further and deny mandamus when it finds a questionable ulterior motive for the request. In *Northwest Industries, Inc. v. B.F. Goodrich Co.*,[16] petitioner, who admittedly had not bought stock for investment purposes, was denied inspection; the court held that petitioner had failed to state the substance of its intended communication sufficiently to indicate a reasonable relationship between the inspection's purpose—communication with other shareholders—and petitioner's interest as a shareholder. On the other hand, in *Lake v. Buckeye Steel Castings Co.*,[17] the court found that communicating with other shareholders regarding the affairs of the corporation was on its face neither an illegal, unreasonable, nor improper purpose. Therefore, unless the corporation could prove the unreasonableness of petitioner's purpose, the court held that mandamus would issue. In *General Time Corp. v. Talley Industries, Inc.*[18] proxy solicitation specifically was held to be a purpose reasonably related to a shareholder's interest as a shareholder; moreover, establishment of proxy solicitation as the primary purpose of the requested inspection was held to entitle petitioner to the shareholder

14. 101 N.J.L. 470, 129 A. 425 (Sup. Ct. 1925) (petitioner sought to inspect the corporate records to gain information to help him block the reappointment of a company officer to a state political position).

15. Inspection has been granted to facilitate communication with other shareholders for various reasons. *See* Hanrahan v. Puget Sound Power & Light Co., 332 Mass. 586, 126 N.E.2d 499 (1955) (giving other shareholders information concerning a proposed merger); Murchison v. Alleghany Corp., 27 Misc. 2d 290, 210 N.Y.S.2d 153 (Sup. Ct. 1960), *aff'd mem.*, 210 N.Y.S.2d 975 (Sup. Ct. 1961) (shareholder sought proxies to change management). *See also* 5 W. FLETCHER, *supra* note 5, § 2223.

16. 260 A.2d 428 (Del. 1969). In a vigorous dissent, the Chief Justice argued that the statute gave an almost absolute right to inspect and that communication with other shareholders on matters relating to a planned shareholder meeting is a purpose germane to petitioner's status as a shareholder.

17. 2 Ohio St. 2d 101, 206 N.E.2d 566 (1965) (proper purpose for petitioner, 2 months after becoming a shareholder, to seek shareholder list to communicate with other shareholders "regarding the affairs of the corporation").

18. 43 Del. Ch. 531, 240 A.2d 755 (Sup. Ct. 1968) (solicitation of proxies for a slate of directors in opposition to management is a proper purpose reasonably related to the shareholder's interest regardless of any further purpose). *See also* Hanrahan v. Puget Sound Power & Light Co., 332 Mass. 586, 126 N.E.2d 499 (1955).

list without further proof. *Lake* and *General Time Corp.* exemplify what appears to be a change in approach by the courts because they provide an indication that establishing a traditionally proper purpose, such as an intent to communicate with other shareholders, will justify mandamus if there is no contrary showing. Furthermore, these recent decisions indicate that a noneconomically oriented motive for demanding the right to inspect only has indirect significance: the right to inspect has been denied only when the court has found the traditionally improper purposes of vexation or speculative intent.[19] An analagous situation exists under federal law dealing with shareholder participation in corporate decision-making. In *Medical Committee for Human Rights v. SEC*,[20] the court, interpreting an SEC rule dealing with the inclusion of shareholder proposals in management's annual proxy statement,[21] indicated that a shareholder proposal to prohibit the corporation from manufacturing a certain product[22] could not be excluded[23] from the proxy sent to all shareholders merely because the proposal appeared to deal with general social or political concerns. Thus, with respect to federal regulation of corporate activity, there is at least a suggestion that shareholders legitimately may attempt to direct the activity of the company not only

19. Incidentally, such intent is not based on an economic concern for the corporation, but the conclusive factor has been the existence of a traditionally improper purpose. *See* cases cited note 13 *supra*.

20. 432 F.2d 659 (D.C. Cir. 1970), *noted in* 24 VAND. L. REV. 387 (1971), *dismissed as moot*, 92 S. Ct. 577 (1972).

21. SEC Rule 14a-8(c) permits a corporation to refuse to include shareholder proposals on proxy statements if the proposal is concerned with, among other things, general social or political goals or if the proposal deals with the day-to-day business of the corporation. 17 C.F.R. § 240.14a-8(c) (Supp. 1971). Under the SEC rule, the corporation bears the burden of proving that the shareholder's proposal is improper. 432 F.2d at 680. Under the common-law test applied in the instant case, the burden of proof problem could be critical. *See* Note, *supra* note 5, at 397, 399. In the instant case, the court ruled that the shareholder had to prove a proper purpose, but since the case was decided on the pleadings and the deposition of petitioner, the burden of proof question was not at issue.

22. Shareholder Medical Committee sought to amend, through the proxy method, the Dow Company's certificate of incorporation to prohibit the corporation from manufacturing napalm. Shareholder gave 2 reasons for opposition to its continued production: first, the Medical Committee, for humanistic reasons, was opposed to the use of napalm against other human beings in war activities; secondly, the Medical Committee, for investment reasons, complained that, as a result of public reaction to napalm, the company's business suffered and it was unable to recruit outstanding college graduates neeessary for company growth. 432 F.2d at 662.

23. The court did not reach the merits of whether Dow could refuse to include this proposal under the SEC rule but remanded the matter to the SEC for a complete explanation concerning why it allowed Dow to exclude the proposal from its proxy statement. *Id.* at 676. The court recognized that the concept of corporate democracy underlying the SEC's proxy rules meant that the nature of the company's business was a proper topic for shareholder concern and discussion, including the possibility that the corporation should manufacture products more socially useful but perhaps less profitable. *Id.* at 681.

for its fiscal consequences but for its social and political implications as well.

In the instant decision, the court recognized that neither animosity toward management nor a desire to gain control of the corporation in order to improve its economic position would be improper purposes for inspection of corporate records. In addition, the court conceded that obtaining information for use in an election of directors is normally a proper purpose. The court, however, rejected the argument that a mere desire to communicate with other shareholders is per se a proper purpose,[24] and, using the *McMahon* decision as its basis, the court imposed the additional requirement that in order to inspect shareholder lists, the shareholder must show that he has a proper purpose for the subsequent communication with other shareholders.[25] In effect, the court held that it could scrutinize the motive underlying petitioner's desire to solicit proxies and determine whether that motive itself was proper. The court noted that the right to inspect corporate records can be a powerful weapon in corporate warfare and extremely disruptive to normal corporate functions;[26] consequently, in order to protect the corporation from any single shareholder's burdensome actions, inspection rights must be limited to purposes which advance the shareholder's interest as a shareholder. The court then found that petitioner had no economic interest in the corporation's activities[27] and that he intended solely to impress his own social and political views on management and other shareholders.[28]

24. The court cited Lake v. Buckeye Steel Castings Co., 2 Ohio St. 2d 101, 206 N.E.2d 566 (1965), as an example illustrating this point.

25. This is not very novel when compared to the decision in Northwest Indus., Inc. v. B.F. Goodrich Co., 260 A.2d 428 (Del. 1969), unless the latter can be explained as a mere procedural requirement. *See* Note, *supra* note 5, at 403. It *is* novel if based on *McMahon*.

26. "Because the power to inspect may be the power to destroy, it is important that only those with a bona fide interest in the corporation enjoy that power." 191 N.W.2d at 410. The court's analogy seems irrelevant to the facts as stated. Nowhere does the court indicate that petitioner was motivated by an intention to disrupt the corporation's business.

27. The court made specific reference to the "quite tenuous" nature of petitioner's stock holding, *see* note 1 *supra*, and cited two 65-year-old cases which recognized that courts will not compel inspection for "insignificant" equity ownership. 191 N.W.2d at 411. The Model Business Corporation Act allows any shareholder who has been a holder of record for at least 6 months or who owns at least 5% of all outstanding shares of the corporation to exercise the inspection right. ABA MODEL BUS. CORP. ACT ANN. § 52 (2d ed. 1971). Minnesota and 8 other states, however, allow inspection by any shareholder. *Id.* § 52, ¶ 3.03(3). The point was not elaborated on in the instant case.

28. The court, using the familiar "floodgates" argument, reasoned that if this relief were granted, anyone favoring a political or social policy different from the company's could secure a writ, deluging the company with a rash of spurious efforts to engage in a proxy fight. The validity of this argument presupposes 2 conditions that, in light of common-law and court decisions, appear to be erroneous: first, that courts will be unable to recognize bad-faith efforts at simple corporate harassment; secondly, that the management rather than the owners are the only ones who can decide what line of business the company should undertake. *See* 432 F.2d at 681.

The court finally held that, since petitioner did not have a bona fide investment interest relevant to his role as a shareholder, he had not shown a proper purpose and thus could not inspect respondent Honeywell's records to obtain a list of shareholders.[29]

The standard enunciated in the instant decision significantly restricts established common-law rights derived from the concept of shareholder ownership of corporations. The decision by the Minnesota Supreme Court to censor the ulterior motive behind what always has been considered a proper purpose is clearly a departure from the accepted common-law rule. Communication with other shareholders in order to elect a new board of directors conventionally has been held to be a proper purpose justifying protection of the shareholder's right to inspect the shareholder ledger and has not been qualified by the requirement that the intended communication be concerned with the corporation's financial status. The instant court's failure to follow this view may be partially explained by the discretionary nature of the mandamus remedy, which retains this nature even when embodied in a statute. If a mere allegation that petitioner seeks to inspect the shareholder ledger to communicate with other shareholders about changing the board of directors would elicit the necessary judicial remedy, it would appear that simple repetition of this formula by petitioner would make the inspection right absolute. In the instant case, the court exercised its discretion by looking beyond the claimed purpose to conclude that the underlying motivation was not proper.[30] This approach, however, appears inconsistent with prior decisions. In the past, courts have not inquired behind an allegedly proper purpose that they have accepted as valid, and the instant court gave no indication that it did not accept petitioner's purpose of communicating with other shareholders as valid.[31] Furthermore, courts have

29. The *Medical Committee* decision was distinguished because petitioner there, unlike the instant case, did express an investment interest as part of its concern. The instant court referred to dicta in *Medical Committee* indicating that management could not use its position to require the company to pursue certain activities according to management's social and political philosophy. 432 F.2d at 681. Analogizing to the instant case, the court stated that an "outsider with no economic concern for the corporation" could not impose his own social convictions on Honeywell. 191 N.W.2d at 412 n.7. The analogy is questionable when a company owner is called an "outsider."

30. *See* Newman, *supra* note 9, at 459.

31. The court did not challenge the veracity or sincerity of petitioner's allegation that he wanted to communicate with other shareholders, thus allowing the inference that this was his primary purpose. The court accepted the good faith of the petitioner but tied his good faith purely to his advocacy of his views. Adopting trial-court dicta, the instant court concluded that this was not the proper forum for petitioner to air his social and political views, regardless of good faith, and that petitioner did not want to engage in a bona fide proxy fight to take over control of the company.

never explicitly required that a proper purpose for inspection be integrated with an investment concern on the part of the petitioners. The more recent cases, particularly the *Lake* and *General Time* decisions, indicate that courts, in applying the common-law test to the issue of inspection rights, are inclined to accept petitioner's stated purpose when he is not motivated by an obviously improper purpose. State courts recently have demonstrated more sympathy to the ideas of corporate democracy and greater shareholder participation in the business of the corporation. This trend is paralleled by federal court interpretations of the Securities and Exchange Commission rules dealing with shareholder proposals in the annual corporate proxy statement.[32]

The instant decision severely impairs the fundamental principle of the common law that shareholders are the equitable owners of a corporation.[33] The thrust of the decision, in effect, is to deny to a shareholder the exercise of an ownership right—inspection of the shareholder ledger—unless he is motivated by a concern for the value of his investment in the company. The impact of the instant holding, is somewhat diluted, however, because it is a relatively simple matter to show a fiscal concern. By the logic of the instant case, petitioner could have argued successfully that, in addition to his humanistic concern, he wanted Honeywell to cease making war materials because it damaged the company's goodwill,[34] because reliance on war production, particularly at a time when American involvement in the Vietnam war is steadily decreasing, is not a sound economic policy, and because the company should concentrate on manufacturing products for a more stable peacetime economy. It is possible that the instant decision requires recitation of a formula showing that the petitioner also was concerned for his investment. Whether a corporation is financially stable and profitable depends on the policies followed by the corporation regarding its products. These policies are formulated by the board of directors, but the shareholders have the ultimate decision on the make-up of the board. Corporate policy, therefore, must be a matter for shareholder concern and a proper subject for shareholder discussion. Corporate policies, moreover, are not restricted merely to questions of profit and loss. The instant court failed to recognize that shareholders often are equally concerned with the social and political implications of their corporation's activities. For example,

32. *See* Medical Comm. for Human Rights v. SEC, 432 F.2d 659 (D.C. Cir. 1970); text accompanying note 20 *supra.*

33. "A corporation is run for the benefit of its stockholders and not for that of its managers." SEC v. Transamerica Corp., 163 F.2d 511, 517 (3d Cir. 1947), *cert. denied,* 332 U.S. 847 (1948).

34. This was petitioner's tactic in *Medical Committee. See* note 22 *supra.*

although a proxy battle to force General Motors to manifest greater sensitivity to public-interest issues[35] failed for lack of shareholder support, General Motors responded to this challenge by appointing a black leader to its board of directors and by creating a public policy review committee composed of members of the board.[36] In addition, many other corporations, in both their shareholder reports and their advertisements, are publicizing corporate efforts to combat poverty and pollution.[37] Under the present status of the law, a shareholder who desires to change his company's participation in what he deems a socially detrimental activity has two choices if he seeks to make the change through consultation with other shareholders. First, he can request that his proposal be included in the company's annual proxy statement, in which he is limited to a one hundred-word statement in support of his proposal.[38] Management is not so limited. Corporations generally have resisted shareholder-originated proposals for change, but the *Medical Committee* decision[39] and present corporate sensitivity to social issues may allow the shareholder to succeed in at least bringing the issue before other shareholder-owners.[40] Secondly, he may try to exercise his right of inspection to

35. "Campaign GM, the Campaign to Make General Motors Responsible," which was formed in late 1969, used proxy machinery and annual meetings in an effort to focus investors' attention on issues of public interest. At the 1970 General Motors shareholders' annual meeting, Campaign GM sought to introduce 2 resolutions: first, to add to the board of directors 3 new members who would be public-interest oriented; and secondly, to add a Shareholders Committee for Corporate Responsibility to gather facts and make recommendations concerning the corporation's role in modern society and possible means of achieving a proper balance between the interests of shareholders, employees, consumers, and the general public. For an extensive analysis of the first 2 phases of Campaign GM by a law professor who participated in the project see Schwartz, *The Public-Interest Proxy Contest: Reflections on Campaign GM,* 69 MICH. L. REV. 419 (1971); Schwartz, *Towards New Corporate Goals: Co-Existence with Society,* 60 GEO. L.J. 57 (1971).

36. Schwartz, *Towards New Corporate Goals: Co-Existence with Society, supra* note 35, at 59-60.

37. The trend is particularly noticeable with General Motors (controlling automobile emissions), Proctor & Gamble (minimizing pollution caused by soaps and detergents), and the Chase Manhattan Bank (aiding black-owned small businesses).

38. 17 C.F.R. § 240.14a-8(b) (Supp. 1971).

39. 432 F.2d 659 (1970). It is interesting to note that the Securities and Exchange Act, upon which the *Medical Committee* decision was based, evinces a legislative intent to give shareholders a more direct voice in the governing of the corporation. Schwartz, *The Public-Interest Proxy Contest: Reflections on Campaign GM, supra* note 35, at 436-51. On the other hand, the common law, upon which state decisions rely, is aimed primarily at protecting the shareholder's beneficial ownership of the corporate assets. *See* N. LATTIN, THE LAW OF CORPORATIONS 348 (2d ed. 1971); Note, *supra* note 5, at 394.

40. An inference from the *Medical Committee* decision is that although SEC Rule 14a-8(c) will allow management to reject a shareholder proposal for the proxy statement if the proposal deals with *general* social or political goals, a proposal to make a *specific* change in the company's operations would not fall under this disqualification. Nonetheless, the proposed action must not interfere with the day-to-day operations of the company because a proposal that would result in

obtain other shareholders' names in order to communicate personally with them. Among the states that have dealt with the inspection right, the trend[41] indicates that a shareholder may be able to enforce the right if he alleges a traditionally proper purpose.[42] Unless the instant decision is either distinguished or overruled, however, it will stand as an obstacle in the way of a corporate owner with a good-faith concern who seeks to discuss with other co-owners the possibility of changing a specific activity of their company.

Criminal Law—Information—Persons Arrested Without Warrant aud Accused by Direct Informatiou Have a Right to Prompt Judicial Determination of Probable Cause for Arrest

Plaintiffs[1] brought a class action in federal district court seeking to enjoin defendant law enforcement officials[2] from failing to provide per-

interference could also be denied access to the proxy statement under the same SEC rule. 432 F.2d at 680. For an analagous situation that occurred 20 years earlier see Peck v. Greyhound Corp., 97 F. Supp. 679 (S.D.N.Y. 1951) (management's refusal to include shareholder's proposal that "management consider the advisability of abolishing the segregated seating system in the south" upheld). Had the shareholder specifically proposed that Greyhound stop segregated seating on its own buses in the South, the decision might have been different.

41. *Cf.* General Time Corp. v. Talley Indus., Inc., 43 Del. Ch. 531, 240 A.2d 755 (Sup. Ct. 1968); Lake v. Buckeye Steel Castings Co., 2 Ohio St. 2d 101, 206 N.E.2d 566 (1965); text accompanying notes 17-18 *supra.* Northwest Indus., Inc. v. B.F. Goodrich Co., 260 A.2d 428 (Del. 1969) (inspection denied because petitioner failed to show a reasonable relationship between inspection's purpose and petitioner's interest as shareholder), has been distinguished because it merely indicates the proper form in which a demand for inspection should be made under the state statute. Note, *supra* note 5, at 403.

42. If he succeeds in obtaining the inspection right, however, the shareholder still may be unable to copy the list and communicate with other shareholders because of the astronomical expense of such an undertaking. Campaign GM concluded that the cost for one first-class mailing to each shareholder listed in the 133 large volumes of the General Motors shareholder ledger would have cost nearly $100,000. This was based upon a first-class postage rate of 6 cents and excluded the cost of copying the list. Schwartz, *The Public-Interest Proxy Contest: Reflections on Campaign GM, supra* note 35, at 426, 493.

1. Plaintiffs were incarcerated in the Dade County, Florida, jail at the time the instant suit was filed. Three of them alleged that they remained incarcerated because their poverty did not allow them to post bail. *See* note 4 *infra.* The fourth was charged with robbery, a crime punishable in Florida by life imprisonment, FLA. STAT. ANN. § 813.011 (1965), and therefore was not entitled to bail under the Florida constitution. FLA. CONST. art. 1, § 14.

2. Defendants were the state attorney, sheriffs, police chiefs, justices of the peace, and judges of small claims courts in Dade County. These officials were sued in their official capacities as individuals charged with the responsibility of administering the system under which plaintiffs were incarcerated.

sons held in pretrial detention preliminary hearings before a magistrate to determine probable cause for their arrests. Each plaintiff had been arrested without a warrant and incarcerated prior to the filing of a direct information by the state attorney without the review of a committing magistrate.[3] Plaintiffs contended that this failure to provide immediate preliminary hearings before a judicial officer to determine the probable cause for their arrests violated both the probable cause provision of the fourth amendment and the due process clause of the fourteenth amendment.[4] Defendants maintained that a direct information filed by a state

3. The instant court commented that "[a] person may be charged with a crime in Dade County, Florida, in one of five ways:

"(1) A police officer witnesses the commission of a crime, places the accused under arrest and takes him to jail. Sometime between 24 hours and two weeks later the arresting officer files a sworn affidavit with the office of the state attorney who, then files a direct information and issues a capias against the defendant.

"(2) A police officer conducts an investigation of an alleged criminal offense, decides he has sufficient evidence to arrest, and places the defendant in jail. The arresting officer then goes to the state attorney with his affidavit and a direct information is filed against the defendant by the state attorney.

"(3) A police officer conducts an investigation but takes the case to the state attorney *before* making the arrest and, after issuance of the direct information, arrests the defendant and places him in jail.

"(4) A police officer conducts an investigation, presents the matter by affidavit to a justice of the peace, who issues a warrant for arrest and conducts a preliminary hearing to determine probable cause as to the commission of the alleged crime. The defendant is released if no probable cause is found to exist.

"(5) The results of an investigation are submitted by the state attorney to the grand jury, which determines probable cause and returns an indictment to a judge. After review, the judge either issues the arrest warrant and causes the indictment to be filed or dismisses the charge." 332 F. Supp. at 1109-10. Although proeedures (1) through (3) are all under attack in the instant suit, it is not absolutely clear from the opinion whether plaintiffs were arrested before or after the filing of informations. The strong inference is, however, that the arrests came first. The opinion states that in addition to the probable delay of 24 hours to 2 weeks before the arresting officer's affidavit is sworn, there is a delay of 24 to 72 hours plus weekends before the information is filed with the clerk of the trial court, and an average delay of 10 to 15 days from the time the arresting officer appears until the time defendant is arraigned. Thus an accused can spend 11 to 29 days in jail before arraignment without a preliminary hearing.

4. The due process allegation was contained in Count I of the complaint. Count II alleged that plaintiffs were denied equal protection of the law in that arresting officers often processed cases through a justice of the peace, who conducts a preliminary hearing for probable cause, rather than through the state attorney, as was done in this case. The complaint argued that such discretion on the part of the police creates an arbitrary and unreasonable classification of arrestees—those who get a preliminary hearing and those who do not. Count III alleged that the setting of a monetary bail bond as a condition for release unreasonably creates a classification based solely on wealth, therefore also violating plaintiffs' right to equal protection of the law. The court held that its ruling on Count I rendered resolution of Count II unnecessary, and the court dismissed the allegation in Count III by saying that plaintiffs' confinement was the result of setting bail after considering only factors such as the severity of the crime, plaintiffs' ties to the community, past criminal records, and financial resources. Consequently, the bonds were not set in excess of the amount the judicial officer deemed necessary to secure plaintiffs' appearance at trial.

attorney was a constitutionally acceptable procedure for validating arrest and pretrial detention, and that the mere failure to provide a preliminary hearing did not amount to a violation of any constitutional right. Upon plaintiffs' motion for summary judgment, *held*, judgment for plaintiffs. Use of the direct information to detain for trial persons arrested without warrants violates the fourth and fourteenth amendments by failing to provide a prompt hearing before a judicial officer to determine probable cause for the arrest. *Pugh v. Rainwater*, 332 F. Supp. 1107 (S.D. Fla. 1971).

Of the several methods by which a person may be formally accused and brought to trial for the commission of a crime, by far the most common are indictment or presentment by a grand jury and information by a public prosecutor. An indictment is normally initiated by a prosecutor who submits a written accusation of a crime to the grand jury. If the latter finds probable cause that the person accused has committed a crime, it returns a true bill to the criminal court for further action. The method of presentment is identical except that the true bill is drawn up and returned by the grand jury upon its own discovery of probable criminal activity. Unlike either an indictment or a presentment, an accusation by information is a procedure whereby the prosecutor himself determines the necessary probable cause, draws up a formal accusation, and files it with the criminal court for further action.[5] Although the object of the formal accusation is to inform the accused of the charge against him so that he can prepare his defense, its existence obviously presupposes that a valid determination of probable cause for the accusation has been made. Since the fourth amendment[6] has been made applicable to the states through the fourteenth amendment[7] and has been construed as speaking of arrest warrants as well as search warrants,[8] a constitutional question can arise concerning the validity of the determination of probable cause made in any of the three accusatory processes outlined if the formal accusation is used as the sole basis for the issuance by the prosecutor of a capias, or writ of arrest. There is an

5. These comments on the nature of the indictment, the presentment, and the information are necessarily very generalized, the processes being almost entirely dependent upon local constitutional, statutory, or procedural rules, and are intended merely to point out their basic differences. For a detailed summary of the mechanics of a criminal prosecution see L. HALL, Y. KAMISAR, W. LAFAVE, & J. ISRAEL, MODERN CRIMINAL PROCEDURE 3-12 (3d ed. 1969).

6. "The right of the people to be secure in their persons . . . against unreasonable searches and seizures, shall not be violated, and no Warrants shall issue, but upon probable cause, supported by Oath or affirmation . . . ." U.S. CONST. amend. IV.

7. Mapp v. Ohio, 367 U.S. 643 (1961).

8. Giordenello v. United States, 357 U.S. 480 (1958).

even greater problem concerning the fourth amendment requirement of a valid determination of probable cause when an accused has been arrested without a warrant and detained before the return of an indictment or presentment or before the filing of an information.[9] The satisfaction of this requirement is expressly provided for on the federal level by statute[10] and procedural rule,[11] and by similar methods in most states,[12] which prescribe the use of a preliminary hearing on probable cause before a magistrate or other judicial officer. The accused is present at such hearings, and, because the proceeding sometimes is used as a discovery device, it is conducted in an adversary manner.[13] Thus a valid determination of probable cause is a constitutional concern during each of two distinct periods of pretrial detention: the period subsequent to the filing of the formal accusation, and the period prior thereto when an accused has been arrested without a formal accusation having been filed.[14] As to the former period, the validity of the information procedure of determining probable cause has been seriously questioned. In 1884, the Supreme Court held in *Hurtado v. California*[15] that the due process clause of the fourteenth amendment did not require a grand jury indictment, guaranteed by the fifth amendment to federal defendants accused of serious crimes, in a state felony prosecution when state law provided for a proceeding by information.[16] Twenty-nine years later, in *Lem*

9. Virtually all jurisdictions employ procedures by which warrantless arrests may be made by an officer in certain situations. *See, e.g.*, FLA. STAT. ANN. § 901.15 (Supp. 1971).

10. The Federal Magistrates Act § 303, 18 U.S.C. § 3060 (1970).

11. FED. R. CRIM. P. 5.

12. The relevant Florida statutes, for example, are as follows: "When arrest by a warrant occurs in the county where the alleged offense was committed and the warrant issued, the officer making the arrest shall without unnecessary delay take the person arrested before the magistrate who issued the warrant or, if the magistrate is absent or unable to act, before the most accessible magistrate in the same county." FLA. STAT. ANN. § 901.06 (Supp. 1971). "A peace officer making an arrest without a warrant shall take the arrested person without unnecessary delay before the most accessible magistrate in the same county and shall make a complaint stating the facts constituting the offense for which the person was arrested." FLA. STAT. ANN. § 901.23 (Supp. 1971).

13. *See, e.g.*, Blue v. United States, 342 F.2d 894 (D.C. Cir. 1964), *cert. denied*, 380 U.S. 944 (1965).

14. Another important question arising in this context is how much time may elapse before the probable cause determination must be made. State and federal statutes generally require that all arrestees be taken before a magistrate "without unreasonable delay," either to make an immediate determination of probable cause or to set a date for a preliminary hearing. An unreasonable delay in holding the hearing, usually defined by statute as a certain maximum number of days after arrest, normally will require the release of the arrestee. *See, e.g.*, 18 U.S.C. § 3060 (1970); FLA. STAT. ANN. § 907.045 (Supp. 1971).

15. 110 U.S. 516 (1884).

16. The Supreme Court has never ruled that the right to a grand jury indictment in a state prosecution is a "fundamental" one. Thus it is not guaranteed to all defendants under the holding of Powell v. Alabama, 287 U.S. 45 (1932). This case held that the right to counsel was one of the

Woon v. Oregon,[17] the Court relied on *Hurtado* in upholding a state procedure through which an accused could be proceeded against by information without an examination by a magistrate of probable cause. The opinion, by way of dictum, said that in the absence of an indictment, the state was not required to provide a preliminary hearing during the period prior to the filing of the information.[18] Similarly, many lower federal courts have ruled that there is no constitutional right to a preliminary hearing on the probable cause for an arrest, at least when the issue arises after conviction or after an indictment has been returned.[19] These decisions are predicated on the theory that since a preliminary hearing is not a critical stage of the criminal process and since a subsequent indictment effectively resolves the issue of probable cause, failure of the state to provide a preliminary hearing is not a denial of due process. State courts also have refused to view the preliminary hearing as a constitutional requirement.[20] There remains, however, the question

fundamental rights guaranteed by the due process clause of the fourteenth amendment, and was therefore available to defendants in all jurisdictions. *See* 42 WASH. L. REV. 903 (1967).

17. 229 U.S. 586 (1913).

18. *Id.* at 590.

19. Anderson v. Nosser, 438 F.2d 183 (5th Cir. 1971) (unreasonable delay in bringing defendant before magistrate may be false imprisonment under state law, but does not rise to status of denial of due process); Murphy v. Beto, 416 F.2d 98 (5th Cir. 1969) (preliminary hearing before magistrate is not a federal constitutional right that, if denied, requires petitioner's release on habeas corpus); Kulyk v. United States, 414 F.2d 139, 141-42 (5th Cir. 1969) ("The right under the federal rules to be promptly taken before a magistrate has not been given constitutional status and has not been applied to persons in state custody"); McCoy v. Wainwright, 396 F.2d 818 (5th Cir. 1968) (petitioner not deprived of due process simply because not afforded a preliminary hearing in state prosecution); Worts v. Dutton, 395 F.2d 341 (5th Cir. 1968) (no federal constitutional right to preliminary hearing in state court because not a critical stage of proceeding); Kerr v. Dutton, 393 F.2d 79 (5th Cir. 1968) (commitment hearing not critical stage of state proceeding, so denial of counsel therein not unconstitutional); Scarbrough v. Dutton, 393 F.2d 6 (5th Cir. 1968) (7-month detention prior to trial without preliminary hearing is not grounds for reversal of conviction because hearing is for determining probable cause, and, because defendant could lose no rights that would prejudice his later defense, it is not per se a critical stage of criminal proceeding); King v. Wainwright, 368 F.2d 57 (5th Cir. 1966) (preliminary hearing not essential to due process of law, and does not affect validity of conviction). For similar holdings in and outside of the Fifth Circuit see United States v. Milano, 443 F.2d 1022 (10th Cir. 1971); United States v. La Pera, 443 F.2d 810 (9th Cir. 1971); Collins v. Swenson, 443 F.2d 329 (8th Cir. 1971); Ramirez v. Arizona, 437 F.2d 119 (9th Cir. 1971); Jackson v. Smith, 435 F.2d 1284 (5th Cir. 1970); Barber v. Arkansas, 429 F.2d 20 (8th Cir. 1970); Via v. Perini, 415 F.2d 1052 (6th Cir. 1969); United States v. Conway, 415 F.2d 158 (3d Cir. 1969); Joyce v. Cox, 315 F. Supp. 832 (W.D. Va. 1970).

20. Anderson v. State, 241 So. 2d 390 (Fla. 1970) (denial of preliminary hearing not prejudicial when later grand jury indictment mooted issue of probable cause); Sangaree v. Hamlin, 235 So. 2d 729 (Fla. 1970) (preliminary hearing not a step in due process; not a prerequisite to prosecution or to filing of information or indictment); Montgomery v. State, 176 So. 2d 331 (Fla. 1965) (preliminary hearing is not a critical stage, and prosecution may be initiated regardless of whether it is held and regardless of whether probable cause is found); Baugus v. State, 141 So. 2d 264 (Fla. 1962) (preliminary hearing is neither a step in the due process of law nor a prerequisite to filing an

whether an information, when filed, validly resolves the issue of probable cause for a subsequent arrest or cures the lack of a preliminary hearing for one arrested and detained prior to its filing, especially when the detention is for an appreciable length of time. *Hurtado* and *Lem Woon* have been recently interpreted as meaning that since the use of a direct information is constitutional, then a fortiori a state attorney must be competent to determine probable cause for arrest.[21] *Ocampo v. United States*,[22] decided a year after *Lem Woon*, lent support to this theory by holding the determination of probable cause to be a quasi-judicial function capable of being vested in a prosecutor. On the other hand, there have been recent indications that a direct information filed by a prosecutor may be valid only if it is based upon a determination of probable cause by a "neutral and detached" magistrate.[23] The Supreme Court, in *Giordenello v. United States*,[24] for example, construed Federal Rules of Criminal Procedure 3 and 4 as requiring judicial determination of probable cause in the issuance of an arrest warrant, and there is a strong indication that this construction was based on principles derived from the Constitution rather than from the Federal Rules.[25] In an analogous area, the Court has ruled that only a neutral and detached magistrate may determine probable cause for the issuance of a valid search warrant,[26] and that such a warrant issued by a state attorney general acting in his dual capacity as a justice of the peace is invalid per se when he is

information); *accord*, Lovell v. State, 250 So. 2d 915 (Fla. App. 1971); Maxwell v. Blount, 250 So. 2d 657 (Fla. App. 1971); Karz v. Overton, 249 So. 2d 763 (Fla. App. 1971); Bullard v. Smith, 225 Ga. 416, 169 S.E.2d 329 (1969); People v. Shastal, 26 Mich. App. 347, 182 N.W.2d 638 (1970); Allred v. State, 187 So. 2d 28 (Miss. 1966); State v. War, 38 N.J. Super. 201, 118 A.2d 553 (1955); Webb v. Commonwealth, 204 Va. 24, 129 S.E.2d 22 (1963); Crouse v. State, 384 P.2d 321 (Wyo. 1963).

21. State v. Kanistanaux, 68 Wash. 2d 652, 414 P.2d 784 (1966); *see* 42 WASH. L. REV. 903 (1967).

22. 234 U.S. 91 (1914).

23. Kinnaird v. State, 251 Ind. 506, 242 N.E.2d 500 (1968), *noted in* 45 IND. L.J. 56 (1969). In the comment it is noted that a state court, confronted with statutes allowing direct informations and a constitutional provision identical to that of the fourth amendment, felt constrained to rule that a proper arrest warrant could not be issued without some kind of judicial sanction.

24. 357 U.S. 480 (1958).

25. *See* Aguilar v. Texas, 378 U.S. 108, 112 n.3 (1964); Giordenello v. United States, 357 U.S. 480, 485-86 (1958).

26. *See, e.g.*, Mancusi v. DeForte, 392 U.S. 364 (1968) (subpoena duces tecum, while invalid as search warrant on other grounds, is also invalid as search warrant because issued by district attorney who is not a neutral and detached magistrate); Johnson v. United States, 333 U.S. 10 (1948) (the protection afforded by the fourth amendment consists of the requirement that a neutral and detached magistrate, rather than the police, make the inference of probable cause prior to a search); United States v. Lefkowitz, 285 U.S. 452 (1932) (the informed and deliberate determinations of magistrates empowered to issue search warrants are to be preferred over the hurried actions of police officers who may happen to make arrests).

also actively in charge of conducting the investigation of the case.[27] Focusing directly on the preliminary hearing, the Supreme Court recently held, in *Coleman v. Alabama*,[28] that a state hearing on the issues of bail and probable cause for submitting a case to the grand jury is indeed a critical stage in the criminal process, at least insofar as there is a necessity that the defendant be afforded counsel. Finally, two recent circuit court decisions in the District of Columbia, *Cooley v. Stone*[29] and *Brown v. Fauntleroy*,[30] although dealing with juvenile defendants, have expressly held that the right to a preliminary hearing is a constitutional one.

After establishing its jurisdiction over the state criminal procedures in question,[31] the instant court turned to the primary issue of whether a person who is arrested and held for trial upon an information filed by a state attorney is entitled to a hearing before a judicial officer on the question of probable cause. Examining two Supreme Court cases relied upon by defendants, *Hurtado v. California*[32] and *Lem Woon v. Oregon*,[33]

27. Coolidge v. New Hampshire, 403 U.S. 443 (1971). Justice Black's dissent argues that there need be no "little trial" by a neutral magistrate before the actual trial, and that the fourth amendment does not disqualify the state attorney from issuing the warrant. *Id.* at 493 (Black, J., dissenting).

28. 399 U.S. 1 (1970).

29. 414 F.2d 1213 (D.C. Cir. 1969).

30. 442 F.2d 838 (D.C. Cir. 1971).

31. Defendants had argued that the court had no jurisdiction, on the basis of the Federal Anti-Injunction Statute, 28 U.S.C. § 2283 (1970), which states that "[a] court of the United States may not grant an injunction to stay proceedings in a State court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments," and on the basis of several recent Supreme Court cases—Byrne v. Karalexis, 401 U.S. 216 (1971); Dyson v. Stein, 401 U.S. 200 (1971); Perez v. Ledesma, 401 U.S. 82 (1971); Boyle v. Landry, 401 U.S. 77 (1971); Samuels v. Mackell, 401 U.S. 66 (1971); Younger v. Harris, 401 U.S. 37 (1971). The court replied that the relief specifically precluded under the statute is the enjoining of a state prosecution, or a declaratory judgment with the same effect, and that, moreover, in each of the above-cited cases the plaintiff had asked that a state criminal law statute be declared unconstitutional. In the present case plaintiffs only asked for "a declaration of procedural rights and an injunction from the continued denial thereof." 332 F. Supp. at 1111. This situation is distinguishable, therefore, from those proscribed by *Younger* and § 2283. The court then went further, saying that if necessary the case can be construed as one of the exceptions recognized by *Younger* in which a federal court can take jurisdiction if the facts show "a 'great and immediate' 'irreparable injury' other than the 'cost, anxiety, and inconvenience of having to defend against a single criminal prosecution,' " and an injury which cannot be eliminated simply by an individual's defense against his own criminal prosecution. 332 F. Supp. at 1111. The court cited the following cases for the proposition that Florida consistently has denied the right asserted, thus making the injury irreparable: Anderson v. State, 241 So. 2d 390 (Fla. 1970); Sangaree v. Hamlin, 235 So. 2d 729 (Fla. 1970); Montgomery v. State, 176 So. 2d 331 (Fla. 1965); Baugus v. State, 141 So. 2d 264 (Fla. 1962).

32. 110 U.S. 516 (1884).

33. 229 U.S. 586 (1913).

the court found neither case controlling. The *Hurtado* case, holding that a determination of probable cause by a grand jury indictment was not required for a state felony prosecution, was not controlling because the Court there assumed that, prior to the filing of an information, probable cause would have been determined by a committing magistrate.[34] The court then distinguished *Lem Woon*, noting that its legal question bore on the validity of the information itself and not on the constitutionality of the pretrial detention. Similarly, the court distinguished several other cases cited by the defense for the proposition that there was no due process right to a preliminary hearing. Recognizing the holdings of these cases, the court found that the issue in each was the validity of the trial and conviction as affected by the absence of a preliminary hearing, and not the validity of the pretrial detention itself.[35] The distinctive issue of the instant suit was viewed by the court as being the validity not only of a present confinement, but also of a recurring part of a prosecutorial system that permits incarceration of an accused by information without a determination of probable cause by a magistrate. Addressing this issue, the court found that the basic due process right under the fourteenth amendment is the opportunity to be heard[36] within a reasonable time and in a proper manner.[37] Moreover, an individual's freedom from unreasonable seizure and from deprivation of liberty without due process of law depends on judicial safeguards against the arbitrary power of the police and the prosecutor.[38] The court determined that a preliminary hearing satisfies these requirements. On the other hand, a nonwarrant arrestee who has been proceeded against by information is given neither the opportunity to be heard nor the judicial safeguard provided by an independent determination of probable cause by a disinterested third party. The court, therefore, concluded that the due process clause of the

34. "[W]e are unable to say that the substitution for a presentment or indictment by a grand jury *of the proceeding by information, after examination and commitment by a magistrate, certifying to the probable guilt of the defendant*, with the right on his part to the aid of counsel, and to the cross-examination of the witnesses produced for the prosecution, is not due process of law.' (Emphasis added.) 110 U.S. at 53[8]." 332 F. Supp. at 1112.

35. Hamilton v. Alabama, 368 U.S. 52 (1961); Murphy v. Beto, 416 F.2d 98 (5th Cir. 1969); McCoy v. Wainwright, 396 F.2d 818 (5th Cir. 1968); Worts v. Dutton, 395 F.2d 341 (5th Cir. 1968); Scarbrough v. Dutton, 393 F.2d 6 (5th Cir. 1968); Kerr v. Dutton, 393 F.2d 79 (5th Cir. 1968); King v. Wainwright, 368 F.2d 57 (5th Cir. 1966). Another case cited in the instant opinion, Anderson v. Nosser, 438 F.2d 183 (5th Cir. 1971), did not consider the validity of a conviction, but the instant court found the *Anderson* facts analogous to those in the foregoing post-conviction cases. In *Anderson*, plaintiffs were at the time of suit free pending trial, so the court in effect was being asked, as in the cases above, to grant relief from an already terminated deprivation of rights.

36. *See* Grannis v. Ordean, 234 U.S. 385 (1914).

37. *See* Armstrong v. Manzo, 380 U.S. 545, 552 (1965).

38. *See* McNabb v. United States, 318 U.S. 332, 343-44 (1943).

fourteenth amendment requires a preliminary judicial hearing within a reasonable time after an accused has been deprived of his freedom.[39] Noting the *Cooley*[40] and *Brown*[41] decisions and their requirement of a probable cause hearing, the court additionally concluded that the fourth amendment probable cause requirement, which applies to arrest warrants[42] and is applicable to the states through the due process clause of the fourteenth amendment,[43] demands that plaintiffs be afforded such a judicial hearing. Accordingly, the court ordered that plaintiffs be given an immediate hearing and that defendants submit a plan whereby each subsequent arrestee will be assured of a similar hearing.

The holding in the instant case is limited on its face to requiring that a judicial probable cause hearing be afforded in all cases in which prosecution is to be upon direct information.[44] Although the opinion may appear to deal only with that period of pretrial detention prior to the actual filing of the information, the court's holding that the necessity of a preliminary hearing is based directly upon rights under the fourth and fourteenth amendments makes it clear that even the filing of the information will not obviate that necessity. Consequently, state law enforcement officials no longer will be able to incarcerate an accused, or exact bail from him, before the filing of an information without providing him a prompt preliminary hearing.[45] Previously, the practice of incarcerating an accused for a period of time before filing the information

39. The court noted in passing the following important situations outside of criminal law that, in order to comply with due process, require probable cause hearings before a state can take action against a person or his property: "It has been held that a hearing must be given *before* a drivers license and vehicle registration can be suspended, Bell v. Burson, 402 U.S. 535 . . . (1971); Salkay v. Williams, 445 F.2d 599 (5th Cir. 1971); *before* prohibiting the sale of liquor to an individual for one year, Wisconsin v. Constantineau, 400 U.S. 433 . . . [(1971)]; *before* termination of welfare payments (even though a subsequent hearing was afforded), Goldberg v. Kelly, 397 U.S. 254 . . . (1970); *before* garnishment of wages (even though there was a subsequent trial), Snidach [*sic*] v. Family Finance Corp., 395 U.S. 337 . . . (1969); *before* a thirty day suspension from a public school, Williams v. Dade County School Board, 441 F.2d 299 (5th Cir. 1971); *before* refusal of admission to public hospital staff, Sosa v. Board of Managers, 437 F.2d 173 (5th Cir. 1971); and *before* termination of employment on college faculty, Ferguson v. Thomas, 430 F.2d 852 (5th Cir. 1970)." 332 F. Supp. at 1113-14.

40. 414 F.2d 1213 (D.C. Cir. 1969).

41. 442 F.2d 838 (D.C. Cir. 1971).

42. *See* Giordenello v. United States, 357 U.S. 480 (1958).

43. *See* Mapp v. Ohio, 367 U.S. 643 (1961).

44. The court also holds that the preliminary hearing must be held "within a reasonable time of arrest." 332 F. Supp. at 1116. The court, however, does not deal directly with the question of what is a "reasonable time" other than to conclude that the particular plaintiffs involved were entitled to an immediate hearing. *See generally* note 14 *supra*.

45. FLA. STAT. ANN. § 907.045 (Supp. 1971) requires a mandatory hearing for a defendant charged by indictment or information after he has been in custody for more than 30 days.

had been permitted to allow the gathering of enough evidence to go forward with a case. Despite strong judicial warnings, this practice had continued until the instant case.[46] Now, before a suspect is arrested, or held for any length of time, the prosecutor will have to produce enough evidence to show probable cause. Not only will this requirement better protect persons from unwarranted arrests, but it also will afford those arrested a speedier process of justice, and prompt release if no probable cause is found to exist.[47] Although the holding in the instant case is limited to criminal actions involving the use of an information, its reasoning appears to be applicable to situations in which either the indictment or the presentment is involved. If one accused by information has a constitutional right to a preliminary hearing on probable cause, why should one accused by indictment or presentment not also have such a constitutional right? Notwithstanding the express constitutional provision for the grand jury procedure,[48] the neutrality and propriety of the indictment have been questioned by some,[49] and it is obvious that both state and federal indictment procedures[50] have defects similar to those of the information procedure. For example, the return of an indictment against one already in custody has generally been regarded as obviating the necessity for a preliminary hearing, because the indictment allegedly has resolved the issue of probable cause.[51] Although both Federal Rule of Criminal Procedure 5(c) and section 303 of the Federal Magistrates Act require that a preliminary hearing be held within a reasonable time after arrest, the latter goes on to say that if an indictment is returned prior to a preliminary hearing, the hearing is no longer necessary. Thus, as was true of the information procedure, if a federal prosecutor is able to postpone the preliminary hearing long enough to discover his evidence and obtain an indictment, the defendant is no longer entitled to a prelim-

46. In State *ex rel.* Carty v. Purdy, 240 So. 2d 480 (Fla. 1970), the Florida Supreme Court stated that if law enforcement officers continued such practices, then the courts might resort to a *McNabb-Mallory* type rule that, in the federal courts, automatically excludes all evidence obtained against a suspect prior to his probable cause determination before a magistrate, whether such evidence is voluntarily obtained or not, and regardless of its probative value.

47. The court states that between January 1, 1970, and March 31, 1971, the state attorney decided not to file direct informations in 1,165 cases in which defendants had been charged or arrested as a result of police investigation. Most of these "no actions" resulted from arrests on charges lacking sufficient evidence to justify the filing of an information.

48. U.S. CONST. amend. V.

49. *See, e.g.*, Weinberg & Weinberg, *The Congressional Invitation to Avoid the Preliminary Hearing: An Analysis of § 303 of the Federal Magistrates Act of 1968*, 67 MICH. L. REV. 1361 (1969). The authors here argue that the grand jury is not a proper body to reach an independent judicial determination of probable cause, since it is primarily a rubber stamp for the prosecutor.

50. This discussion treats the indictment and the presentment procedures as identical.

51. *See* notes 19 & 20 *supra*.

inary hearing at all, despite the existence of the federal rule.[52] A similar procedure can be followed in Florida, despite the existence of new rules of procedure[53] calling for a preliminary hearing. Thus there is a real possibility that an arrestee may be held in pretrial detention for a considerable period of time before a determination of probable cause is made, and that this detention will not jeopardize the prosecutor's case if it is cured by the return of an indictment. Although the instant opinion does not address this problem, its constitutional arguments for an absolute right to a preliminary hearing are persuasive, and it may be later inferred that a preliminary hearing is necessary despite the existence of an indictment. There are excellent reasons why this inference should be made. As pointed out by the Chief Justice of the Florida Supreme Court, speaking in the context of the new state procedural rules,[54] the preliminary hearing "confers upon an accused person procedural rights which are unquestionably distinct and superior to whatever rights are available to an accused at the ex parte grand jury and information stage of [criminal] proceedings."[55] Such rights—including presence of counsel, compulsory attendance, confrontation, and cross-examination of witnesses, and possibly even the right to suppress evidence—may have the effect of dissuading the prosecutor from seeking further prosecution of a weak case.[56] Federal Rule of Criminal Procedure 5 guarantees similar procedural rights to federal defendants, and some of these rights are capable of being effectively lost if not available until trial. The right of discovery is probably one of the most important to a defendant at a preliminary hearing, for with it he can test the soundness of the case against him and better prepare his defense. History shows that the original purpose of the preliminary hearing was that of a discovery device, but most courts in the United States have held that these hearings exist only to determine probable cause.[57] Only recently have a few federal cases held that there is also a need to use the preliminary hearing as a discovery device.[58] The

52. Weinberg & Weinberg, *supra* note 49, at 1385; Comment, *The Preliminary Examination in the Federal System: A Proposal for a Rule Change*, 116 U. PA. L. REV. 1416 (1968).

53. FLA. R. CRIM. P. 1.122.

54. *Id.*

55. Sangaree v. Hamlin, 235 So. 2d 729, 734 (Fla. 1970) (Ervin, C.J., dissenting).

56. *Id.*

57. *See* Anderson, *The Preliminary Hearing—Better Alternatives or More of the Same?*, 35 MO. L. REV. 281, 288 (1970); Weinberg & Weinberg, *supra* note 49, at 1365; Note, *The Preliminary Hearing—An Interest Analysis*, 51 IOWA L. REV. 164, 176 (1965); Comment, *Preliminary Hearings—The Case for Revival*, 39 U. COLO. L. REV. 580, 583 (1967); Comment, *supra* note 52, at 1419.

58. *See, e.g.*, Blue v. United States, 342 F.2d 894 (D.C. Cir. 1964), *cert. denied*, 380 U.S. 944 (1965).

preliminary hearing is likely to become more and more important, even to the point at which it will be recognized as an absolute right of all criminal defendants, regardless of how they are arrested, charged, or proceeded against. The instant case is an important step in that direction.

Federal Employees—Racial Discrimination—Back Pay Remedy Implied When Federal Job Applicant Denied Eqnal Employment Opportunity in Violation of Executive Order No. 11,478

Plaintiff, a black applicant for federal employment, was refused a job by the Social Security Administration (SSA) solely on the basis of an unfavorable and racially motivated reference report from plaintiff's former employer. At an administrative appeal before the SSA, plaintiff alleged racial discrimination[1] in violation of Executive Order No. 11,478, which declares that equal employment opportunity is a policy of the Government and prohibits such discrimination in federal employment.[2] The SSA found that plaintiff had not been discriminated against because of race, but the Director of Equal Employment Opportunity for the Department of Health, Education, and Welfare reversed that finding and recommended plaintiff be considered for the next suitable position available. Plaintiff, however, seeking immediate employment as well as any back pay that would have accrued had she been hired, further appealed to the Civil Service Commission Board of Appeals and Review

1. Plaintiff argued that the hiring officer's failure to investigate the reference report to determine the veracity of its contents and the merit of her charges of discrimination against her former employer was itself a violation of the executive order. Plaintiff also alleged that the hiring officer worked in an "environment of racial discrimination."

2. The order that was in effect at the time of the alleged discrimination by the Government was Exec. Order No. 11,246, 3 C.F.R. 167 (Supp. 1965), but Exec. Order No. 11,478 superseded it by the time of the trial. The terms of both orders are substantially identical concerning federal employment. The more recent version provides in § 1 that "[i]t is the policy of the Government of the United States to provide equal opportunity in Federal employment for all persons, to prohibit discrimination in employment because of race. [sic] color, religion, sex, or national origin, and to promote the full realization of equal employment opportunity through a continuing affirmative program in each executive department and agency. This policy of equal opportunity applies to and must be an integral part of every aspect of personnel policy and practice in the employment, development, advancement, and treatment of civilian employees of the Federal Government." 3 C.F.R. 462 (Supp. 1971). Both orders were promulgated pursuant to 5 U.S.C. § 7151 (1970) (originally enacted as Pub. L. No. 88-352, § 701(b), 78 Stat. 241, 253-54 (1964)), which authorizes the President to use his "existing authority" to carry out the stated policy.

(BAR). Although the BAR awarded plaintiff an immediate position, it did not feel that it had jurisdiction to award her back pay. Plaintiff then brought the instant action in the Court of Claims to recover the back pay. Defendant admitted that plaintiff would have been recommended and hired had it not been for the unfavorable reference report and acknowledged that the denial of employment constituted discrimination in violation of the executive order. Defendant argued, however, that an action would not lie against the Government for the back pay of an applicant never appointed to office because federal hiring is within the complete discretion of the executive department, and because the Government did not waive sovereign immunity. On cross motions for summary judgment to the United States Court of Claims, *held*, for the plaintiff. When a federal job applicant is denied equal employment opportunity in violation of Executive Order No. 11,478 and discretionary elements of hiring are not present, the Court of Claims may imply a monetary remedy from the executive order and award back pay. *Chambers v. United States*, 451 F.2d 1045 (Ct. Cl. 1971).

The nature of federal employment has long been considered a nonproprietary, noncontractual privilege[3] because of the constitutionally granted[4] executive discretion in appointment of government officers.[5] Paraphrasing Mr. Justice Holmes, no constitutional right to an appointment to federal or other public office exists as an adjunct to other rights granted by the Constitution.[6] The rationale of executive discretion in this area is that the federal government must not be burdened by unnecessary or unwanted employees. For example, veterans of World War II had no collective or individual right to retain their positions in the armed forces after the termination of hostilities; likewise no action will lie for failure of the President to appoint an applicant to the office of Secretary of State.[7] In certain situations, however, the discretionary

3. Taylor v. Beckham, 178 U.S. 548 (1900); Crenshaw v. United States, 134 U.S. 99 (1890); Bailey v. Richardson, 182 F.2d 46 (D.C. Cir. 1950), *aff'd*, 341 U.S. 918 (1951). The Supreme Court stated in *Crenshaw* that "[an officer] enjoys a privilege revocable . . . at will . . . ." 134 U.S. at 108.

4. U.S. CONST. art. II, § 2.

5. *See, e.g.*, Keim v. United States, 177 U.S. 290, 293 (1900) ("The appointment to an official position in the Government, even if it be simply a clerical position, is not a mere ministerial act, but one involving the exercise of judgment. . . . Therefore it is one of those acts over which the courts have no general supervising power."); Tierney v. United States, 168 Ct. Cl. 77 (1964); Donnelly v. United States, 134 F. Supp. 635 (Ct. Cl. 1955).

6. McAuliffe v. New Bedford, 155 Mass. 216, 220, 29 N.E. 517, 518 (1892).

7. Although there would seem to be a practical difference between "merit" and "executive-political" appointments—such as a Commander in the Navy as opposed to the Secretary of State—*Keim* indicates that the discretionary function extends to all levels of the executive branch in matters of hiring, discharge, and promotion, without regard to the functional necessity of permitting the President to select his own staff.

power of the executive has been limited either by statutes, executive orders, or regulations that create employment discharge procedures and preferences in hiring.[8] Federal employees discharged in violation of these procedural requirements have been permitted to recover back pay even though the authority for the procedures created no specific cause of action.[9] In *Service v. Dulles*,[10] for example, the Supreme Court granted back pay to an employee of the Department of State whose discharge violated existing regulations promulgated by the Secretary. The Court held that the attempted dismissal was invalid because of procedural defects and ineffective as a discharge of a government officer.[11] The absence of an explicit creation of a cause of action in the regulations was rendered unimportant by the following analysis: the employee held a valid appointment as an officer of the government, and since there had been no valid exercise of the discretion to revoke his appointment, he remained for all purposes an officer and was entitled, therefore, to enjoy the primary benefit of the privilege of

8. *E.g.*, Veterans' Preference Act of 1944, ch. 287, 58 Stat. 387 (codified in scattered sections of 5 U.S.C.). 5 U.S.C. § 7501(a) (1970) provides: "An individual . . . may be removed or suspended without pay only for such cause as will promote the efficiency of the service." Veterans eligible for employment preferences, for example, are specifically granted the right to appeal to the Civil Service Commission from an adverse decision made in an action against them for cause. 5 U.S.C. § 7701 (1970).

9. Fletcher v. United States, 392 F.2d 266 (Ct. Cl. 1968) (discharge in violation of Post Office regulation allowing cross-examination of witnesses in administrative appeals); Mallow v. United States, 161 Ct. Cl. 207 (1963) (discharge procedurally defective because plaintiff was denied personal appearance guaranteed by Veterans' Preference Act of 1944, 5 U.S.C. §§ 7512(b)(2), 7701 (1970)); Daub v. United States, 292 F.2d 895 (Ct. Cl. 1961) (discharge in violation of Army personnel regulations).

10. 354 U.S. 363 (1957). The Secretary of State sought to dismiss an officer for disloyalty under the McCarran Rider, ch. 533, § 103, 65 Stat. 581 (1951), which authorized the Secretary to exercise absolute discretion to discharge "whenever he shall deem such termination necessary or advisable in the interests of the United States." Ruling that departmental procedural regulations applied, the Supreme Court found that the Secretary of State could exercise his McCarran discretion only "following *unfavorable* action in the employee's case by the Department Loyalty Security Board . . . and approval of the Board's action by the Deputy Under Secretary." 354 U.S. at 375.

11. *Id.* at 388. In United States *ex rel.* Accardi v. Shaughnessy, 347 U.S. 260 (1954), the Supreme Court found that a statement by the Attorney General prior to the Board of Immigration Appeals' recommendation on plaintiff's petition to suspend deportation might have prejudiced the Board's decision. Regulations required the Board to exercise its own judgment in all cases, including decisions that would be reviewed by the Attorney General. The Court stated that it "object[ed] to the Board's alleged *failure to exercise* its own discretion, contrary to existing valid regulations." 347 U.S. at 268. The *Accardi* principle is well stated by the Court in *Service*: "[R]egulations validly prescribed by a government administrator are binding upon him as well as the citizen, and . . . this principle holds even when the administrative action under review is discretionary in nature . . . . [B]ecause those regulations were violated . . . [plaintiff's] dismissal by the Secretary cannot stand." 354 U.S. at 372.

his office—the salary incident thereto.[12] The decisions in *Watson v. United States*[13] and *Glidden v. United States*[14] similarly indicate that violations of a statutory best evidence rule in an administrative proceeding and failure to state reasons for unsatisfactory discharge are denials of rights that will nullify attempted dismissals. Actions by federal employees to compel promotion—to recover back pay for a grade or status to which the employees had not been appointed—have not fared so well, however. These promotion cases in effect create a corollary to the discharge rationale and state that no person is entitled to the salary incident to an office to which he has not been appointed, even if the reason is negligent failure by the executive to exercise its discretion.[15] In *Gnotta v. United States*,[16] plaintiff brought an action for discriminatory failure to promote[17] in violation of Executive Order No. 11,246, the predecessor of Executive Order No. 11,478.[18] The Eighth Circuit, in discussing its role vis-a-vis judicial review,[19] determined that a judgment for plaintiff would be improper under the district courts' jurisdiction, which is concurrent with the Court of Claims',[20] because of a statute banning any court from reviewing discretionary agency actions.[21] The propriety of implying a remedy for the employee from the executive order was like-

12. Ganse v. United States, 376 F.2d 900 (Ct. Cl. 1967); Price v. United States, 80 F. Supp. 542 (Ct. Cl. 1948); Borak v. United States, 78 F. Supp. 123 (Ct. Cl.), *cert. denied*, 335 U.S. 821 (1948).

13. 162 F. Supp. 755 (Ct. Cl. 1958) (probationary employee).

14. 185 Ct. Cl. 515 (1968) (Air Force court-martial based upon summary of investigative report prepared in part by civilian police whom plaintiff had no opportunity to question).

15. United States v. McLean, 95 U.S. 750 (1878) (action by postmaster paid on commission basis for increment of volume handled despite failure of Postmaster General to readjust basis; judiciary held not competent to treat executive duties as performed when in fact neglected).

16. 415 F.2d 1271 (8th Cir. 1969), *cert. denied*, 397 U.S. 934 (1970).

17. Plaintiff alleged that his Italian ancestry prevented his promotion as an employee of the Army Corps of Engineers. The hearing officer found, however, that the evidence did not support the allegation of discrimination and the BAR agreed.

18. *See* note 2 *supra*. For a discussion of the history and antecedents of the executive orders in question see Farmer v. Philadelphia Elec. Co., 329 F.2d 3 (3d Cir. 1964).

19. The majority relied upon the basic presumption that administrative functions are reviewable, which was adopted by the Administrative Procedure Act, 5 U.S.C. § 702 (1970), and interpreted in Abbott Laboratories v. Gardner, 387 U.S. 136, 140 (1967).

20. *Compare* Tucker Act, 28 U.S.C. § 1346(a)(2) (1970) ("The district courts shall have original jurisdiction, concurrently with the Court of Claims, of . . . [a]ny other civil action or claim against the United States, not exceeding $10,000 in amount, founded either upon the Constitution, or any Act of Congress, or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort"), *with* 28 U.S.C. § 1491 (1970) (no monetary limitation).

21. "This chapter [judicial review] applies, according to the provisions thereof, except to the extent that . . . agency action is committed to agency discretion by law." 5 U.S.C. § 701(a)(2) (1970).

wise discussed and rejected on the intent of its authors. Although not discussed, the legislative history of section 7151 of title 5 of the United States Code,[22] the present statutory authority for the order, discloses that its origin is the first congressional treatment of discrimination in public and private employment—the Civil Rights Act of 1964.[23] Reviewing the apparently successful previous treatment by executive order[24] of discrimination in federal employment—an area otherwise devoid of statutory or decisional rules—Congress, in section 701(b), provided for the first time a statutory basis for such presidential orders, but at the same time specifically exempted the federal government from the civil liability imposed upon "employers" by the terms of Title VII for "unlawful employment practices" that incude any discrimination against individuals: discharge, refusal to hire or promote, different treatment, etc.[25] An additional problem posed by the *Gnotta* court was sovereign immunity, which, according to traditional views, cannot be waived by implication or by any division of the Government other than Congress.[26]

The instant court first examined the effect of the stipulation between the parties that but for defendant's racial discrimination, plaintiff would have received federal employment. Since the majority considered the stipulation equivalent to a concession that the discretionary functions of appointment already had been exercised favorably and exhausted when the hiring officer received the unfavorable reference report,[27] the court went on to consider whether Executive Order No. 11,478 properly could be the basis of an implied remedy. The court reasoned that since it previously had implied remedies for the violation of procedural rights guaranteed by departmental regulations in discharge situations, it similarly could imply a remedy in the instant situation on the basis of the executive order. Although it approved of the promotion cases in which recovery had been denied on the executive discretionary rationale, the majority did not consider them dispositive of the instant issue. Because the majority interpreted the stipulation to mean that no discretionary

22. "It is the policy of the United States to insure equal employment opportunities for employees without discrimination because of race, color, religion, sex, or national origin. The President shall use his existing authority to carry out this policy." 5 U.S.C. § 7151 (1970).

23. Pub. L. No. 88-352, 78 Stat. 241, 253-54. Since this portion of the Civil Rights Act of 1964 is now codified at 42 U.S.C. §§ 2000e to -15 (1970), as well as 5 U.S.C. § 7151 (1970), an investigation of the context of the section's enactment in search for congressional intent is difficult.

24. *See* Farmer v. Philadelphia Elec. Co., 329 F.2d 3 (3d Cir. 1964).

25. 42 U.S.C. § 2000e-2 (1970).

26. United States v. Shaw, 309 U.S. 495 (1940).

27. It appears that the discrimination occurred after the hiring officer normally would have made his final determination and/or did in fact determine to recommend plaintiff, but the temporal aspect of the factual situation and of the stipulation is somewhat unclear.

decisions remained to be made concerning plaintiff and that all such decisions already made had been favorable to plaintiff's application at the point in the hiring process at which the proscribed discrimination occurred, the majority concluded that only ministerial functions remained to be performed. The court thus considered its decision as neither reviewing nor performing a discretionary function, but merely as ascertaining what rights, if any, were created in plaintiff by the violation of Executive Order No. 11,478. Turning to those rights, the court next reasoned that since the executive order in question had been promulgated by the President with the knowledge of the court's existing jurisdiction, and since Congress intended general jurisdictional statutes to be controlling in the absence of a contrary manifestation,[28] the executive order and its statutory authority created in plaintiff a right to equal employment opportunity, the denial of which caused plaintiff to suffer a wrong at the hands of the SSA. In the absence of a statute expressly barring a remedy,[29] the majority concluded that the implication of a remedy would be proper. The majority reasoned that while it could not appoint plaintiff to office,[30] it could award money damages as compensation for a legal wrong and accordingly held that plaintiff was entitled to recover back pay.[31]

In an extended dissent, Judge Skelton[32] urged that the instant court

28. In United States v. King, 395 U.S. 1, 4 (1969), the Supreme Court reasoned that the absence of a clear indication that Congress did *not* intend the Declaratory Judgment Act, 28 U.S.C. §§ 2201, 2202 (1970), to apply to the Court of Claims was insufficient to confer jurisdiction to render such judgments. For a broad discussion of implied remedies see Note, *Implying Civil Remedies from Federal Regulatory Statutes*, 77 HARV. L. REV. 285 (1963). For a discussion of statutory construction based upon the type of statute involved see 2 J. SUTHERLAND, STATUTES AND STATUTORY CONSTRUCTION § 2801 (3d ed. 1943); 3 *id.* § 5818.

29. *See* notes 19 & 28 *supra*.

30. "If this court were to grant recovery to plaintiff it would in effect bestow upon plaintiff a promotion which he never reeeived. In doing so, this court would be making an administrative decision." Tierney v. United States, 168 Ct. Cl. 77, 80 (1964); *see* note 15 *supra*.

31. The majority cited Betts v. United States, 172 F. Supp. 450, 454 (Ct. Cl. 1970), for the proposition that absent authority to make appointments, the Court of Claims "does have jurisdiction to award . . . damages as compensation for violations of rights granted . . . by statute or regulation." The court, in awarding summary judgment to plaintiff, stated that it "hold[s] that plaintiff can recover *back pay* . . . less any amount she might have earned in the interim." 451 F.2d at 1054 (emphasis added).

32. Chief Judge Cowen also dissented, arguing that plaintiff had not been discriminated against in violation of statutory policy and the executive orders. He reasoned on the basis of Swift & Co. v. Hocking Valley Ry., 243 U.S. 281 (1917), that a stipulation "contrary to the facts shown in the record" may be rejected. 451 F.2d at 1058 (Cowen, C.J., dissenting). Referring to the hiring of another Negro to the position plaintiff otherwise would have obtained, Judge Skelton likewise found no violation of government equal opportunity policies: "If there was any discrimination, it was between two Negroes as individuals and without regard to race." *Id.* at 1086. Judges Skelton and Cowen both agreed with the hearing examiner that the hiring officer who refused to recommend

did not have jurisdiction to render judgment for plaintiff. Since plaintiff was never appointed to office, and since the executive department and not the courts have exclusive authority to appoint, Judge Skelton concluded that the majority in effect acted beyond the competence of the Court of Claims. Moreover, because there was no specific provision in the statute or executive order creating a cause of action, the dissent reasoned that none should be implied, and that if implied, such a cause of action would be nullified by the absence of an express waiver of sovereign immunity. Finally, Judge Skelton observed that since plaintiff's cause of action was based upon an alleged wrongful act of an officer of the Government in the exercise of his function, plaintiff was actually suing on conduct sounding in tort, over which the Court of Claims has no jurisdiction.[33]

The force of logic supports the reasoning that led Judge Skelton to conclude in his dissent that the Court of Claims was without jurisdiction to hear the instant case. Recovery in the typical discharge case generally has been premised on the fact that the employee held a valid appointment, which remained unrevoked because the disputed attempt to dismiss had been procedurally defective. Under this theory, the employee was on a par with any other employee of the Government, who, apparently forgotten when monthly checks were issued, seeks to recover the salary due him by virtue of his office—a situation sufficiently contractual in nature to fall within the jurisdiction of the Court of Claims. In a promotion suit, on the other hand, the discretion of the executive forms an absolute bar to recovery[34] because, by reason of the failure of the executive to appoint the employee, the greater salary sought is incident to an office that the employee does not hold. The dissent thus perceived the exercise of discretion in federal employment as an all-or-nothing proposition and rejected the majority's suggested intermediate position of a complete and favorable exercise of discretion without formal ap-

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plaintiff was under no duty or obligation to investigate the veracity of the unfavorable reference report submitted by plaintiff's former employer. Judge Davis, in his opinion concurring with the majority, addressed himself solely to the dissenting judges' treatment of the stipulation of discrimination, pointing out that the case had been pleaded and argued on the stipulation and that the administrative transcripts and investigative report on which the dissenters relied had not been part of the record because neither party had entered them. Despite his statement that the issue of discrimination was eliminated from the investigation of the court by the stipulation, Judge Davis determined under the rationale of Pettway v. American Cast Iron Pipe Co., 411 F.2d 998 (5th Cir. 1969), that plaintiff's rights indeed had been violated. 451 F.2d at 1057 (Davis, J., concurring).

33. 28 U.S.C. § 1491 (1970) limits the jurisdiction of the Court of Claims to "any claim against the United States . . . for . . . damages in cases not sounding in tort."

34. The majority deemed this bar to have been removed and would not have granted recovery but for this interpretation of the stipulation.

pointment. This infusion of a substantial performance doctrine into the question of executive hiring discretion, implied in the majority opinion, would be neither helpful nor appropriate. The dissent does not treat in any depth the validity of implying a remedy from Executive Order No. 11,478, but Judge Skelton's refusal to find such a remedy is readily supportable in light of the legislative history of the statutory authorization supporting the order.[35] It would be difficult indeed to argue that Congress, by specifically exempting the United States from the civil liability otherwise imposed for employment discrimination by Title VII of the Civil Rights Act of 1964, intended to imply this liability from a bare statement of the employment policy of the federal government.[36] Indeed, Senator Humphrey, in explaining the addition of this statement to the House version of the bill, indicated that it did not purport to create any new substantive law.[37] Even if Congress had intended or envisioned an implied remedy against the Government by its enactment of what is now section 7151 of title 5 of the United States Code, the requirement of an express and specific waiver of sovereign immunity was not met.[38] Perhaps the most interesting aspect of the dissent lies in Judge Skelton's denomination of the true nature of plaintiff's claim as tortious. An examination of the Federal Tort Claims Act[39] discloses that by the literal terms of this statute, Congress created an "executive discretion" exception, retaining immunity to actions which, like plaintiff's, were based upon the execution of a statute or regulation by an employee of the Government or upon the exercise of a discretionary function.[40] Even assuming the majority's premise that no discretionary elements are involved to bar recovery, the first portion of the exception remains unaf-

35. *See* note 23 *supra* and accompanying text.

36. *See* 5 U.S.C. § 7151 (1970).

37. UNITED STATES EQUAL EMPLOYMENT OPPORTUNITY COMMISSION, LEGISLATIVE HISTORY OF TITLES VII AND XI OF CIVIL RIGHTS ACT OF 1964, at 3004 (1966). M. SOVERN, LEGAL RESTRAINTS ON RACIAL DISCRIMINATION 66 (1966), stated that "Title VII's failure to repeat this substantive requirement [refraining from practicing racial discrimination] is, hy itself, unimportant; however, the exclusion means that victims of government discrimination are left to their old remedies. If Title VII offers something better, the failure to make it available to victims of government discrimination is regrettable."

38. *Cf.* United States v. Shaw, 309 U.S. 495 (1940) (no waiver of sovereign immunity by filing claim against estate, absent specific statutory permission to be sued).

39. Act of Aug. 2, 1946, ch. 753, 60 Stat. 842 (codified in scattered sections of 28 U.S.C.).

40. 28 U.S.C. § 2680(a) (1970). The section excludes from the coverage of the Act those claims "based upon an act or omission of an employee of the Government, exercising due care, in the execution of a statute or regulation . . . or based upon the exercise or performance or the failure to exercise or perform a discretionary function or duty on the part of a federal agency . . . ." In Dalehite v. United States, 346 U.S. 15, 32 (1953), the Supreme Court stated: "One only need read [28 U.S.C.] § 2680 in its entirety to conclude that Congress exercised care to protect the Government from claims, however negligently caused, that affected the governmntal functions."

fected by the logic of this premise. However, the presence of this exception implied that Congress considered such conduct tortious, and as the dissent forcefully points out, claims for damages in cases sounding in tort are specifically excluded from the jurisdiction granted the Court of Claims.[41]

The result reached by the majority at first glance would seem far reaching in its impact—the imposition of liability on the federal government for racial discrimination in violation of a job applicant's implied right to equal employment opportunity. On further examination it becomes clear, however, that the basis of this decision—the majority's evaluation of stipulated discrimination as an exclusion of discretionary elements of hiring—is in reality a highly restricted development. On a pragmatic level, it is doubtful whether such a stipulation will be made in the future, thus limiting recovery to instances when the plaintiff can prove both actual discrimination and full exercise of all discretionary elements of hiring in a manner favorable to the applicant. The majority's avoidance of any profound examination of the jurisdictional questions raised by Judge Skelton's dissent is perhaps more indicative of a sympathetic view of the issues involved and of a striving to achieve a just result than of an objective evaluation of the merits of the instant case. While it is apparent that some change is needed in the existing status of the law regarding the "rights" of federal employees, the instant decision is not sufficiently broad to afford any practical remedy for existing abuses and will serve mainly to stimulate forum shopping. In addition, given the size of the federal bureaucracy, it is doubtful that payment of a judgment in Washington will have great practical force in changing personal discrimination by federal employees in local offices throughout the nation. A statutory fine imposed upon discriminating government officials, payable directly to the victim, probably would be a more effective deterrent to such violations of federal policy than a reprimand from a distant superior.

41. 28 U.S.C. § 1491 (1970).

Securities Regulation—Section 5 of the Secnrities Act of 1933—Registration of Spin-off Distrihutions of Suhsidiary's Stock Required

Plaintiff, the Securities and Exchange Commission (SEC), sought to have defendants[1] enjoined from future distributions of subsidiaries' unregistered stock. The action was commenced after a series of transactions whereby four subsidiaries of defendant Harwyn, a publicly held corporation, obtained the assets of unaffiliated, nonpublic corporations in exchange for Harwyn's controlling interest in each subsidiary.[2] Following the asset acquisitions by the subsidiaries, Harwyn spun-off[3] to its own shareholders some of its retained and unregistered shares in the subsidiaries. The final step in these transactions was the development of an over-the-counter market in the spun-off shares.[4] By this method the previously nonpublic asset-contributing corporations were able to enter the public market without registration when shares of their newly acquired corporate shells were traded by Harwyn's shareholders.[5] Plaintiff contended that "spinning off" a subsidiary's unregistered shares in furtherance of a plan to convert the subsidiary into a publicly held corporation constituted a violation of the registration requirements in section 5 of the 1933 Securities Act.[6] Defendants argued that the registration

1. The SEC brought suit in fcderal district court under Securities Exchange Act of 1934, § 22, 15 U.S.C. § 78aa (1970), which provides that district courts of the United States have jurisdiction over any action brought by the SEC. There were 15 named defendants in the action, including Harwyn Industries, its officers, and the Harwyn subsidiaries and their officers.

2. SEC v. Harwyn Indus. Corp., 326 F. Supp. 943, 954 (S.D.N.Y. 1971).

3. In a spin-off the parent corporation declares a dividend to its stockholders. The dividend is paid in the form of shares of stock in subsidiaries of the parent. For a more detailed discussion of the spin-off transaction see H. SOWARDS, THE FEDERAL SECURITIES ACT § 2.02(2) (1971); *How Stocks Debut at the Back Door,* BUS. WEEK, Mar. 29, 1969, at 123.

4. In each of the 4 transactions the new management of the subsidiary facilitated the development of trading by listing the subsidiary's stock with the National Quotation Bureau for over-the-counter trading. 326 F. Supp. at 946.

5. A "shell corporation" is a publicly owned, once viable, enterprise whose assets have been dissipated so that little remains other than the corporate name. A "clean shell" is one without past debts or outstanding lawsuits. *How Stocks Debut at the Back Door, supra* note 3, at 123.

All 4 of the Harwyn subsidiaries involved here were shell corporations; however, the clearest example is that of Harwyn's subsidiary Motel. Motel was wholly owned by Harwyn, had never engaged in any significant business, and had no assets of any value. The company (Group V) seeking to go public transferred all of its assets into Motel and in exchange was issued controlling (80%) interest in Motel's stock. What stock Harwyn retained in Motel then was spun off to Harwyn's shareholders who proceeded to trade the stock on the public market, thus creating a market in it.

6. Securities Act of 1933 § 5(a)(1), 15 U.S.C. § 77e(a) (1970), provides: "Unless a registration statement is in effect as to a security, it shall be unlawful . . . directly or indirectly . . . (2) to carry or cause to be carried through the mails or in interstate commerce, by any means of instru-

requirements of the Act were applicable to spin-off transactions, asserting that such transactions were not "sales for value" within the meaning of section 2(3) of the Securities Act.[7] The district court *held,* judgment for plaintiff.[8] A spin-off, by a parent corporation, of a subsidiary's unregistered shares, when undertaken to create a public market in the shares, constitutes a sale that requires registration under the 1933 Securities Act. *SEC v. Harwyn Industries Corp.,* 326 F. Supp. 943 (S.D.N.Y. 1971).

The 1933 Securities Act was designed to protect investors by requiring complete disclosure of facts affecting stock issues through registration with the SEC prior to public sale.[9] Section 5(a)[10] renders unlawful all sales, through the mails or in interstate commerce, of any unregistered security. A sale is defined in section 2(3)[11] as including every contract of sale or disposition of a security, or interest therein, for value. The courts have interpreted the two provisions broadly, requiring registration whenever possible, in order to effectuate the purpose of the Act.[12] There are, however, two exemptions from the registration requirement that are pertinent here. The first appears in section 4(1), which exempts "transactions by any person other than an issuer, underwriter, or

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ments of transportation, any such security for the purpose of sale . . . ."

In addition to violation of the registration provisions, the SEC also alleged violation of the antifraud provisions of the 1933 and 1934 Securities Acts. These additional allegations were dismissed summarily by the court.

7. Securities Act of 1933 § 2(3), 15 U.S.C. § 77b(3) (1970), defines "sale" to include "every contract of sale or disposition of a security or interest in a security, for value." Securities Act of 1933, § 4(1), 15 U.S.C. § 77d (1970), however, provides: "The provisions of section 77e of this title shall not apply to—(1) transactions by any person other than an issuer, underwriter, or dealer."

8. The court, however, denied injunctive relief. Defendants had relied on past SEC inaction in spin-off situations, and had consulted legal counsel to ascertain the legality of the transaction and the proper legending of the stock issued to insiders as unregistered and for purposes of investment only. One defendant had sought the SEC's opinion but had received no answer. Under these circumstances the court found it would be inequitable to grant injunctive relief. *Cf.* Hecht Co. v. Bowles, 321 U.S. 321, 328-30 (1944).

9. SEC v. Ralston Purina Co., 346 U.S. 119, 124 (1953); A.C. Frost & Co. v. Coeur D'Alene Mines Corp., 312 U.S. 38, 40 (1941); Gilligan, Will & Co. v. SEC, 267 F.2d 461, 463 (2d Cir. 1959), *cert. denied,* 361 U.S. 896 (1959).

10. 15 U.S.C. § 77e (1970).

11. 15 U.S.C. § 77b (1970).

12. "The supplementary provisions and definitions are so designed as to prevent any circumvention of the registration requirement by devious and sundry means. This is one of the reasons for broad and liberal interpretations the courts have uniformly given to this particular phase of the Securities Act of 1933." SEC v. North American Research & Development Corp., 424 F.2d 63, 71 (2d Cir. 1970); *cf.* United States v. American Trucking Ass'ns, Inc., 310 U.S. 534, 543 (1940) (court looked to the legislative intent rather than the liberal meaning of the word "employee" as used in the Motor Carrier Act); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 861 (2d Cir. 1968), *cert. denied,* 394 U.S. 976 (1969) (Court broadly construed the phrase "in connection with the purchase or sale of any security" as it was used in § 15(c) of the Securities Exchange Act).

dealer."[13] The most inclusive of these terms—underwriter—is defined in section 2(11), for purposes of this exemption, as "any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking . . . ."[14] The policy supporting the exemption is to insulate sales by the ordinary investor from the registration requirement.[15] The second exemption, rule 133,[16] is relevant in the context of stock exchange transactions made pursuant to plans for mergers or consolidations. The rationale of the exemption is that when stockholders collectively authorize the corporate act, the element of individual consent required for a sale in the contractual sense is lacking.[17] In recent years the SEC has been increasingly concerned that the "no-sale" rule furnishes a vehicle for evasion of the Act's regulation provisions.[18] In *SEC v. Micro-Moisture*[19] this concern led to a successful action by the SEC to prevent use of the Rule 133 exemption when the merger and exchange of stock were merely steps in a larger plan by the controlling shareholders to market unregistered stock. Subsequently, in *Great Sweet Grass Oils Ltd.*,[20] the SEC declared the exemption totally inapplicable to this kind of transaction. The Commission held that when the issuer, or person acting on his behalf, has knowledge of a plan to market unregistered securities through shareholders, registration of the securities is required under section 5. Transactions meeting the requirements of the rule in appearance only were

13. 15 U.S.C. § 77d(1) (1970).

14. Securities Act of 1933 § 2(11), 15 U.S.C. § 77b(11) (1970).

15. "Congress clearly intended to exempt sales by the ordinary investor regardless of the derelictions [regarding registration] of his broker or dealer." 1 L. Loss, SECURITIES REGULATION 644 (2d ed. 1961).

16. SEC Rule 133, 17 C.F.R. § 230.133 (1971), provides in part: "(a) For purposes only of section 5 of the Act, no 'sale,' 'offer to sell,' or 'offer for sale' shall be deemed to be involved so far as the stockholders of a corporation are coneerned where, pursuant to statutory provisions in the state of incorporation, there is submitted to the vote of such stockholders a plan or agreement for a statutory merger or consolidation or reclassification of assets of such corporation to another person in consideration of the issuance of securities of such other person . . . ." For a more complete discussion of Rule 133 see Orrick, *Registration Problems Under the Federal Securities Act—Resales Following Rule 133 and Exchange Transactions,* 10 HASTINGS L.J. 1 (1958).

17. 1 L. Loss, *supra* note 15, at 521.

18. "It has become increasingly clear that the 'no-sale' rule, which is a rule of statutory construction or definition, has become an instrument of evasion of the law and a means by which illegal distributions of securities have been achieved in secrecy and in violation not only of the registration and disclosure provisions of the Securities Act and the Securities Exchange Act." SEC Securities Act Release No. 3698 (Oct. 2, 1956).

19. 148 F. Supp. 558 (S.D.N.Y. 1957), *final injunction granted,* 167 F. Supp. 716 (S.D.N.Y. 1958), *aff'd sub nom.*, SEC v. Culpepper, 270 F.2d 241 (2d Cir. 1959).

20. 37 S.E.C. 683 (1957).

strongly condemned.[21] The SEC has exhibited similar concern over use of the spin-off as a means to avoid sale characterization. When employed for that purpose, the spin-off prevents the distributing corporation from qualifying as an underwriter and allows the transaction to be included within the 4(1) exemption.[22] The House Reports on the original bill furnished a sound basis for the belief that spin-off distributions were exempt as transactions that did not constitute a sale.[23] In 1946 the SEC strengthened this view in a release stating that neither dividends nor distribution of securities to stockholders constituted a sale requiring registration.[24] Since that time, however, the SEC has attempted to close the gap, characterized by some commentators as a "loophole," in the registration requirements of the Act.[25] A 1969 release, for example, was issued for this purpose, but it was ambiguous and did not clearly apply to spin-offs of the *Harwyn* type.[26] Thus, although there had been no decision on the question whether spin-offs are sales requiring registration,[27] it appeared settled that, despite SEC objection, spun-off shares of a subsidiary's stock were exempt from registration.[28]

The instant court acknowledged at the outset that stock dividends do not normally constitute a sale and thus are not ordinarily within the purview of the section's registration requirement. The court distinguished the conventional stock dividend, however, from the instant spin-offs, asserting that in the principal case the primary purpose of Har-

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21. *Id.* at 691.

22. 15 U.S.C. § 77(d) (1970).

23. "The House provision exempting stock dividends . . . is omitted from the substitute [bill], since stock dividends are exempt without express provision, as they do not constitute a sale, not being given for value." H.R. REP. No. 152, 73d Cong., 1st Sess. 25 (1933).

24. The SEC further clarified the exemption with a release providing: "Neither the declaration of the dividend, nor the distribution of the securities to stockholders . . . would in my opinion constitute a sale within the meaning of the Securities Act, and no registration of the securities so distributed would be required under the Act." SEC Securities Act Release No. 929 (July 29, 1936).

25. "The availability of the spin-off remains as a dangerous loophole in the securities laws." Note, *The Spin-Off: A Sometimes Sale,* 45 N.Y.U.L. REV. 132, 143 (1970).

26. "Under such a pattern, when the shares are issued to a publicly owned or acquiring company, a sale takes place within the meaning of the Securities Act, and if the shares are then distributed to the shareholders of the acquiring company, that company may be an underwriter within the meaning of Section 2(11) of the Act as a person 'who purchased from an issuer with a view to . . . the distribution of any security' or as a person who 'has a direct or indirect participation in any undertaking.' " SEC Securities Act Release No. 4982 (July 2, 1968).

27. Note, *supra* note 25, at 132.

28. "The declaration of an ordinary stock dividend does not constitute a sale for the reason that there is no transfer for value. Similar reasoning should apply to a 'spin-off,' wherein the parent company declares a dividend to stockholders payable in the stock of its subsidiary. Such a dividend should not constitute a sale." 11 H. SOWARDS, *supra* note 3, § 2.02(2); *see* Bromberg, *Corporation Liquidation and Securities Law—Problems in the Distribution of Portfolio Securities,* 3 B.C. IND. & COM. L. REV. 1 (1961); *cf.* 1 L. LOSS, *supra* note 15, at 517-18.

wyn's distribution of its shares in its subsidiaries had been the creation of an active public market in the unregistered shares. Construing the spin-offs as a critical element in the ultimate achievement of the public market, the court held that the scheme must be considered in its entirety and not as a mere isolated distribution. The court then turned to the question whether Harwyn's spin-off distributions were given for value and whether they constituted a sale within the definition of section 2(3). Acknowledging the reasonableness of defendants' position to the contrary,[29] the court, nevertheless, concluded that defendants had received value for the unregistered spun-off shares by virtue of the public market created for the unregistered shares and the assets transferred to the subsidiaries. Because it found nothing in section 2(3) requiring that the value in a sale flow from the parties who receive the stock distribution, the court reasoned that Harwyn's distribution of the shares had been for value; thus the spin-off of the unregistered shares constituted a "sale." The court then determined that because of the sale Harwyn had qualified as an underwriter under section 2(11) and, therefore, was not entitled to an exemption from registration by reason of section 4(1). The court explained its holding by acknowledging that its interpretation of the statute was accomplished with an emphasis on the statute's broad purpose of providing adequate disclosure to members of the investing public. The only means of preventing the subversion of that purpose, the court concluded, was to refrain from "strangulating literalism"[30] and require that shares of subsidiaries' stock be registered prior to spin-off distributions.

In the instant decision the court sought to extend the Act's protection of investors and to close the spin-off "loophole" by treating the spin-off and its accompanying steps as a single transaction constituting a "sale for value."[31] The difficulty with this approach is that the value upon which the court relied is the establishment of a public market in the unregistered shares, which is dependent upon "fortuitous sales by shareholders of the [parent] corporation, and . . . is not really given by any one of them, but rather is *generated* by the shareholders acting as a group."[32] Value does not proceed from the distributees to the distributor, although commentators have stressed that it must in such cases.[33] Since

29. *See* note 8 *supra.*

30. 326 F. Supp. at 954.

31. *Id.*

32. Note, *supra* note 25, at 141 (emphasis in original).

33. "Apparently, no court has ever had occasion to say that a 'distribution' occurs only if the distributees give 'value,' but this is almost surely a correct statement." Bromberg, *supra* note 29, at 10.

the distributees do not give value for the shares, they are not within the protective scope of the Act.[34] Moreover, because they are not issuers, underwriters, or dealers, the Act places no limitation on subsequent sales by them.[35] By finding value in the instant case, however, the court effectively made the subsidiary the issuer and the parent corporation, both by definition and earlier releases,[36] a section 2(11) underwriter whose subsequent stock distribution required registration. The decision therefore constitutes a judicial expansion of the term "sale" beyond the scope of its intended meaning.[37] By expanding the definition of a "sale" *Harwyn* has introduced the possibility that legitimate transactions, such as normal stock dividends and even outright gifts of unregistered stock, will be subject to challenge on the same grounds as the distribution in the instant case. The intended result could have been attained, without resort to this dangerous extentsion of the term "sale," by applying the reasoning adopted in *Micro-Moisture* and *Sweet Grass*. Had the instant court construed the spin-off as an element of a plan to distribute unregistered stock to the public, it readily could have found that the issuer had had knowledge of the plan, and therefore it could have concluded that the parent had acted on behalf of the issuer. The subsequent spin-off distribution by the parent thus would have required registration. While a holding to that effect would provide the courts with considerable discretion in determining when a spin-off is only the final step in a plan to circumvent the registration requirement and would effectively close the spin-off loophole, it is subject to the same criticism as that which followed the *Sweet Grass* holding. The hypothetical holding in effect would close the loophole by reading the sale requirement out of section 5 registration provisions.[38] Before either of these approaches is widely adopted a more acceptable solution to the spin-off problem should be devised. While other means have been suggested,[39] the SEC's recently adopted

34. Note, *supra* note 25, at 141.

35. Securities Act of 1933 §§ 2, 4, 15 U.S.C. §§ 77(b), (d) (1970).

36. SEC Securities Act Release No. 3698 (Oct. 2, 1956).

37. "It [SEC] has sound precedent in the light of landmark decisions involving securities distributed subsequent to a merger and in its long-standing interpretation and treatment of secondary distrihutions in connection with Rule 133 . . . ." 11 H. SOWARDS, *supra* note 3, § 2.02[9].

38. "In any event, where the persons negotiating an exchange, merger or similar transaction have sufficient control of the voting stock to make a vote of stockholders a mere formality, Rule 133 does not apply. In such case the transaction is not corporate action in a real sense, but rather is action reflecting the consent of the persons in control, and consequently results in a 'sale' to them. Therefore, if an exemption from registration is available it must be found in the statute and cannot be based on Rule 133." Great Sweet Grass Oils Ltd., 37 S.E.C. 683, 691 (1957).

39. One suggestion is to borrow the "legitimate business purpose" test from tax law and to allow only spin-offs that are justified by a business reason. Note, *supra* note 25, at 143; Comment,

Rule 15(c)2-11[40] offers the most workable approach. Under this rule, the spin-off problem is met at the broker-dealer level. The rule makes it unlawful for any broker-dealer to submit a quotation to an interdealer quotation system unless the security has been the subject of bid-and-ask quotations on a regular basis within the last 30 days.[41] This rule prevents broker-dealers, without whom a market cannot be effectively established,[42] from creating active markets in the inactive stocks of shell corporations, the most frequent spin-off vehicle. In addition to the broad proscription against avoiding registration through stock spin-offs, the proposed rule includes an exception[43] that permits broker-dealers to establish a market in inactive stock if detailed information summaries concerning the issuer and the security are maintained and kept available. While under the exception it is still possible to create a public market in unregistered shares, the detailed information requirement will protect the public by providing as much information on which to base investment decisions as would have been available from a registration statement.[44] Thus the new rule should close the "back door" to the trading markets and protect the investor by assuring the availability of adequate information, at the same time the rule will prevent the establishment of a regulatory approach that could hinder legitimate spin-offs of subsidiary corporation shares.

Securities Regulation: Corporate Spin-offs As a Device for Public Distribution Without Registration, 42 U. COLO. L. REV. 111, 116-18 (1970), suggests using third-party beneficiary contract theory to bring spin-offs under § 2(3) as a "contract of sale or disposition of a security."

40. Wall Street J., Sept. 13, 1971, at 12, col. 1.

41. 35 Fed. Reg. 10597 (1970).

42. *Id.* at 10597-98.

43. In *Harwyn* the court noted that the spun-off securities were prepared for public trading by listing them with the National Quotation Bureau prior to distribution. 326 F. Supp. at 946.

44. Subparagraph (4) of the rule provides an exception to the 30-day limitation if the broker-dealer issuing the quotation makes available information including a current balance sheet, profit and loss statement for the past 2 years, number of shares issued and numbers outstanding, and members of the board of directors. 35 Fed. Reg. 10598 (1970).

Securities Regulatiou—Sectiou 13(d) of the Securities Exchange Act of 1934—A Group Owniug More Than Than Five Percent of a Company's Stock Must File Withiu Ten Days of its Formation

Appellant, GAF Corporation, filed a complaint in federal district court[1] alleging that appellees had violated section 13(d) of the Securities Exchange Act of 1934,[2] which requires any person or group acquiring more than ten percent[3] of a class of registered equity securities to file certain statements within ten days of the acquisition.[4] Appellees, four members of the same family, together owned approximately 10.25 percent of GAF's preferred shares outstanding, although no individual member owned more than ten percent. Appellant contended that appellees had pooled their interests to seize control of GAF, and that the group thus formed had acquired beneficial ownership of the stock formerly held by the group's members as individuals. Therefore, appellant maintained that the *group*, as an entity separate from its members, was obligated to comply with section 13(d).[5] Appellees asked that the complaint be dismissed under Rule 12(b)(6) of the Federal Rules of Civil Procedure. The district court granted this request, reasoning that the

1. GAF Corp. v. Milstein, 324 F. Supp. 1062 (S.D.N.Y. 1971).

2. 15 U.S.C. § 78m(d) (1970).

3. As of December 22, 1970, § 13(d)(1) was amended to require filing after the acquisition of 5% of a class of equity securities. 15 U.S.C. § 78m(d)(1) (1970).

4. Section 13(d) provides in pertinent part: "(d)(1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security . . . is directly or indirectly the beneficial owner of more than 5 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security . . . send to each exchange where the security is traded, and file with the Commission, a statement containing such of the following information . . .

(A) the background and identity of all persons by whom or on whose behalf the purchases have been or are to be effected;

(B) the source and amount of the funds or other consideration used or to be used in making the purchases . . .

(C) if the purpose of the purchases . . . is to acquire control . . . any plans or proposals which such persons may have to liquidate such issuer . . .

(D) the number of shares of such security which are beneficially owned . . .

(E) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer . . ."

. . . .

"(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for the purposes of this subsection."

5. Appellees contended that appellant did not have standing to assert a violation of § 13(d) or § 10(b). The court determined that appellant did have standing to assert a violation of § 13(d), but not to assert a violation of § 10(b).

mere formation of a group seeking control without acquiring additional stock does not require filing.[6] On appeal to the Second Circuit, *held*, reversed. The formation of a group owning more than ten percent of a class of equity securities of a corporation constitutes the acquisition of beneficial ownership of the securities by the group, and therefore is a reportable event under section 13(d) of the Securities Exchange Act of 1934. *GAF Corp. v. Milstein*, 453 F.2d 709 (2d Cir. 1971).

Section 13(d) was added to the Securities Exchange Act of 1934 by the Williams Act of 1968.[7] The latter Act, as originally introduced, was designed to reduce the growing number of corporate takeovers accomplished by stock acquisition.[8] Congress soon learned, however, that corporate takeovers are not necessarily detrimental to the public interest, and in fact, are often beneficial.[9] Therefore, Congress abandoned its negative view of corporate takeovers and used the bill to provide for investor protection during battles for corporate control.[10] The announced intent of Congress was to provide shareholders and the investing public with the information necessary to make informed investment decisions without "tipping the scales . . . in favor of management or in favor of persons making takeover bids."[11] In trying to fulfill this intent, the Act was specifically designed to deal with the two methods of corporate acquisition that previously had not been covered by securities law: (1) cash tender offers, and (2) open-market or privately negotiated acquisitions.[12] Section 13(d) was the congressional response to the latter.[13] Congress realized that an individual or group could acquire the power to influence or change management through large open-market or privately negotiated purchases without informing the investing public of its intentions toward the company. To avoid this situation, section 13(d) provides that any person or group acquiring more than five percent of a

6. 324 F. Supp. at 1068.

7. Act of July 29, 1968, Pub. L. No. 90-439, 82 Stat. 454, *amending* 15 U.S.C. §§ 78-*l*-n (1964).

8. In his floor speech Senator Harrison Williams (D., N.J.), who introduced the bill, stated: "In recent years we have seen proud old companies reduced to corporate shells after white-collar pirates have seized control . . . then sold or traded away the best assets, later to split up most of the loot among themselves." 111 CONG. REC. 28257 (1965).

9. It was pointed out in the Senate hearings that corporate takeovers often prove beneficial to shareholders by providing imaginative new management or by forcing old management to take innovative steps. *Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 120 (1967).

10. S. REP. NO. 550, 90th Cong., 1st Sess. 2 (1967).

11. 113 CONG. REC. 24664 (1967).

12. S. REP. NO. 550, *supra* note 10, at 3.

13. Requirements for cash tender offers are codified in 15 U.S.C. § 78n(d) (1970).

class of equity securities must file, within ten days after acquisition, a disclosure statement with the SEC, the target corporation, and the exchange on which the issuer's securities are traded.[14] Congress neglected, however, to define "acquisition" for the purpose of triggering the filing requirement of section 13(d), but the House and Senate Reports did address themselves directly to the issue of when a group should file. These reports emphasize that when a number of individuals who collectively own more than ten percent of a class of securities agree to act in concert, the group has become beneficial owner of the securities at the time of agreement.[15] The only case that had dealt with when a group has acquired ten percent of a class under section 13(d) was *Bath Industries, Inc. v. Blot*.[16] Blot, a member of the board of directors and a shareholder in Bath, had become dissatisfied with Bath's president and sought to have him removed. Encountering opposition from the other directors, Blot formed a group of individuals who controlled substantial voting interests in Bath stock. The group collectively owned more than ten percent of the company's stock, although no individual owned more than ten percent. Bath filed a complaint alleging violation of the filing and disclosure provisions of section 13(d). The district court held that the group should have filed within ten days of its formation.[17] When appealed, however, the Seventh Circuit held that disclosure is required "when, but only when, any group of stockholders owning more than 10% of the outstanding shares of the corporation agree to act in concert *to acquire additional shares*."[18]

The instant court stated that for the purpose of deciding whether the 12(b)(6) motion was properly granted, it must accept as true all the properly pleaded allegations in the complaint. Thus, given that appellees had formed a group owning more than ten percent of GAF's stock for the purpose of taking control, the court reasoned that the critical issue

14. This statement must also disclose the purchaser's identity, source of funds, existing arrangements as to shares, and any plans for control. *Id.* §§ 78m(d)(1), (3).

15. The House and Senate Reports state: "Section 13(d)(3) would prevent a group of persons who seek to pool their voting or other interests in the securities of an issuer from evading the provisions of the statute because no one individual owns more than 10 percent of the securities. The group would be deemed to have become the beneficial owner, directly or indirectly, of more than 10 percent of a class of securities at the time they agreed to act in concert. Consequently, the group would be required to file the information called for in section 13(d)(1) within 10 days after they agree to act together, whether or not any member of the group had acquired any securities at that time." S. REP. NO. 550, *supra* note 10, at 8; H.R. REP. NO. 1711, 90th Cong., 2d Sess. 8-9 (1968).

16. 427 F.2d 97 (7th Cir. 1970), *noted in* 71 COLUM. L. REV. 466 (1971); 45 N.Y.U.L. REV. 1136 (1970).

17. Bath Indus., Inc. v. Blot, 305 F. Supp. 526, 538 (E.D. Wis. 1969).

18. 427 F.2d at 109 (emphasis in original).

was whether there had been an acquisition by the group that would trigger the reporting section of the statute. Finding no definition of "acquisition" in the Act, the court turned to the dictionary and found that it means "to come into possession [or] control."[19] In determining whether the group came into possession or control of the members' stock, the court was not limited to examining legal title to the securities, which remained in the members, because section 13(d) requires filing by those acquiring *beneficial ownership* of the stock.[20] The court then analyzed the components of beneficial ownership of stock and found that, in battles for corporate control, the only relevant element is voting control. The court further reasoned that since the purpose of forming the appellee group was to seek corporate control, the group must have received the voting control of its members' stock. Thus the court found that the group, by gaining voting control of the stock, had obtained beneficial ownership of the stock, and this constituted "acquisition" under section 13(d). The court also noted that the history and purpose of the Act supported its holding. In conclusion, the court stated that the creation of an organized group of substantial stockholders was an occurrence with sufficient potential for changing or influencing corporate control that such an aggregation alone, without purchase of additional shares, would trigger the disclosure requirements of section 13(d).

The principal reason for the conflicting conclusions reached by the *Bath* court and the instant court is the different emphasis they placed on the two elements of congressional purpose behind section 13(d):[21] (1) to provide investor protection, (2) without favoring either management or persons seeking control. The *Bath* court, while recognizing the intent to protect investors, relied mainly upon the congressional desire to "avoid tipping the scales" as its justification for the strained interpretation given section 13(d).[22] That court rejected the two interpretations of the deadline for disclosure that are most consistent with the wording of the statute: (1) disclosure within ten days of the formation of the group, and (2) disclosure within ten days after acquiring additional shares.[23] Instead, it effected a judicial compromise by requiring disclosure after formation, but before the acquisition of additional shares.[24] Thus, the

19. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 18 (1961).

20. 15 U.S.C. § 78m(d)(1) (1970).

21. This possibility was suggested in Comment, *Section 13(d) and Disclosure of Corporate Equity Ownership*, 110 U. PA. L. REV. 853, 871 (1971), which provided a detailed analysis of § 13(d) and predicted the outcome of the instant case.

22. *Id.*; *see* 427 F.2d at 109; 71 COLUM. L. REV. 466, 473 (1971).

23. *See* Comment, *supra* note 21, at 869.

24. 427 F.2d at 109.

Bath court sacrificed sound statutory construction in favor of congressional neutrality in the struggle for corporate control. The instant court, on the other hand, placed its emphasis on investor protection. It realized that while Congress might have hoped that the statute would not aid either side in the conflict, the bill, as enacted, did give an advantage to incumbent management.[25] Furthermore, Congress was fully apprised of this result when it passed the Williams Act,[26] and apparently decided that investor protection deserved priority over strict neutrality. The instant court recognized that the mere formation of a group controlling more than ten percent of a class of stock constituted an event that indicated a significant possibility for change in the issuer's management and that as a result the investor should be notified as soon as possible. Thus the court found that the statute required disclosure within ten days of the formation of the group. Although the facts of the instant case are limited to a group formed for the purpose of seeking control, the court's holding and the legislative history in no way indicate that section 13(d) disclosure is limited to situations involving attempted corporate takeovers. The underlying principle of section 13(d) is that all new, rapidly accumulated aggregations of stock[27] are potentially influential in corporate matters, meriting investor notification regardless of the accumulator's motive. Whether such sweeping disclosure requirements are desirable remains to be seen. It is apparent, however, that when the instant decision is compared to *Bath*, it is superior for two basic reasons: (1) it chooses an interpretation that is consistent with the wording of the statute, and (2) it gives greater effect to the predominant legislative intent.

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25. *Hearings on S. 510, supra* note 9, at 127.

26. This point was made repeatedly in the Senate Hearings. *See, e.g., Hearings on S. 510, supra* note 9, at 114 (statements of Messrs. Fleischer, Kaplan, and Mundheim).

27. Section 13(d) provides an exception to filing for any person or group which has not acquired over 2% of the class of stock during the preceding 12-month period. 15 U.S.C. § 78m(d)(6)(B) (1970). This subsection also gives the SEC power to exempt acquisitions in which the purchasers do not seek control. *Id.* § 78m(d)(6)(D). The Commission has not yet promulgated rules to exempt such acquisitions.

State Police Power—Zoning—Validity of Local Ordinance Depends on Considerations of Regional, Not Merely Local, General Welfare

Plaintiffs sued to have the New Jersey Zoning Act[1] declared unconstitutional and to have a municipal zoning ordinance enacted thereunder declared invalid. The municipal ordinance provided that the floor sizes for over 55 percent of the acreage of the township could be no smaller than 1500 square feet and limited additional multifamily units to a total of 700.[2] Plaintiffs were six individuals, all with low incomes, representing a class of people living outside the municipality[3] who, because of the zoning restrictions in question, had been unsuccessful in seeking housing within it, and two developers who owned land in the municipality. Plaintiffs argued that the New Jersey Zoning Act thwarts the general welfare by failing to enumerate, as one of the Act's stated purposes, any provision for housing needs.[4] In addition, they contended that, even if the New Jersey Zoning Act is upheld, the municipal zoning ordinance is still deficient since it fails to promote reasonably the purpose of the Act with respect to single and multifamily housing. Defendant municipality maintained that the ordinance aims at the creation of a balanced community by encouraging moderate- and high-income housing to offset the existing low-income housing.[5] Defendant also argued that the ordinance seeks to

1. N.J. STAT. ANN. § 40:55-30 to -51 (Supp. 1971). Section 40:55-32 provides: "Such regulations shall be in accordance with a comprehensive plan and designed for one or more of the following purposes: to lessen congestion in the streets; secure safety from fire, flood, panic, and other dangers; promote health, morals or the general welfare; provide adequate light and air; prevent the overcrowding of land or buildings; avoid undue concentration of population. Such regulations shall be made with reasonable consideration, among other things, to the character of the district and its peculiar suitability for particular uses, and with a view of conserving the value of property and encouraging the most appropriate use of land throughout such municipality."

2. Madison Township Ordinance of Sept. 25, 1970. The ordinance imposes a minimum floor space requirement in zone R40 of 1500 square feet, and in zone R80 of 1600 square feet. The ordinance also restricts the acreage available to multifamily dwellings so that no more than 700 additional units can be built. Two-bedroom units cannot exceed 20% of the total units in any apartment development, and units with 3 or more bedrooms are not permitted. The ordinance further provides that no more than 200 units may be constructed in any year.

3. The nonresident plaintiffs obtained standing under N.J. STAT. ANN. § 40:55-47.1 (Supp. 1971), which provides that "any person, whether residing within or without the municipality, whose right to use, acquire, or enjoy property is or may be affected by any action taken under the act to which this act is a supplement, or whose rights to use, acquire, or enjoy property . . . under any other law of this state or of the United States have been denied, violated or infringed by an action or a failure to act" may bring suit under the New Jersey zoning provisions.

4. N.J. STAT. ANN. § 40:55-30 to -51.

5. The township conceded the invalidity of the numerical limitation on new multifamily units.

protect local drainage systems from the effects of high density residential development, which could lead to drainage problems and endanger water resources. The Supreme Court of New Jersey, Middlesex County, *held*, the ordinance is totally invalid. When a local zoning ordinance aims at excluding low income families from undeveloped areas of the municipality by unreasonably limiting the development of multifamily housing and by imposing size restrictions on residential lots, it is invalid under the New Jersey Zoning Act since it fails to promote a balanced municipality in accordance with the general welfare of the larger geographical region. *Oakwood at Madison, Inc. v. Township of Madison*, No. L-7502-70 (N.J. Super. Ct., Oct. 27, 1971).

Although zoning disputes have been the source of frequent litigation, the United States Supreme Court rarely has spoken on the subject. In *Buchanan v. Warley*,[6] a 1917 decision, it struck down a zoning ordinance that prohibited blacks from owning property in certain areas of the municipality on the ground that the ordinance violated the equal protection clause. In 1926, in the noted decision of *Village of Euclid v. Ambler Realty Co.*,[7] the Supreme Court upheld the constitutionality of a local zoning ordinance that was designed to limit the expansion of nearby industries into a suburban residential area. The Court, in resisting the due process attack on the ordinance, stressed the point that, under the police power of the state, a strong presumption of constitutionality existed in favor of such ordinances.[8] Two years later, in *Nectow v. City of Cambridge*,[9] the Supreme Court made its last pronouncement dealing with the constitutionality of a zoning ordinance. Echoing the rationale set forth in *Euclid*, the Court held that a zoning ordinance is invalid under the due process clause only "if it does not bear a substantial relation to the public health, safety, morals, or general welfare."[10] In the years since this group of decisions was handed down, there have been a number of demographic and economic changes in and around the larger metropolitan centers in this country that have prompted a serious reexamination of the function of zoning ordinances in our society. At the heart of these changes has been a steady stream of middle- and upper-income families moving from the central cities into the surrounding suburbs, where the population density is significantly less. This lower

6. 245 U.S. 60 (1917).
7. 272 U.S. 365 (1926).
8. *Id.* at 395.
9. 277 U.S. 183 (1928).
10. *Id.* at 188.

density results in a manageable demand for municipal services with which suburban governments are financially able to cope. The possibility of increased population in the suburbs, however, threatens to impair the present ability of most suburban governments to meet that demand. Acutely aware of this potential problem, suburban governments have responded by discouraging the development of inexpensive housing and multifamily dwellings because they fear that such property and its inhabitants will require more municipal services, primarily in the area of education, than taxes on the property can support.[11] Through the establishment of large minimum lot size and floor space requirements, suburban housing has been placed beyond the financial grasp of low-income urban families, thus effectively confining them to the inner city.[12] The ill effects of exclusionary zoning do not end there, however. Not only do the urban poor lose housing opportunities, they also lose job opportunities. As those who hold the better urban jobs move to the suburbs, the market for service-type jobs increases in the suburbs while it declines in the inner city. Since those who formerly held such jobs in the inner city cannot afford to move to the new suburban job locations because of zoning restrictions, there is a labor shortage in the suburbs and widespread unemployment in the inner city.[13] Opponents of exclusionary zoning maintain that through this zoning device the suburbs seek to enhance their own general welfare while ignoring the drastic effects that the pursuit of this aim might have on the welfare of the inhabitants of the inner city.[14] They contend that exclusionary zoning is unconstitutional and have based their argument on both equal protection and due process theories. The equal protection rationale, first applied in *Buchanan v. Warley*,[15] frequently has been utilized as a line of attack and has been successful in some cases in which it was claimed that a zoning ordinance was racially discriminatory.[16] In other factual situa-

11. One study, for example, conducted in the Parkway School District of St. Louis, Missouri, has calculated that any home valued at less than $26,274 will not generate enough taxes to support its share of the educational system. NATIONAL COMM'N ON URBAN PROBLEMS, BUILDING THE AMERICAN CITY, H.R. DOC. NO. 91-34, 91st Cong., 1st Sess. 215 (1969).

12. In the instant case, for example, the zoning ordinance in question made housing within the zoned areas so expensive as to be beyond the financial means of 90% of American families.

13. Reverse commuting—urban workers commuting to the suburbs to work—generally is precluded by cost and inconvenience. *See* Aloi & Goldberg, *Racial and Economic Exclusionary Zoning: The Beginning of the End?*, 1971 URBAN L. ANN. 9, 12.

14. *See* Sager, *Tight Little Islands: Exclusionary Zoning, Equal Protection, and the Indigent*, 21 STAN. L. REV. 767, 795 (1969).

15. 245 U.S. 60 (1917).

16. *See* Anderson v. Forest Park, 239 F. Supp. 576 (W.D. Okla. 1965).

tions, however, equal protection has been a rather impotent constitutional weapon. Under the rational basis test, which traditionally has been applied to zoning ordinances except when racial discrimination is alleged, municipalities have been able to justify their ordinances simply by showing a reasonable relation between the purpose of the ordinance and community general welfare.[17] Courts have been unwilling to find an equal protection violation when the ordinance has had the effect of discriminating on an economic basis. Under the fourteenth amendment, economic discrimination has been actionable only when it has resulted in the violation of a fundamental right, such as the right to vote,[18] or the creation of a suspect classification, such as race.[19] Since no court has held that exclusionary zoning produces either of those consequences, municipalities thus far have avoided the application of the compelling state interest test, which requires a greater showing of justification for a zoning ordinance than does the rational basis test. As a result, equal protection theory has not been a fruitful basis for assaulting exclusionary zoning. The other major method of attack has been the due process clause. All zoning ordinances are based on the police power of the state and enjoy a strong presumption of validity. The leading decision recognizing this idea is the *Euclid* case, in which the Supreme Court said that a zoning ordinance will not be held invalid unless proved to be "clearly arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare."[20] Although the position of the Supreme Court has not changed since *Euclid*,[21] some recent state decisions appear to be relaxing the presumption of validity by requiring the municipality to meet due process attacks on zoning ordinances with some justification for their enactment. The first of these was *Board of County Supervisors v. Carper*,[22] in which an entire county was zoned to forbid lots of less than two acres, even though the population problems that prompted the ordinance were shown to exist only in the eastern third of the county. Holding the ordinance invalid, the Virginia Supreme Court of Appeals stated that the police power does not give municipalities the right arbitrarily or capricously to deprive a person of the

17. *See* Nectow v. City of Cambridge, 277 U.S. 183 (1928); Village of Euclid v. Ambler Realty Co., 272 U.S. 365 (1926).

18. *See* Harper v. Virginia Bd. of Elections, 383 U.S. 663 (1966).

19. *See, e.g.*, Loving v. Virginia, 388 U.S. 1 (1967); McLaughlin v. Florida, 379 U.S. 184 (1964); Korematsu v. United States, 323 U.S. 214 (1944).

20. 272 U.S. at 395.

21. *See* Nectow v. City of Cambridge, 277 U.S. 183 (1928); Zahn v. Board of Pub. Works, 274 U.S. 325 (1927).

22. 200 Va. 653, 107 S.E.2d 390 (1959).

legitimate use of his property. This decision was followed by a series of Pennsylvania decisions firmly establishing in that jurisdiction the view that exclusionary zoning cannot always be justifed under the police power of the state. The trend-setting case was *National Land & Investment Co. v. Easttown Board of Adjustment*,[23] in which the Pennsylvania Supreme Court declared that "a zoning ordinance whose primary purpose is to prevent the entrance of newcomers in order to avoid future burdens, economic and otherwise, upon the administration of public services and facilities cannot be held valid."[24] Despite this favorable trend, it should be noted that serious procedural obstacles still face the opponents of exclusionary zoning. Besides overcoming the view prevailing in most jurisdictions that such zoning is within the police power, plaintiffs must overcome the standing barrier, which traditionally has prevented a nonresident from challenging zoning ordinances. Courts generally have upheld zoning ordinances if they promote the health, safety, morals, or general welfare of the persons *within a community*.[25] Even courts sympathetic to hearing constitutional attacks on exclusionary zoning have been unwilling to hold on equal protection or due process grounds that the standing concept should be broadened to include those who live outside the zoning municipality.[26]

The court in the instant case first considered plaintiffs' challenge to the constitutionality of the New Jersey Zoning Act. The court pointed out that to be constitutionally valid the Act must reasonably further the public health, safety, or general welfare. Under this standard, it concluded that even though the Act did not specifically include provision for housing needs as one of its stated purposes such a requirement reasonably could be implied, in order to further the general welfare.[27] On this basis, the court dismissed plaintiffs' challenge to the constitutionality of the Act. The court then turned to plaintiffs' claim that the local zoning ordinance in question is invalid because it fails to promote the purposes of the New Jersey Zoning Act. It noted that the ordinance

23. 419 Pa. 504, 215 A.2d 597 (1965).

24. *Id.* at 532, 215 A.2d at 612; *see* Concord Township Appeal, 439 Pa. 466, 268 A.2d 765 (1970) (absent extraordinary justification, a zoning ordinance with 2- and 3-acre minimum lot sizes is completely unreasonable). *But cf.* Fischer v. Township of Bedminster, 11 N.J. 194 (1952) (5-acre minimum lot sizes upheld as preserving the character of the community, maintaining its property values, and devoting the land to its most appropriate use).

25. *See, e.g., Ex parte* Ackerman, 6 Cal. App. 5, 91 P. 429 (Ct. App. 1907); Cook County v. Chicago, 311 Ill. 234, 142 N.E. 512 (1924).

26. *See, e.g.*, Lionshead Lake, Inc. v. Township of Wayne, 10 N.J. 165, 89 A.2d 693 (1952); Haar, *Zoning for Minimum Standards: The Wayne Township Case*, 66 HARV. L. REV. 1051 (1953).

27. No. L-7502-70 at 5.

makes housing in the affected areas so expensive that it is out of the economic reach of over 90 percent of all families in the county and in the nation. The court also noted that defendant municipality is seeking to attract new industry from the central cities and that exclusionary zoning in the suburb would tend to aggravate the crowding of the inner cities of the region by making it virtually impossible for the poor urban dweller to afford restricted suburban housing. The court concluded that the ordinance in question is fiscal zoning—an attempt to hold down the future cost of government services resulting from increased population. Nevertheless, in the court's estimation, the ordinance had to be judged on the basis of whether it provides a balanced plan for the region as a whole, and not on the basis of its fiscal objectives. Persuaded by the *National Land* decision, in which the court struck down large-lot zoning in undeveloped areas because of a lack of reasonable relation to the general welfare,[28] the instant court determined that "the general welfare does not stop at each municipal boundary."[29] It added that significant areas of vacant and developable land should not be zoned with such large minimum lot sizes that regional as well as local housing needs are shunted aside.[30] The court then considered defendant's drainage argument and noted that apparently no scientific study of the flood and drainage problems of smaller lots was made before passing the ordinance and that there was no evidence that those problems would be prevented by low population density zoning. The court also cited *National Land* for the proposition that a municipality cannot "stand in the way of the natural forces which send our growing population into hitherto undeveloped areas in search of a comfortable place to live."[31] Accordingly, it ruled that defendant, in enacting its zoning ordinances, had an obligation to consider the housing needs of not only its own citizens, but of those in the region as well.

While the instant decision at first glance seems disappointingly narrow because it does not rely on either of the familiar, traditional constitutional law mainstays—equal protection and due process—a closer analysis reveals that it has some startling and potentially significant implications. The instant court was afforded an opportunity to repudiate the traditional police power test for local zoning ordinances

28. The instant court distinguished Fischer v. Township of Bedminster, 11 N.J. 194, 93 A.2d 378 (1952), on the ground that most of the land in question here was vacant and therefore had no established residential character or residential property value.

29. No. L-7502-70, at 12.

30. *Id.*

31. 419 Pa. at 532, 215 A.2d at 612.

in reaching its decision, but chose not to do so. Instead, the court held that the general welfare, which must be considered in the passage of any state or local legislation, now means "regional general welfare" rather than merely the "general welfare of those residing within the boundaries of a municipality." The instant court in effect changed one of the statutory bases for justification under due process, rather than specifically changing the true constitutional test. Unquestionably, this new rationale marks a significant departure from prior law. If the concept of regional general welfare gains wide acceptance, it may provide opponents of exclusionary zoning with the legal weapon that they have been seeking to mount a successful challenge to the validity of such laws. On a practical level, the regional general welfare approach has at least three crucial advantages over the traditional equal protection and due process theories. First, it provides a possible method of circumventing the standing problem that heretofore has frustrated suits against exclusionary zoning. Even though standing was conferred by statute on the nonresident plaintiffs in the instant case,[32] one of the implications of the court's reasoning is that the same result would have been reached in the absence of the statute. The instant decision plainly recognizes that persons living outside municipal boundaries have certain recognizable interests in local zoning laws. The critical point, however, is that the instant court related this conclusion more to the idea of regional general welfare than to the statute. If the standing implications of the instant decision are not followed, then it seems that the expanded concept of general welfare is rendered meaningless since the rights presumably acquired through it could not be asserted by nonresidents of a community. Secondly, the concept of regional general welfare may lessen the formidable burden of proof problems that exclusionary zoning foes now face. One of the chief reasons is that under this expanded concept suburban municipalities will have to weigh interests that they never before have been compelled to consider. These new interests focus primarily upon the housing needs of persons living in the surrounding areas. Opponents of exclusionary zoning now may be able to turn this to their advantage. They could attack such zoning by showing that no consideration whatever was given these interests or that they were unjustifiably ignored. This approach contrasts sharply with establishing under traditional general welfare principles that an exclusionary zoning ordinance has no rational purpose, a task that has been futile far more often than not. Thirdly, the regional general welfare concept presents the basic issues in exclusionary zoning cases in

32. *See* note 3 *supra.*

a light that is true to the competing social and economic interests which usually are involved. If accepted, it means that courts no longer will draw the legal battle line between the suburb and an individual land developer. On the contrary, the battle line will be drawn between the suburb and the urban poor. This view of the issues seems to be the most realistic position that the courts could take and the one that is most conducive to a careful analysis of the case and a fair decision, whatever the ultimate fate of exclusionary zoning may be.

Regardless of the more practical consequences stemming from general acceptance of the regional general welfare concept, there are some broader aspects to the instant decision that should not be overlooked. As a judicial doctrine, the regional general welfare concept suggests consequences that courts must fully understand. If, indeed, it leads to the crumbling of suburbia's protective barriers, there will be an aftermath of bitterness. An end to exclusionary zoning strikes at the very heart of some of the most basic middle- and upper-class values; it may signal an end to the idea that a person can choose the type of community he wants to live in and be confident of its future desirability and continuity. Whether this change is right or wrong, strong resistance is sure to arise, and it is conceivable that it will resemble to a great degree the kind of resistance that has plagued school desegregation in this country since 1954. People may attempt to do by private means what exclusionary zoning formerly achieved for them as a matter of enacted law. In the final analysis, courts may be compelled to conclude that, even armed with the regional general welfare concept, they cannot eradicate all of the vestiges of exclusionary zoning. Yet, despite these potential drawbacks, it is most difficult to criticize the instant court for its conviction that the traditional zoning prerogatives of municipalities must give way to broader and more compelling social needs. Hopefully, the instant court's action will spur other courts to a similar understanding of the concept of general welfare. Unfortunately, that at best can be no more than an interim answer; in the end, only legislation, both state and federal, offers the potential for a comprehensive and enduring resolution[33] of the great issues now dividing the suburban rich and the urban poor.

33. *See* Note, *Constitutional Law—Equal Protection—Zoning—Snob Zoning: Must a Man's Home be a Castle?*, 69 MICH. L. REV. 339 (1970).

BOOK REVIEWS

Close Corporations Examined

CORPORATE AND TAX ASPECTS OF CLOSELY HELD CORPORATIONS. By William H. Painter. Boston: Little Brown & Co., 1971. Pp. xiv, 501. $30.00.

The dilemma of business planning is that to understand its parts it is first necessary to understand the whole, but to understand the whole it is necessary to understand its parts. Professor Painter has produced a book that is of substantial assistance to the lawyer or student confronting this dilemma. The method of attack employed by the author is to address simultaneously both the "parts" of business planning and the "whole" of business planning in a manner sufficiently concise to permit the reader to recall the first chapter of the book as he finishes the last. Yet the treatment is sufficiently detailed to enable the reader to gain more than a mere glimpse of the tax and corporate law problems involved.

The author describes the alternatives to the close corporation and the organization of a close corporation in the first and second chapters, explains control and operational matters in the middle chapters, and concludes with a discussion of a close corporation's first public offering and of the sale of a close corporation. The format selected sets forth the tax and corporate law aspects of the closely-held corporation in a readable and interesting fashion. It emphasizes the practical business context in which legal problems arise and uses examples liberally to illustrate the application of particular concepts. One of the author's most notable achievements is the concise, simple, and understandable statements of difficult concepts.

As the author acknowledges in his preface, the book draws heavily on specialized treatises such as Bittker & Eustice, *Federal Income Taxation of Corporations and Shareholders,* and Loss, *Securities Regulation.* In this regard, it is unfortunate that the timing of the publication of the book resulted in citations to the second edition of Bittker and Eustice, rather than the recently published third edition of that work.

As a research tool the book should prove useful in enabling the attorney to get an overview of the legal problems involved in the business planning problem that confronts him together with ample citations to more detailed works for further research into the problems he has identified. Also useful are the appendices of the book containing comparative summaries of the advantages and disadvantages of various alternatives

in business planning such as the decision to incorporate and methods of selling the business.

There are, however, two important omissions in the book. First, there is very little discussion of important accounting problems that may influence the decision of the business planner on a particular problem, especially with respect to pooling-of-interest or purchase method accounting for corporate acquisitions. Secondly, a discussion of the basic rules relating to corporate tax loss carryover would be of assistance in the chapter dealing with corporate acquisitions.

In summary, the author has accomplished his purpose of providing a concise, readable, and practical book on the wide range of tax, securities, and corporate law aspects of the closely held corporation. It is a book that will be of use to the general practitioner as well as the business specialist who wishes a broad overview of business planning problem areas. Were it not for the 30 dollar price, the book could be very useful to students as well. It is hoped that the publishers will produce a paperback student edition at a substantially reduced price.

JAMES T. O'HARE*

* Assistant Professor of Law, Vanderbilt University School of Law. B.A. 1963, J.D. 1965, Vanderbilt University.