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RECENT CASES

Antitrust—Sham Exceptiou—Allegations of Purposeful and Coucerted Use of Adjudicatory Processes to Harass aud Deter Parties From Having Free Access to These Processes Constitute a Cause of Action Under Antitrust Laws

Plaintiff, a trucking company, brought a class action under section 4 of the Clayton Act[1] against defendants, several common carriers, charging that defendants conspired to monopolize the transportation of goods in violation of antitrust laws.[2] Plaintiff alleged that defendants combined to institute state and federal administrative and judicial proceedings to resist and defeat applications by plaintiff to acquire or register operating rights.[3] It was further alleged that the purpose and effect of defendants' actions were to deprive plaintiff, a business competitor, of "free and unlimited" access to the adjudicatory and administrative tribunals and to destroy competition.[4] The district court dismissed for failure to state a cause of action.[5] The Court of Appeals for the Ninth Circuit reversed.[6] On certiorari to the United States Supreme Court, *held*, affirmed and remanded for trial. When, through a pattern of baseless and repetitive claims, one competitor seeks to deprive another of free and unlimited access to an administrative licensing agency, a cause of action exists under the antitrust laws. *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 935 (1972).

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1. 15 U.S.C. § 15 (1970). This section provides that a person who is injured in his business by anything forbidden in the antitrust laws may sue for treble damages in federal court.

2. *Id.*

3. In order to secure the necessary authorization, applicants had to appear before the California Public Utilities Commission and the Interstate Commerce Commission. Defendants conducted a jointly financed, well-publicized program of opposing all applications by actual or potential competitors. This program was financed through a joint trust fund with monthly contributions made on the basis of each defendant's income. As a result of defendants' activities, plaintiff's and other competitors' financial resources were depleted. Consequently, plaintiff and other competitors were discouraged from instituting and pursuing license applications.

4. Twenty-one out of a sample of 40 matters that had reached the decision stage resulted in action favorable to defendants either because the opposed application was denied in whole or in part, or because the application was withdrawn by the applicant after defendants appeared in opposition.

5. Trucking Unlimited v. California Motor Transp. Co., 1967 Trade Cas. ¶ 72,298, at 84,739 (N.D. Cal. 1967).

6. 432 F.2d 755 (9th Cir. 1970).

In 1961, the Supreme Court, in *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*,[7] held that concerted attempts to influence legislative or executive action are immune from the antitrust laws even though the governmental action sought would result in a restraint of trade.[8] The Court based this general rule of antitrust immunity upon two grounds. First, previous Supreme Court decisions had established that when a restraint of trade results from valid governmental action, there is no violation of the antitrust laws.[9] The Court observed that, as a corollary to this rule, attempts to persuade the executive or the legislative branches to take action resulting in such restraint of trade also should be immune from the antitrust laws.[10] Secondly, the Court stated that the application of the antitrust laws to defendants' activities, which were classified as "political,"[11] would violate their first amendment right to petition the government.[12] In 1965, the Supreme Court, in *UMW v. Pennington*,[13] granted antitrust immunity to conduct aimed at influencing the Secretary of Labor to establish minimum wage rates for certain employees and at changing a coal-purchasing policy of the Tennessee Valley Authority, a federal administrative agency. Although the Court could have granted immunity under the *Noerr* doctrine by classifying the conduct either as "political activity"[14] or as an attempt to secure a valid governmental restraint of trade,[15] it took a different approach. It interpreted *Noerr* as applying to conduct aimed at influencing all "public officials regardless of intent or pur-

7. 365 U.S. 127 (1961).

8. *Id.* at 136. The *Noerr* decision dealt with an alleged conspiracy by a group of railroads that had hired a public relations firm to conduct a publicity campaign designed to obtain the enactment of laws restricting the trucking business. This campaign was held not to be violative of the antitrust laws.

9. Parker v. Brown, 317 U.S. 341 (1943) (government program not violative of Sherman Act even though same program instituted by private individuals would be); United States v. Rock Royal Co-operative, Inc., 307 U.S. 533 (1939) (Secretary of Agriculture may fix minimum prices to be paid to milk producers).

10. Eastern R.R. Presidents Conf. v. Noerr Motor Freight, Inc., 365 U.S.127, 136-37 (1961).

11. *Id.* at 137. The Court noted that the people have a right to inform their representatives about matters that the government has the power to regulate.

12. *Id.* at 138.

13. 381 U.S. 657 (1965).

14. Since the conduct was aimed at changing a policy of the Tennessee Valley Authority, the Court could have found that defendants' actions were political because of defendants' right to inform the government about the matters with which they were concerned. *See* Comment, *Antitrust Immunity: Recent Exceptions to the Noerr-Pennington Defense*, 12 B.C. IND. & COM. L. REV. 1133, 1139 (1971).

15. Since defendants were trying to influence the formulation of a new policy, the conduct could have been characterized as an attempt to influence legislative action. *Id.*

pose,"[16] thereby suggesting that the *Noerr* immunity extended to conduct aimed at influencing not only the executive and the legislative branches but administrative and judicial officials as well. Although the general rule established in *Noerr* and extended in *Pennington* gives antitrust immunity to genuine attempts to influence governmental action, an exception to this rule has been recognized. The Supreme Court in *Noerr* stated that when "a publicity campaign, ostensibly directed toward influencing governmental action, is a mere sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of a competitor . . . ."[17] the antitrust laws would be applied. Since the *Noerr* Court went no further than this brief statement in its description of the kind of conduct that would result in loss of immunity, considerable dispute has arisen concerning the scope of the "sham" exception. One commentator contends that the sham exception is applicable whenever a direct injury to a competitor's business relationship with his customers results from the concerted action of the defendants.[18] Another commentator argues that the sham exception is far narrower because the *Noerr* decision's statement of the exception contemplated only publicity and lobbying campaigns, and because the exception's effect would be avoided by an affirmative showing that the anticompetitive effort was directed toward inducing the government to act.[19] In the few lower court cases[20] in which the sham exception has been raised, the latter reasoning appears to have been followed. The conclusiveness of these holdings on the scope of the sham exception, however, has been uncertain because the Supreme Court had not faced the question directly.

The Court initially observed that the instant case was similar to *Noerr*, and reaffirmed the general antitrust immunity rule of *Noerr* and *Pennington*. It declared that the rights of petition and association would be impaired if the mere advocacy of points of view before administrative agencies and the judiciary concerning the resolution of business interests among competitors were held to be a violation of the antitrust laws. According to the Court, however, plaintiff's allegations set forth con-

16. UMW v. Pennington, 381 U.S. 657, 669-71 (1965). In its discussion of the *Noerr* doctrine, the *Pennington* Court referred continually to "public officials." The Court has been criticized for using such broad terminology. *See, e.g.*, Note, *Antitrust: The Brakes Fail on the Noerr Doctrine*, 57 CALIF. L. REV. 518 (1969).

17. 365 U.S. at 144.

18. *See* Comment, *supra* note 14, at 1144.

19. *See* Note, *supra* note 16, at 528 n.77.

20. *See, e.g.*, Schenley Indus., Inc. v. New Jersey Wine & Spirit Wholesale Ass'n, 272 F. Supp. 872 (D.N.J. 1967).

duct beyond the scope of those protected activities. In considering the applicability of the sham exception, the Court read the complaint as alleging that defendants, for the purpose of destroying competition, combined to use the adjudicatory processes to harass plaintiffs and deprive them of "free and unlimited" access to those tribunals. The Court found specific allegations that before both the courts and the administrative licensing agencies, defendants opposed all applications for operating rights submitted by plaintiffs as well as other competitors. Observing that many forms of conduct can corrupt the administrative and judicial processes, the Court expressed its belief that a line must be drawn at some point between protected and unprotected activity. In its judgment, that point was reached when a pattern of baseless, repetitive claims in the administrative and judicial processes leads the factfinder to conclude that those processes have been abused. The Court then concluded that when such actions result in a denial of access to administrative agencies or to courts, they cannot acquire antitrust immunity either under the right to petition[21] or under the umbrella of "political expression." Observing that defendants' alleged activities were one way of building up a business empire and destroying another, the Court held that the allegations did state a cause of action which, if proved, would fall within the sham exception of the *Noerr* case, as adapted to the adjudicatory process.

Although the instant decision limits the *Noerr* first amendment right to petition, it is not a retreat from *Noerr*. In setting up the sham exception, the *Noerr* Court recognized that there might be instances when this right to petition could be limited. Even though *Noerr* protects those political rights basic to the workings of a representative government, and even though one of them—the right to petition—is involved in the instant case, prohibition of the abuse of that right still leaves defendants the opportunity to protect their interests through legitimate court and agency hearing appearances, lobbying, and the filing of amici briefs[22]—protected activities under *Noerr*. Since the instant decision is the first Supreme Court case to discuss and define the sham exception, it should clear up some of the confusion that arose concerning the exception's meaning and application.[23] At the very least, the decision

21. The Court recognized that defendants had a first amendment right to petition the administrative agencies involved concerning the operating license applications of competitive carriers. It said, however, that this constitutional right could not be used either to violate the antitrust laws or to achieve "substantive evils" which Congress had the power to control.

22. *See* Note, *supra* note 16, at 541 n.161.

23. *See* notes 18-20 *supra* and accompanying text.

shows that the exception is not limited to lobbying and other political expression activities, even though the language in *Noerr* setting up the exception could be construed to apply only to publieity campaigns and lobbying. Nevertheless, some difficulties with the sham exception remain. The Court failed to indicate speeifically what is meant by "an attempt to interfere directly with the business relationships of a competitor."[24] In determining the applicability of the sham exception, it fashioned a legal standard requiring a factual characterization. To determine whether a pattern of baseless claims has resulted in an abuse of either the administrative or judicial processes, the courts now must look to the realities of each case and the particular activities of the parties. As a result of this case-by-case approach, future decisions will face the problem of defining more concretely the kind of business injury that is actionable under the sham exception. Although somewhat misleading, the Court's only comment on this point suggests that plaintiffs will have a relatively easy task in showing the requisite degree of injury. Access to the adjudicatory processes was considered vital to a business's ability to operate, and any interference with that right was sufficient in the Court's judgment to establish an antitrust violation.[25] It should be noted, however, that plaintiffs probably had an easier task in stating a cause of action than can be expected generally. The instant decision involves an extreme example of what has been traditionally characterized as abuse of the judicial process.[26] A less clear-cut case perhaps would necessitate a more penetrating inquiry by a court into defendant's alleged interference with a competitor's business relationships. Just where the line should be drawn between protected and unprotected activity under the *Noerr* rationale is a problem that the Supreme Court did not directly confront. Resolution of this problem will require a standard that is flexible enough to protect all legitimate political activity. This protected activity should include efforts to persuade legislatures to enact laws and courts to interpret them even when anticompetitive ends might be served. Activity that the instant decision is designed to prohibit involves something more than this persuasion. It involves a concerted

24. Eastern R.R. Presidents Conf. v. Noerr Motor Freight, Inc., 365 U.S. 127, 144 (1961).

25. For a discussion of the nature of the injury required see Comment, *supra* note 14, at 1143-44.

26. Abuse of the adjudicatory process for anticompetitive ends violates the antitrust laws. *See, e.g.*, United States v. Singer Mfg. Co., 374 U.S. 174 (1963) (patent infringement proceedings before the United States Tariff Commission to exclude Japanese competition); Woods Exploration & Producing Co. v. Aluminum Co. of America, 438 F.2d 1286 (5th Cir. 1971) (submission of false gas production forecasts to a regulatory agency when these forecasts are used to determine standards).

effort by defendants to accomplish through harassing tactics what they otherwise would not have been entitled to achieve on the merits of their claims. In short, through the subterfuge of frivolous objections, defendants sought to do more than influence or persuade the licensing agencies to deny plaintiffs' applications. They sought ultimately to force plaintiffs to quit trying to do business altogether. Thus, in a sense, defendants arrogated to themselves the power to dictate a decision that they were only entitled to advocate or support. If the distinction between protected and unprotected activity under *Noerr* is maintained along the lines suggested, the basic policy of the antitrust laws to maintain competition will be advanced. The relative economic strengths of businesses, particularly with respect to their ability to litigate extensively,[27] should become less important as a factor in the responsiveness of administrative agencies to the individual industries or businesses. At this point, it is not clear whether the Supreme Court will approach the sham exception with such a policy in mind. All that can be said is that the approach is reasonable and has not been foreclosed, and that further litigation will be necessary to resolve this unsettled issue.

Criminal Procedure—Coufessions—Determination of Confession's Voluntariness by Preponderance of the Evidence Is Not Violative of Fifth Ameudment Prohihition Against Self-Incrimination

Petitioner challenged his state conviction for armed robbery by seeking a writ of habeas corpus in federal district court. In a pretrial motion to suppress, petitioner had disputed the voluntariness of his confession to an armed robbery.[1] With the jury removed,[2] the trial court heard conflicting testimony regarding alleged police coercion preceding

27. For a discussion of this point in connection with the lower court opinion see Comment, *supra* note 14, at 1145-46.

1. Petitioner did not deny making the confession or question its validity. Furthermore, petitioner did not maintain that his confession or its voluntariness was an element of the crime of armed robbery.

2. The Supreme Court in Jackson v. Denno, 378 U.S. 368 (1964), held that an accused has a due process right to a reliable determination of the voluntariness of a confession by the trial court outside the jury's presence. *See* note 15 *infra*.

petitioner's confession[3] and later ruled that, by a preponderance of the evidence, the confession was admissible.[4] Petitioner was found guilty and the conviction was upheld on direct appeal to the Illinois Supreme Court.[5] His subsequent petition for habeas corpus contended that the fifth[6] and fourteenth[7] amendments to the Constitution require that the voluntariness of a confession be determined beyond a reasonable doubt.[8] The district court denied relief,[9] and the Seventh Circuit affirmed.[10] On writ of certiorari to the United States Supreme Court, *held,* affirmed. In determining the voluntariness of a confession, neither the fifth amendment's prohibition against compulsory self-incrimination nor the fourteenth amendment's due process clause requires proof by more than a preponderance of the evidence. *Lego v. Twomey*, 404 U.S. 477 (1972).

There is no question that an accused's confession is frequently a crucial item in the proof of guilt and is certainly one that has impressive

3. Petitioner testified that, after arrest and while in police custody, he was beaten by the local police chief with a gun butt. His explanation of this treatment was that the police chief, a neighbor and former schoolmate of the robbery victim, had sought revenge against him. Petitioner introduced into evidence a photograph of himself, taken the day after his arrest, which showed his face in a swollen and bloodied condition. Petitioner admitted, however, that his face had been scratched in a scuffle with the robbery victim, but he maintained that this encounter did not produce the injuries shown by the photograph. The police chief and 4 other officers denied beating or threatening petitioner and disclaimed knowledge that any other officer had done so.

4. While the trial court did not articulate the standard utilized in determining voluntariness, Illinois law allows the admission of a confession if the judge first finds by a preponderance of the evidence that it is voluntary. *See, e.g.*, People v. Wagoner, 8 Ill. 2d 188, 133 N.E.2d 24 (1956). The jury subsequently was instructed on the prosecution's burden of proving guilt, but not regarding a requirement that the confession be found voluntary before it could be used to prove guilt or innocence. Since only the trial court considers voluntariness, Illinois follows the Orthodox or Wigmore rule. *See* note 14 *infra* and accompanying text.

5. People v. Lego, 32 Ill. 2d 76, 203 N.E.2d 875 (1965).

6. The fifth amendment provides: "No person . . . shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property without due process of law . . . ." U.S. CONST. amend. V.

7. The fourteenth amendment's due process clause makes the fifth amendment applicable to state proceedings. Malloy v. Hogan, 378 U.S. 1 (1964) (incorporation of fifth amendment proceeded on a clause-by-clause basis, with the *Malloy* decision holding that the fifth amendment privilege against self-incrimination was applicable to the states through the fourteenth amendment due process clause).

8. Petitioner cited *In re* Winship, 397 U.S. 358 (1970), as a case standing for the proposition that every fact necessary to constitute a crime must be proved beyond a reasonable doubt. Petitioner further contended that the use of the preponderance standard was in contravention of values protected by the exclusionary rules.

9. Following an initial denial for failure to exhaust state remedies, petitioner's claim was denied relief on the merits by the district court. United States *ex rel.* Lego v. Pate, 308 F. Supp. 38 (N.D. Ill. 1970). Respondent did not contend petitioner deliberately bypassed state procedures in order to test his constitutional claims.

10. Lego v. Pate (7th Cir. 1970) (unreported).

weight with the jury.[11] Consequently, the admission of an involuntary confession is constitutionally prohibited by the fifth amendment's guarantee against self-incrimination.[12] Because of this guarantee, when the accused raises an objection, a determination of voluntariness has been required before admitting his confession into evidence.[13] Prior to 1964 there were three generally recognized means of deciding the admissibility of an allegedly involuntary confession, often referred to as the Massachusetts, Orthodox, and New York procedures.[14] In jurisdictions following the Massachusetts approach, the trial court must first adjudge the confession to be voluntary before it will be submitted to the jury, which then must make its own determination of voluntariness. The Orthodox or Wigmore procedure requires the court to be the sole and final arbitrator of voluntariness. Under the New York procedure, the trial court may exclude the confession only if there is no conflicting evidence on the issue of voluntariness. Otherwise, the jury is instructed it must first determine the voluntariness of the confession before it may consider any probative value contained therein. In 1964, the Supreme Court, in *Jackson v. Denno*,[15] discredited the New York procedure, holding that submission of the question of voluntariness to a jury with-

11. *See generally* Clifton v. United States, 371 F.2d 354, 360 (D.C. Cir. 1966) (Leventhal, J., concurring), *cert. denied*, 386 U.S. 995 (1967); Note, *The "Reasonable Doubt" Standard in Preliminary Proceedings To Determine the Voluntariness of a Confession*, 42 TEMP. L.Q. 60 (1968); 18 AM. U.L. REV. 453 (1969).

12. The common-law justification for the exclusion of an involuntary confession was its "testimonial unworthiness." 3 J. WIGMORE, EVIDENCE § 822 (Chadbourn 3d ed. rev. 1970). In Brown v. Mississippi, 297 U.S. 278 (1936), however, the Supreme Court commenced to adopt a due process rationale for exclusion. In Lisenba v. California, 314 U.S. 219 (1941), and Ashcraft v. Tennessee, 322 U.S. 143 (1944), the Court abandoned probative value as a criterion for exclusion. The Court in Malinski v. New York, 324 U.S. 401 (1945), added a new and developing notion that oppressive enforcement practices should be eliminated by increased protection of individual rights. The general rights of the individual in the admission of a confession were emphasized in recent cases such as Miranda v. Arizona, 384 U.S. 436 (1966), and Sims v. Georgia, 385 U.S. 538 (1967).

13. "It is now axiomatic that a defendant . . . is deprived of due process of law if his conviction is found, in whole or in part, upon an involuntary confession, without regard for the truth or falsity of the confession . . . and even though there is ample evidence aside from the confession to support the conviction." Jackson v. Denno, 378 U.S. 368, 376 (1964). *See also* Rogers v. Richmond, 365 U.S. 534 (1961) (voluntariness not determined by a confession's reliability).

14. As of 1964, the New York procedure was followed by 15 states, the Orthodox procedure by 20 states, and the Massachusetts approach by 15 states. For a specific enumeration of the states subscribing to each rule see Jackson v. Denno, 378 U.S. 368, 410-23 (1964) (appendices to the opinion of Black, J., concurring in part, dissenting in part).

15. 378 U.S. 368 (1964). The *Jackson* decision overruled Stein v. New York, 346 U.S. 156 (1953), which had upheld the New York procedure on the ground that: (1) the jury will find the confession to be voluntary; or (2) the confession will be found involuntary and therefore disregarded according to the trial court's instructions.

out a trial judge first having made an independent determination on the issue is violative of the due process clause of the fourteenth amendment for failure to provide a "reliable determination" of voluntariness.[16] The Court reasoned that the jury, although properly instructed, might confuse evidence pertaining to the separate questions of voluntariness, veracity, and the accused's guilt or innocence.[17] The Court, therefore, held that each state's procedures "must . . . be fully adequate to insure a reliable and clear-cut determination of the voluntariness of a confession, including the resolution of disputed facts upon which the voluntariness issue may depend."[18] The *Jackson* decision, while sanctioning the Orthodox and Massachusetts procedures, in which the trial judge makes at least an initial determination on voluntariness,[19] did not require that the factfinder be bound by any specific standard of proof.[20] Consequently, since *Jackson,* both state and federal courts have split on whether a preponderance of the evidence or a reasonable doubt standard[21] is appropriate to the voluntariness hearing. While numerous opinions have addressed themselves to the relative merits of the two standards,[22] the District of Columbia Court of Appeals in *Clifton v. United States*[23] and *Pea v. United States*[24] provided accurate synopses of the arguments put forward by the proponents of each standard. In *Clifton*, the majority opinion, written by then Circuit Judge Warren Burger, adopted a preponderance of the evidence standard. Noting that the determination of a confession's voluntariness is "in substance, a ruling on its admissibility as evidence,"[25] Judge Burger reasoned that neither civil nor criminal procedure in any jurisdiction requires admissibility to be judged by the reasonable doubt standards.[26] Since *Jackson* requires

16. 378 U.S. at 376-77.

17. *Id.* at 383-84.

18. *Id.* at 391. The Court noted that the guarantee of an independent determination of voluntariness did not dictate whether the trial judge, another judge, or another jury should make the decision, so long as the issue was not resolved by the convicting jury. *Id.* at 391 n.19.

19. *Id.* at 391 n.19; *see* Note, *supra* note 11.

20. This omission is mentioned specifically by Justice Black in his opinion in *Jackson.* 378 U.S. at 404-05. *See also* Note, *supra* 11. Apparently the omission was intentional. Lego v. Twomey, 404 U.S. 484 (1972).

21. For a discussion on the relative meanings of the standards see United States v. Schipani, 289 F. Supp. 43 (E.D.N.Y. 1968).

22. For an exhaustive listing of the states and cases adhering to each standard see Lego v. Twomey, 404 U.S. 479 n.1 (1972).

23. 371 F.2d 354 (D.C. Cir. 1966), *cert. denied,* 386 U.S. 995 (1967).

24. 397 F.2d 627 (D.C. Cir. 1968) (rehearing en banc).

25. 371 F.2d at 357-58.

26. *Id.* at 358. Judge Burger did not find any reason why the confession should be singled out for a unique standard of appraisal. Nor did he deem the impact of a confession upon the jury more harmful than that of other damaging utterances, such as inconsistent statements and admis-

no more than a "reliable determination," he found that "conventional admissibility criteria" are adequate to protect the defendant.[27] Additionally, Judge Burger argued that adoption of a unique standard of appraisal for confessions would denigrate the historic role of the juror as the finder of fact.[28] In conclusion, the majority held that the trial judge must be "satisfied" that the confession was made voluntarily.[29] Although he concurred in the result, Judge Leventhal in *Clifton* felt that the reasonable doubt standard should be applied to the voluntariness hearing. Following the rationale of the Fourth Circuit in *United States v. Inman*,[30] Leventhal deemed the question of voluntariness to be so significant in the final assessment of guilt or innocence that the standards applicable in proving the elements of the crime should govern this determination, and should not be relegated to the evidentiary level.[31] Leventhal argued that *Bram v. United States*,[32] which held that any doubt regarding voluntariness was to be resolved favorably to the accused,[33] requires usage of the reasonable doubt standard. Because a confession often represents the foundation of the prosecution's case, Leventhal contended that the stringent constitutional safeguards otherwise afforded confessions[34] necessitate a standard commensurate with that applied to guilt itself.[35] Adopting Leventhal's rationale, the District of Columbia Circuit reversed *Clifton* in *Pea v. United States*,[36]

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sions, which are admitted by the conventional rules of evidence. *Id.* at 358. Burger then addressed himself to the statement in Bram v. United States, 168 U.S. 532, 565 (1897), that "any doubt as to whether the confession was voluntary must be determined in favor of the accused . . . ." It appears that Judge Burger felt that this statement did not establish a quantitative standard for the admission of confessions, but rather that its plain meaning merely reflected a general constitutional policy adverse to confessions.

27. 371 F.2d at 359.

28. *Id.* at 358. Judge Burger emphasized that for a generation, judicial trends had excluded evidence from the jury. Trial judges had become greatly overburdened, judging the "processes outlined in *McNabb, Mallory, Escobedo, Massiah,* and *Miranda.* The prospects now are that trial judges . . . will not be overworked in passing on the voluntariness of the few confessions which will survive the application of these cases." *Id.* at 360. This usurpation of the jury's fact-finding function was noted by Justice Black in *Jackson.* 378 U.S. at 404-05.

29. 371 F.2d at 359-60.

30. 352 F.2d 954 (4th Cir. 1965).

31. 371 F.2d at 362.

32. 168 U.S. 532 (1897).

33. *Id.* at 565. *See generally* Chapman v. California, 386 U.S. 18 (1967) (before a federal constitutional error can be held harmless, the court must believe it to be harmless beyond a reasonable doubt).

34. *See generally* Miranda v. Arizona, 384 U.S. 436 (1966) (enumerates rights of accused during custodial interrogation and admissibility of confessions taken in derogation of constitutional guarantees).

35. 371 F.2d at 362.

36. 397 F.2d 627 (D.C. Cir. 1968).

The majority in *Pea* reemphasized the practical significance of a confession in the minds of the jurors when they determine guilt or innocence.[37] Most recent cases, however, have favored the preponderance standard.[38] They emphasize that, although the prosecution must prove every essential element of the alleged offense beyond a reasonable doubt, it cannot be argued that every fact decided by a jury must be measured by this standard, and voluntariness is not among these essential elements.[39] In substantiation of this position, it has been noted that a recent Supreme Court decision, *In re Winship*,[40] held that only every fact *necessary* to constitute a crime must be proved beyond a reasonable doubt.[41] From this, it is argued that only those questions directly relating to guilt must be determined beyond a reasonable doubt.[42]

The Court initially stated that the purpose of its holding in *Jackson v. Denno* was to prohibit the admission into evidence of involuntary confessions, because such admission contravenes an accused's fifth amendment rights. The Court also noted that the *Jackson* decision was not based on a desire to enhance the reliability of findings of guilt and hence it offered no support for judicial invasion of the fact-finding function of the jury. The Court next concluded that *In re Winship*[43] was inapplicable since *Winship* requires proof beyond a reasonable doubt of the elements of a crime,[44] and a confession is not such an element. Concerning petitioner's contention that usage of the preponderance standard is inconsistent with the values protected by the exclusionary rules, the Court simply stated that its experience had indicated that no harm to individual federal rights attended use of the less stringent standard. The Court also noted that the exclusionary rules attempt to prevent improper police conduct, but reasoned that an escalation of the applicable standard of proof would not be sufficiently productive in this respect to outweigh the "public interest in placing probative evidence

37. *Id.*

38. *See, e.g.*, Duncan v. State, 278 Ala. 145, 176 So. 2d 840 (1965) (evidence sustaining a prima facie case of voluntariness sufficient for admission); People v. Harper, 36 Ill. 2d 398, 223 N.E.2d 841 (1967) (state must show voluntariness by a preponderance of the evidence); Commonwealth v. Rundle, 429 Pa. 141, 239 A.2d 426 (1968) (only the essential elements of a crime, which do not include a confession's voluntariness, must be proved beyond a reasonable doubt); Monts v. State, 218 Tenn. 31, 400 S.W.2d 722 (1966) (confession admissible if based on "reliable" evidence signifying voluntariness). *But cf. In re* Winship, 397 U.S. 358 (1970) (every fact necessary to constitute a crime must be proved beyond a reasonable doubt).

39. *See, e.g.*, Commonwealth v. Rundle, 429 Pa. 141, 239 A.2d 426 (1968).

40. 397 U.S. 358 (1970).

41. *Id.* at 364.

42. *See* cases cited note 38 *supra.*

43. 397 U.S. 358 (1970).

44. *Id.* at 364.

before juries for the purpose of arriving at truthful decisions about guilt and innocence."[45] The Court held, therefore, that the Constitution permits the voluntariness of a confession to be determined by a preponderance of the evidence.

Justice Brennan, dissenting,[46] reasoned that the clear unconstitutionality of admitting an involuntary confession demands protection for the individual beyond that offered by the preponderance standard. Noting that the voluntariness hearing is, in practicality, the final resolution of the factual conflict on the voluntariness issue, the dissent reasoned that adoption of a lower standard necessarily would increase the probability of convicting innocent defendants. The dissent concluded that compelled self-incrimination is so alien to American jurisprudence that the fifth amendment guarantee requires a reasonable doubt standard for the independent determination of voluntariness.

The significance of the instant case lies much more with the values expressed than with its factual result. It cannot be denied that the Court could have found adequate authority to mandate the reasonable doubt standard. Justice Leventhal's opinions in *Clifton* and *Pea* typify the persuasive constitutional arguments for the more stringent standard. This line of reasoning, which is reflected in the dissent in the instant case, emphasizes the constitutional danger present in the *possible* admission of an involuntary confession. It concludes that only by imposing the reasonable doubt standard upon the voluntariness hearing can the ideal of total exclusion of involuntary confessions be approached. This methodology is indicative of the Warren Court and its landmark decisions in the area of criminal rights.[47] The instant decision, however, adopts a significantly different approach. The majority opinion indicates a deference to reality and the practical exigencies of the criminal process and not to a theoretical ideal.[48] The reasoning of the majority presents a simple and traditional rationale for the preponderance standard—since the admissibility of confessions is purely an evidentiary matter, and since the jury is the ultimate finder of fact, a preponderance of the evidence should suffice to bring the confession before the jury. Yet this reasoning is of little significance compared to the values that are thereby implemented. In place of the ideals expressed by the dissent,

45. 404 U.S. at 489.

46. Justices Douglas and Mitchell joined in the dissent. *Id.* at 490.

47. *See, e.g.*, Miranda v. Arizona, 384 U.S. 436 (1966); Jackson v. Denno, 378 U.S. 368 (1964); Mapp v. Ohio, 367 U.S. 643 (1961); Ferguson v. Georgia, 365 U.S. 570 (1961). *See generally* F. GRAHAM, THE SELF-INFLICTED WOUND (1970).

48. For a discussion of the Warren Court's decisions that indicate an ideal of totally excluding confessions from criminal procedure see F. GRAHAM, *supra* note 47.

the Court recognized three practical considerations underlying its choice of reasoning. First, in noting that its "experience" had shown no derogation of constitutionally protected rights through application of the preponderance standard, the majority found no compelling need to implement a more stringent standard as a prophylactic measure to possible constitutional violations. The Court displayed a willingness to defer to the adequacy of present procedures through its rejection of a standard that, in the opinion of the dissent, would reduce the admission of involuntary confessions.[49] Secondly, the Court emphasized that adoption of the reasonable doubt standard would be counterproductive to the public interest satisfied by admitting probative evidence to the jury. This stance conflicts with the trend established by the Warren Court.[50] Whereas the Warren Court decisions stress compliance with due process requirements for the admission of a confession, regardless of its probative value, and emphasize protection of individual criminal rights,[51] the instant rationale indicates a slight, yet significant, regression by the Court towards a probative value standard.[52] This shift of emphasis suggests a greater concern on the part of the present Supreme Court for the interest of society in having probative matter before the jury vis-à-vis that of the individual defendant—in protection against involuntary confession. An extension of this approach would suggest a possible judicial dormancy in the area of criminal confessions. Thirdly, the Court stressed that the adoption of a more stringent standard would not appreciably deter lawless conduct by the police and prosecution. This conclusion is especially important, for it signifies an acknowledgement by the Court of a practical limit to its ability to affect day-to-day law enforcement procedures.[53] This decision suggests a possible trend on the part of the Court to avoid establishing procedural standards for use by enforcement agencies unless such standards can, and in practice will, move reality closer to an ideal. The present Court, therefore, may be expected to alter present criminal procedures only when a concommitant change will occur in the daily procedures of law enforcement agencies and in the protection of individual liberties.

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49. 404 U.S. at 494.

50. *See* materials cited note 47 *supra*. In *The Self-Inflicted Wound*, the author discusses the "due process revolution" wrought by the Warren Court. F. GRAHAM, *supra* note 47.

51. *See* F. GRAHAM, *supra* note 47.

52. *See* materials cited note 12 *supra*.

53. Implicit in the Court's decision is a recognition of the administrative pressure placed upon trial courts by the procedures mandated by the Warren Court. *See* note 28 *supra*.

Landlord and Tenant—Forcible Entry and Detainer Statute—Provisions for Immediate Trial and Limitation of Triable Issnes Not Violative of Due Process or Eqnal Protection Clauses

Plaintiffs, month-to-month tenants of defendant-landlord,[1] brought a class action to have the Oregon Forcible Entry and Wrongful Detainer Statute (FED)[2] declared unconstitutional and to have its continued enforcement enjoined. Because the Portland City Bureau of Dwellings had declared defendant's apartment building unfit for habitation and in violation of the Portland Housing Code,[3] plaintiffs had refused to pay their monthly rents, thus prompting defendant-landlord to institute the FED action to regain possession of the premises. Plaintiffs asserted that the inadequate time allowed to prepare for the FED trial and the statutory bar of any defense other than denial of the landlord's allegation that the tenant has remained in possession after stopping rental payments violated plaintiff's constitutional rights to due process and equal protection.[4] The federal district court granted defendant's petition to dismiss.[5] On appeal to the United States Supreme Court, *held*, affirmed.[6] The provisions in Oregon's Forcible Entry and Wrongful Detainer Statute for an immediate trial and for limiting the triable issues to the question of possession are not violative of the tenant's constitutional rights to due process and equal protection. *Lindsey v. Normet*, 405 U.S. 56 (1972).

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1. The original complaint was filed by Donald and Edna Lindsey and 7 other tenants. Although permission to maintain the suit as a class action was granted, the Lindseys were the only tenants to appeal. Lindsey v. Normet, 405 U.S. 56, 58 n.1 (1972).

2. ORE. REV. STAT. §§ 105.105-.160 (1971).

3. City inspectors found rusted gutters, broken windows, a delapidated stairway, and improper sanitation. Further, the inspector posted a notice that the apartment was unfit for habitation and that it must be vacated within 30 days unless the owner could show cause why the dwelling should not be declared unfit for occupancy.

4. ORE. REV. STAT. § 105.135 (1971) states: "[T]he service shall be not less than two or more than four days before the day of trial appointed by the court." ORE. REV. STAT. §§ 105.145-.150 (1971) provides, in effect, that the defendant-tenant can only answer with respect to whether the plaintiff-landlord's allegations are true. Sufficient complaints need only allege that the landlord is entitled to possession of the premises because the tenant has remained in possession after defaulting in rent payments.

5. Lindsey v. Normet, Civil No. 70-8 (D. Ore., Sept. 10, 1970) (unreported).

6. The Court did reverse the district court's decision upholding the validity of the Oregon FED provision requiring a tenant who appeals an adverse decision to post an appeal bond of twice the estimated rental payments due during the appellate litigation. ORE. REV. STAT. § 105.160 (1971). The Supreme Court held the double-bond requirement violative of plaintiff's right to equal protection of the laws.

Since a lease is essentially an interest in land,[7] the landlord and tenant relationship traditionally has been governed by the law of real property. At common law, the landlord was under no legal obligation to make repairs on the leased property[8] but promised only to leave the tenant in "quiet possession" when the tenant promised to pay the rent. The tenant's rental obligation terminated only if he vacated the premises due to the landlord's breach of his covenant to assure quiet enjoyment.[9] If the tenant defaulted in rental payments, the landlord's only remedy was the prolonged, expensive, common-law action of ejectment.[10] The frequent inability of landlords to afford this remedy necessitated resort to a method of "self-help" whereby a landlord was privileged to evict nonpaying tenants forcibly.[11] Because this judicially sanctioned self-help remedy engendered more violence and disruption than the courts had anticipated, and in order to give landlords a prompt, inexpensive method to remove nonpaying tenants without unduly crowding the general jurisdiction dockets of the courts, legislatures enacted forcible entry and detainer statutes.[12] Consistent with these objcctives, FED statutes now provide for a trial to determine, as the sole issue, the landlord's right to possession; the proceeding usually is heard within a few days after the tenant receives notice of the pending action.[13] The FED stat-

7. *E.g.*, Evans v. Faught, 231 Cal. App. 2d 698, 42 Cal. Rptr. 133 (1965); Michaels v. Brookchester, Inc., 26 N.J. 379, 140 A.2d 199 (1958). *See also* 1 H. TIFFANY, REAL PROPERTY § 74 (3d ed. 1939).

8. *See* Viterbo v. Friedlander, 120 U.S. 707 (1887) (landlord under no obligation to make repairs); Gaddis v. Consolidated Freightways, Inc., 239 Ore. 553, 398 P.2d 749 (1965) (in absence of agreement, lessee bears ohligation to repair). *See generally* Quinn & Phillips, *The Law of Landlord-Tenant: A Criticial Evaluation of the Past with Guidelines for the Future*, 38 FORDHAM L. REV. 225 (1970).

9. *See* Royce v. Guggenheim, 106 Mass. 201 (1870) (if landlord changes premises so as to interfere with tenant's quiet enjoyment, tenant may terminate lease). *See generally* 1 AMERICAN LAW OF PROPERTY § 3.45 (A.J. Casner ed. 1952).

10. 2 H. TIFFANY, *supra* note 7, §§ 215, 278-86 (1910). On the tenant's side, courts developed the doctrine of constructive eviction, which relieved the tenant of his obligation to pay rent if he showed that he had vacated the premises because of a complete lack of maintenance amounting to a breach of the landlord's duty to assure quiet possession. *See* 1 AMERICAN LAW OF PROPERTY § 3.51 (A.J. Casner ed. 1952); 1 H. TIFFANY, *supra* §§ 141-45 (3d ed. 1939). This doctrine has been extended to cases in which the tenant maintains possession. *E.g.*, Johnson v. Pemberton, 197 Misc. 739, 97 N.Y.S.2d 153 (N.Y.C. Mun. Ct. 1950); *see* Schoshinski, *Remedies of the Indigent Tenant: Proposal for Change*, 54 GEO. L.J. 519, 529-31 (1966).

11. *E.g.*, Smith v. Reeder, 21 Ore. 541, 28 P. 890 (1892) (court sanctioned self-help by landlord in bodily removing tenant).

12. All states have unlawful detainer statutes of some kind. *See, e.g.*, CAL. CIV. PRO. CODE §§ 1161-79a (West 1955), *as amended*, (Supp. 1971); N.Y. REAL PROP. ACTIONS LAW §§ 701-67 (McKinney 1968), *as amended*, (Supp. 1970). *See generally* 52A C.J.S. *Landlord and Tenant* § 752 (1968).

13. *See generally* Note, *Unlawful Detainer: Synopsis of California Law and Constitutional Considerations*, 44 S. CAL. L. REV. 768, 770-71 (1971).

utes thus reinforce the feudal property concept that the landlord's duty to maintain service and the tenant's obligation to pay rent are independent covenants, and, therefore, the landlord can bring an FED action for possession regardless of his own possible breaches of duty.[14] Although criticism of landlord-tenant law has been mounting in response to the critical housing situation in metropolitan centers,[15] there has been little court action directed toward modification of FED statutes. For example, in *Javins v. First National Realty Corp.*,[16] the first case to discard the antiquated rules of property law when dealing with urban apartment leases,[17] the court looked beyond the issue of possession but did not focus on the wrongful detainer statute there involved. In that case, in an opinion written by Judge J. Skelly Wright, the court held that a warranty of habitability is implied by operation of law in all leases of urban dwelling units covered by housing codes, and that the tenant may raise the landlord's breach of that warranty as an affirmative defense in the landlord's action to regain possession.[18] Although there is reason to anticipate that *Javins* will stimulate further judicial examination of landlord-tenant law, only one case has considered constitutonal objections to FED statutes.[19] In *Hutcherson v. Lehtin*,[20] a California federal district court held that tenant's rights to equal protection and due process of the law were not violated by the California unlawful detainer statute. In refusing to allow tenants to plead affirmative defenses of housing code violations and breach of their landlord's covenant to repair, the court held that it was necessary to narrow the issues to the question of possession in order to accomplish the legislative purpose of speedy adjudication.[21] The court invoked the historical property law

14. *See generally* Gibbons, *Residential Landlord-Tenant Law: A Survey of Modern Problems with Reference to the Proposed Model Code*, 21 HASTINGS L.J. 369, 371-80 (1970).

15. *See, e.g.*, Quinn & Phillips, *supra* note 8; Note, *Judicial Expansion of Tenant's Private Law Rights: Implied Warranties of Habitability and Safety in Residential Urban Leases*, 56 CORNELL L. REV. 489 (1971).

16. 428 F.2d 1071 (D.C. Cir.), *cert. denied*, 400 U.S. 925 (1970).

17. 428 F.2d at 1077-80.

18. Commentators without exception have praised Judge Wright for his decision. *See, e.g.*, 39 GEO. WASH. L. REV. 152 (1970); 24 VAND. L. REV. 425 (1971).

19. One recent case deals with the New York detainer statute, but the court limited itself to the adequacy of notice and did not reach the underlying constitutionality of the statute. Valazquez v. Thompson, 451 F.2d 202 (2d Cir. 1971).

20. 313 F. Supp. 1324 (N.D. Cal.), *appeal dismissed for lack of jurisdiction*, 399 U.S. 522, *modified*, 400 U.S. 923 (1970) (new judgment entered vacating district court decision and remanding for order dismissing complaint).

21. 313 F. Supp. at 1328. The court did indicate, however, that retaliatory eviction, in which the landlord evicts the tenant for having reported the former to the authorities for housing code violations, does violate tenants' fourteenth amendment rights. *See, e.g.*, Edwards v. Habib, 366 F.2d 628 (D.C. Cir. 1965); Hosey v. Club Van Cortland, 299 F. Supp. 501 (S.D.N.Y. 1969).

concept that the landlord's covenant to repair was independent of the tenant's obligation to pay rent.[22] Finally, the court in *Hutcherson* justified its conclusion by declaring that any due process argument propounded by the tenant was untenable because the tenant, after relinquishing possession, could initiate his own action at law against the landlord for breach of the covenant to repair and for violations of the housing code.[23]

Noting first that four days was sufficient time to prepare for the single issue of the landlord's right to regain possession,[24] the Court concluded that the short notice-to-trial rule was necessary in order to prevent subjecting the landlord to undeserved economic loss and to protect the tenant from incessant and perhaps violent harassment.[25] As to the limitation on litigable issues, the Court dispensed with plaintiffs' argument that such a restriction deprived them of due process, by suggesting that tenants could vindicate their claims against landlords by initiating their own legal actions.[26] Finally, the Court recognized that the Oregon statute was supported by the legitimate purpose of facilitating the settlement of landlord-tenant disputes promptly and peacefully, and that this permissible state objective could be achieved by the FED statute's strict limitation of triable issues.[27] The instant Court found, therefore, that the Oregon FED statute's provisions for a speedy trial and limited triable issues did not violate plaintiffs' rights to due process and equal protection of the law. In a vigorous dissent, Justice Douglas attacked the majority's holding that the speedy trial provision afforded plaintiffs due process of law. Douglas reasoned that it was unrealistic to believe that a slum tenant could obtain a lawyer or that, if retained,

22. 313 F. Supp. at 1328. The court declared that the landlord's refusal to repair did not grant the tenant any right to withhold rent.

23. *Id.* at 1329. The court stated, however, that the tenant could have made the repairs himself and deducted the cost from the rent, or he could have abandoned the premises and been relieved of his obligation to pay rent. *Id.* at 1328.

24. The Court stated that the tenants had as much access to the relevant facts as did the landlord and should have known the terms of their leases. The Court also believed that making rental payments a condition precedent to a continuance was reasonable.

25. The Court adopted the rationale of McGowan v. Maryland, 366 U.S. 420 (1961). The *McGowan* Court held that state action that affects some groups of citizens differently than others violates equal protection "only if the classification rests on grounds wholly irrelevant to the achievement of the state's objective." 366 U.S. at 425. The instant Court reasoned that the objective of Oregon was to achieve prompt and peaceful solutions to disputes over possession of real property.

26. The Court based this conclusion on Bianchi v. Morales, 262 U.S. 170 (1923), and Grant ɔer & Mfg. Co. v. Gray, 236 U.S. 133 (1915). Those cases held that it did not violate the due ɔss clause to segregate an action for possession of real property from a separate action that :d allow the assertion of equitable defenses.

27. The Court, however, did hold the double bond requirement unconstitutional.

the lawyer could prepare a competent defense in four days.[28] As to the statutory restriction on triable issues, Justice Douglas insisted that the limitation precluding the assertion of affirmative defenses was reminiscent of feudal property principles under which the tenant alone was expected to maintain the rented dwelling.[29] Justice Douglas finally observed that since Oregon law regards a lease as an ordinary contract, all defenses relevant to the legality and operation of the lease should be included within the ambit of the opportunity to be heard guaranteed by the due process clause of the fourteenth amendment.[30]

The instant decision, which constitutionally buttresses the Oregon wrongful detainer statute, affirms an outmoded and singularly inappropriate attitude toward landlord-tenant relations that reason and contemporary social values cannot sustain. Not only does the decision deliver a severe blow to those tenants' rights advocates who support complete abolition of FED statutes,[31] but the urban landlord is further strengthened in his already advantageous relationship with his tenant.[32] By upholding the four-day notice-to-trial provision, the Court disregarded the difficult problems of the about-to-be-ousted tenant. Although the majority carefully weighed the landlord's potential economic loss from lengthy adjudication, the injustice to the slum tenant who cannot find or afford a lawyer[33] was glossed over summarily. Even if legal counsel were obtained, four days would seem an inadequate time to prepare for even a limited trial.[34] Indeed, in most FED cases, the only parties

28. Adopting a pragmatic approach, Justice Douglas attacked the 4-day notice requirement as violative of plaintiff's right to sue and defend in the courts. *See* Chambers v. Baltimore & O.R.R., 207 U.S. 142 (1907). *See also* Javins v. First Nat'l Realty Corp., 428 F.2d 1071 (D.C. Cir. 1970). Justice Douglas also argued that the section of the FED statute providing for the short time between notice and trial violated the notice rule as laid down in Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1950).

29. *See, e.g.*, NATIONAL COMM'N ON URBAN PROBLEMS, RESEARCH REPORT NO. 14, at 110-11 (1968).

30. The dissent further argued that a defendant in an FED action should not be precluded from raising the affirmative defense that he was evicted for turning his landlord in to the housing authorities for housing code violations. *See* Edwards v. Habib, 397 F.2d 687 (D.C. Cir. 1968). According to Justice Douglas' analysis, this transgression occurred in the instant case, and the tenant should not have been deprived of his right to complain.

31. *See generally* Daniels, *Judicial and Legislative Remedies for Substandard Housing: Landlord-Tenant Law Reform in the District of Columbia*, 59 GEO. L.J. 909 (1971); Note, *California Unlawful Detainer Procedure—A Proposed Legislative Change*, 21 HASTINGS L. J. 49 (1970).

32. *See* Slawson, *Standard Form Contracts and Democratic Control of Law Making Power*, 84 HARV. L. REV. 529 (1971); Javins v. First Nat'l Realty Corp., 428 F.2d 1071 (D.C. Cir. 1970).

33. Note, *supra* note 31, at 492.

34. There seems to be patent inequity in granting the landlord's FED action preference on court calendars when the tenant may be homeless as he awaits his own action to be called from the crowded docket. *See, e.g.*, Boddie v. Connecticut, 401 U.S. 371, 389 (1971) (Brennan, J.,

present at trial are the judge, the landlord, and the landlord's counsel.[35] There is even less justification for upholding the limitation of triable issues. Although the majority found that the Oregon statute was justified by legitimate state interest in providing for "prompt and peaceful settlement," the instant means for effecting the result operates with undue harshness upon tenants. By the limitation of triable issues to the single issue of possession, the landlord, in effect, gains a twofold strategic advantage over his tenants. First, the shrewd landlord may bring his limited action quickly, before the tenant has time to initiate an action in which all issues would be litigable. By this course of action, the landlord often can force the indigent tenant into expending all his resources in an action he cannot hope to win. Funds depleted, the tenant is no longer able to prosecute or sustain a lengthy, expensive action at law and, thus, has lost any realistic opportunity to put his grievances before a court. Secondly, the threat of FED action may prove an important negotiating tool for the lawyerish landlord. Although the instant Court accorded little weight to the slum tenant's bargaining disadvantage, threatened FED action could enable a landlord not only to shirk repair and other duties but also to intimidate a tenant and thereby prevent him from reporting housing code violations. Furthermore, the Court failed to examine closely the landlord-tenant contractual relationship itself. Since Oregon law regards a lease as a contract, there is no reason to eliminate contract defenses in actions on the lease. Reason does not support retention of the antiquated agrarian rule that the landlord's duty to repair and the tenant's duty to pay are independent covenants when that rule affords a landlord the right to recover in full for rent regardless of whether he has violated his duty to maintain the premises. The Court in the instant case might well have held the Oregon FED statute unconstitutional had it adopted a more realistic view of current landlord-tenant conditions. Because the states and landlords have other remedies available that produce less drastic consequences to the tenant than the summary eviction statutes, and because the legal community is becoming more aware of the critical problems of urban housing, there is every possibility that the constitutional validity of forcible entry and detainer statutes will again receive the Court's review.[36]

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concurring); Griffin v. Illinois, 351 U.S. 12 (1956) (petitioner constitutionally guaranteed adequate and effective review).

35. Note, *supra* note 13.

36. Even the instant Court noted the possibility that the Oregon FED statute could deprive a tenant of his constitutional rights in a specific factual situation, thus implying the possibility of further review if such a factual situation were to arise.

Securities Regnlatiou—Section 16(b) of Securities Exchange Act of 1934—Insider May Sell Enough Stock To Bring His Holdings Below Ten Percent and Witbin Six Montbs of the Original Purchase Sell tbe Remainder Without Liability for Short-Swing Profits

Respondent[1] acquired the status of a statutory insider[2] by purchasing 13.2 percent of the outstanding stock of Dodge Manufacturing Company in an unsuccessful takeover attempt.[3] Respondent then sold the entire amount within six months in two separate transactions, the first of which brought its holdings to just under ten percent.[4] Petitioner, a shareholder in Dodge, made a demand upon respondent for the profits realized in both sales,[5] and respondent sought a declaratory judgment in federal district court to determine the extent of its liability under section 16(b) of the Securities Exchange Act of 1934.[6] Respondent con-

1. Emerson Electric Company.

2. "Statutory insider" refers to one who comes within the provisions of § 16(b) and who is considered, by reason of meeting the criteria established therein, to have access to inside information regarding a corporation. *See* notes 7 & 8 *infra*.

3. Emerson had attempted a merger with Dodge, which was rejected by Dodge's board on March 12, 1967. Emerson, in an attempt to acquire a majority of Dodge voting stock, and then vote a merger, invited tenders of up to 550,000 shares of Dodge common stock at $63 per share. When the tender offer expired June 16, 1967, Emerson purchased 152,282 shares, which constituted 13.2% of the outstanding Dodge stock. Prior to that date Emerson owned no shares of Dodge stock. Shortly before Emerson's purchase of the Dodge stock, Dodge and petitioner, Reliance Electric Company, had entered into a merger agreement whereby Dodge was to be merged into Reliance. Emerson attempted to prevent the merger and a proxy fight ensued, with a resulting victory for Reliance.

4. After the Dodge shareholders endorsed the merger with Reliance, Emerson sold all of its Dodge holdings. On August 28, 1967, Emerson sold 37,000 shares at $68 per share to an investment broker, thus reducing its holdings to 9.96% of the outstanding shares of Dodge. On September 11, 1967, Emerson sold the remaining 115,282 shares to Dodge at $69 per share. These transactions followed a plan outlined by Emerson's general counsel advising that it dispose of enough shares to bring its holdings below 10%, in order to immunize the disposal of the remaining shares from liability under § 16(b).

5. Petitioner's demand was based upon the § 16(b) provision that profits made on transactions covered by the statute shall be recoverable by the issuer of the securities. *See* note 6 *infra*. Emerson's profit on the first sale amounted to $185,000; its profit on the second sale amounted to $691,692; total profit from the transactions amounted to $876,692.

6. Section 16(b) provides: "For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer, (other than an exempted security) within any period of less than six months . . . shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months . . . . This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase of the security

tended[7] that it was liable only for the profits realized on the first sale, because after that transaction it was no longer a ten percent owner within the meaning of section 16(b).[8] The district court held respondent liable for the entire amount of its profits, finding that the two sales were effected pursuant to a single, predetermined plan of disposition with the intent of avoiding section 16(b) liability.[9] On an interlocutory appeal, the Court of Appeals for the Eighth Circuit reversed.[10] Finding that respondent had "split" its sale to avoid section 16(b) liability, the court nevertheless held that if after the initial sale, the arbitrary standards enacted by Congress in 16(b) concerning a more-than-ten percent security holder are no longer met, the subsequent sales are free of section 16(b) regulation.[11] On appeal to the United States Supreme Court, *held*, affirmed. Section 16(b), in limiting the coverage of its liability provisions to those persons who are ten percent owners at the time of both the purchase and sale, clearly contemplates that a statutory insider may sell enough shares to bring his holdings below ten percent, and, within six months of the original purchase, effect another sale free from liability under the statute. *Reliance Electric Co. v. Emerson Electric Co.*, 404 U.S. 418.

Section 16(b) of the Securities Exchange Act was enacted to prevent corporate insiders[12] from abusing their positions by taking advantage of information unavailable to the public in order to aid themselves

involved, or any transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection." 15 U.S.C. § 78p(b) (1970).

7. Respondent initially contended that it was not liable at all because it was not a "beneficial owner" at the time of the *purchase* of the shares. This contention was rejected by the district court on the ground that it was contrary to the legislative purpose manifested in the statute. Emerson Elec. Co. v. Reliance Elec. Co., 306 F. Supp. 588, 589-90 (E.D. Mo. 1969). The Court of Appeals for the Eighth Circuit upheld this finding. Emerson Elec. Co. v. Reliance Elec. Co., 434 F.2d 918, 922-24 (8th Cir. 1970), and Emerson did not pursue this argument before the Supreme Court. Reliance Elec. Co. v. Emerson Elec. Co., 404 U.S. 418 (1972).

8. The term "such beneficial owner" refers to one who owns "more than 10 percentum of any class of any equity security (other than an exempted security) which is registered pursuant to section 78*l* of this title . . . ." Securities Exchange Act of 1934, § 16(a), 15 U.S.C. § 78p(a) (1970).

9. *See* notes 4 & 6 *supra*.

10. The court construed the term "time of sale" to include "the entire period during which a series of related transactions takes place pursuant to a plan by which a ten percent beneficial owner disposes of his stockholdings." 434 F.2d at 923.

11. The Court of Appeals reversed the district court's judgment on respondent's liability for the profits from the second sale, and remanded for a determination of liability from the first sale. 434 F.2d at 918.

12. The term "insiders" refers to those directors, officers, and 10% beneficial owners who, by profiting from the transactions occurring within 6 months of each other, come within the provisions of § 16(b). *See* notes 2 & 6 *supra*.

in market activities.[13] Widespread and pervasive disregard by corporate insiders of their fiduciary positions[14] led to the adoption of strict and arbitrary[15] criteria for defining those transactions governed by the statute's provisions.[16] Section 16(b) was deliberately designed to discourage short-term speculation by insiders through the imposition of liability without any requirement of proof that an insider *intended* to profit from unfair use of information,[17] or even that the insider was privy to such confidential information.[18] The purpose was to stop the *possible*,[19] not the actual use of inside information;[20] section 16(b) liability therefore becomes automatic[21] and attaches "to any profit by an insider on any short-swing transaction embraced within the arbitrarily fixed time limits

13. *See* Moore & Wiseman, *Market Manipulation and the Exchange Act*, 2 U. CHI. L. REV. 46 (1934); Rubin & Feldman, *Statutory Inhibitions Upon Unfair Use of Corporate Information by Insiders*, 95 U. PA. L. REV. 468 (1947). For a survey of the history of stock market regulation in this country and of the Act itself see Tracy & MacChesney, *The Securities Exchange Act of 1934*, 32 MICH. L. REV. 1025 (1934).

14. One famous example concerned 2 brothers whose ownership of a little over 10% of a company's stock gave them a controlling interest. Just before the company voted to omit a dividend, they sold their stock for $16,000,000. After the news became public, they repurchased an equivalent amount of stock for $7,000,000 showing a $9,000,000 profit on the short-swing deal. S. REP. NO. 792, 73d Cong., 2d Sess. 9 (1934).

15. *See* Munter, *Section 16(b) of the Securities Exchange Act of 1934: An Alternative to "Burning Down the Barn in Order to Kill the Rats,"* 52 CORNELL L.Q. 69 (1966); *Hearings Before the House Comm. on Interstate and Foreign Commerce*, 77th Cong., 1st Sess. 1248 (1941) (testimony of George P. Rea).

16. S. REP. NO. 1455, 73d Cong., 2d Sess. 55 (1934). Section 16(b) was designed "to protect the interests of the public against the predatory operations of directors, officers, and principal stockholders of corporations by preventing them from speculating in the stock of the corporations to which they owed a fiduciary duty." *Id.* at 68; *see* Shaw v. Dreyfus, 172 F.2d 140, 142 (2d Cir. 1949); *Hearings on H.R. 7862 and H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 85 (1934) (testimony of Thomas Corcoran).

17. *See, e.g.*, Blau v. Lamb, 363 F.2d 507, 515 (2d Cir. 1966), *cert. denied*, 385 U.S. 1002 (1967). *See also* Truncale v. Blumberg, 80 F. Supp. 387 (S.D.N.Y. 1948).

18. *See, e.g.*, Ferraiolo v. Newman, 259 F.2d 342, 344 (6th Cir. 1958), *cert. dcnied*, 359 U.S. 927 (1959).

19. Gold v. Scurlock, 324 F. Supp. 1211, 1214 (E.D. Va. 1971).

20. "The section does indeed cover trading by those who in fact have no such information . . . . If only those persons were liable, who could be proved to have a bargaining advantage, the execution of the statute would be so encumbered as to defeat its whole purpose." Gratz v. Claughton, 187 F.2d 46, 49-50 (2d Cir.), *cert. denied*, 341 U.S. 920 (1951).

21. "That is to prevent directors receiving the benefits of short-term speculative swings on the securities of their own companies, because of inside information. The profit on such transactions under the bill would go to the corporation. You hold the director, irrespective of any intention or expectation to sell the security within six months after, because it will be absolutely impossible to prove the existence of such intention or expectation, and you have to have this crude rule of thumb, because you cannot undertake the burden of having to prove that the director intended, at the time he bought, to get out on a short swing." *Hearings on S. Res. 84, 56 & 97 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st & 2d Sess. 6557 (1934) (testimony of Thomas Corcoran).

of the statute."[22] In order to maintain the remedial nature[23] of section 16(b), illustrated by the provision that the profits from such transactions inure to the benefit of the corporation,[24] the courts, until recently, have interpreted the statute in the broadest possible terms,[25] resolving all doubts and ambiguities against insiders.[26] For example, in following this basic principle of broad statutory construction, the courts have gone so far as to require that a director not only must account for purchases and sales during the tenure of his office, but also for purchases made shortly before his appointment,[27] and for sales made shortly after his resignation.[28] When ambiguities in section 16(b) have caused difficulties of construction, the courts have looked to the legislative intent of the section as a whole,[29] taking the position "that the statute was intended to be thoroughgoing, to squeeze all possible profits out of stock transactions, and thus to establish a standard so high as to prevent any conflict between the selfish interest of a fiduciary officer, director, or stockholder and the faithful performance of his duty."[30] One area that has presented problems in the application of section 16(b) involves tender offers, mergers, and acquisitions. Questions have arisen regarding

22. Feder v. Martin Marietta Corp., 406 F.2d 260, 262 (2d Cir. 1969), *cert. denied*, 396 U.S. 1036 (1970).

23. Volk v. Zlotoff, 285 F. Supp. 650, 655 (S.D.N.Y. 1968); *see* Smolowe v. Delendo Corp., 136 F.2d 231, 239 (2d Cir.), *cert. denied*, 320 U.S. 751 (1943).

24. 15 U.S.C. § 78p(b) (1970).

25. *See* Volk v. Zlotoff, 285 F. Supp. 650, 655 (S.D.N.Y. 1968).

26. Truncale v. Blumberg, 80 F. Supp. 387, 390 (S.D.N.Y. 1948).

27. Adler v. Klawans, 267 F.2d 840 (2d Cir. 1959).

28. Feder v. Martin Marietta Corp., 406 F.2d 260 (2d Cir. 1964). In other instances of broad statutory construction under § 16(b), an exercise of an option to convert preferred into common stock has been held to be a "purchase" within the 6-month provision. Park & Tilford, Inc. v. Schulte, 160 F.2d 984 (2d Cir. 1947). An option has also been held to be a "sale" when granted, Bershad v. McDonough, 428 F.2d 693 (7th Cir. 1970), *cert. denied*, 400 U.S. 991 (1971), and a mutual rescission of the exercise of a stock purchase option has been found insufficient to immunize a transaction from § 16(b) liability. Volk v. Zlotoff, 285 F. Supp. 650 (S.D.N.Y. 1968). *But see* Silverman v. Landa, 306 F.2d 422 (2d Cir. 1962) (a sale occurs when the optionee exercises the option). In construing the term "purchase," the District Court for the Southern District of New York said that a purchase was effected when an insider received stock of a parent corporation in exchange for his stock in a subsidiary. Blau v. Hodgkinson, 100 F. Supp. 361, 373 (S.D.N.Y. 1951). Other courts have held that a transfer of shares from one corporate officer to another in payment of a pre-existing debt is a "sale." Smolowe v. Delendo Corp., 136 F.2d 231, 239 (2d Cir. 1943). A person performing the functions of a corporate officer, although not officially one, has been held an "officer," Colby v. Klune, 178 F.2d 872, 873 (2d Cir. 1949), and a purchaser of corporate stock who was not a director of the corporation at the time of his purchase, but became one prior to reselling the stock, has been held to the same liability as one who had, at all times, been a direetor. Blau v. Allen, 163 F. Supp. 702, 704 (S.D.N.Y. 1958).

29. *See, e.g.*, Adler v. Klawans, 267 F.2d 840, 844 (2d Cir. 1959); Blau v. Oppenheim, 250 F. Supp. 881, 884, 885 (S.D.N.Y. 1966).

30. Smolowe v. Delendo Corp., 136 F.2d 231, 239 (2d Cir. 1943).

whether stock that is acquired or disposed of in merger-type transactions should be considered "purchased" or "sold" within the meaning of the statute,[31] and the courts have followed two basic approaches in applying the statute in such cases.[32] These have been referred to as the "subjective" or "pragmatic" approach, in which the court examines the transaction to determine whether or not it lends itself to the type of speculative abuse that section 16(b) was designed to prevent,[33] and the "objective" or "per se" test, in which the statute is applied to all transactions that fall within the literal import of its terms.[34] In *Abrams v. Occidental Petroleum Corp.*,[35] the Second Circuit followed the pragmatic approach, and apparently refused to find liability when the insider had no opportunity for speculative abuse, although the transaction complained of fell within the express language of the statute.[36] Most courts today take a similar approach, inquiring into the nature of each transaction in order to see if application of the statute will serve its purposes[37] when dealing with section 16(b) cases involving the exemption provision of the statute. This provision states that section 16(b) shall not be construed to cover any transaction in which a beneficial owner was not such both at the time of purchase and sale.[38] In *Stella v. Graham-Paige Motors Corp.*,[39] the Second Circuit, in determining that defendant, who did not own ten percent immediately prior to the purchase in question, was indeed a beneficial owner at the time the purchase was made, construed the term "at the time of" to mean simultaneously with the purchase of stock.[40] The majority opinion agreed with the lower

31. Note, *Stock Exchanges Pursuant to Corporate Consolidation: A Section 16(b) "Purchase or Sale"?*, 117 U. PA. L. REV. 1034 (1969).

32. *Id.*

33. *See, e.g.*, Petteys v. Butler, 367 F.2d 528 (8th Cir. 1966), *cert. denied*, 385 U.S. 1006 (1969); Blau v. Lamb, 363 F.2d 507 (2d Cir. 1966); Blau v. Max Factor & Co., 342 F.2d 304 (9th Cir.), *cert. denied*, 382 U.S. 892 (1965); Ferraiolo v. Newman, 259 F.2d 342 (6th Cir. 1958).

34. *See, e.g.*, Heli-Coil Corp. v. Webster, 352 F.2d 156 (3d Cir. 1965); Park & Tilford, Inc. v. Schulte, 160 F.2d 984 (2d Cir. 1947). For a discussion of these approaches see Lowenfels, *Section 16(b): A New Trend in Regulating Insider Trading*, 54 CORNELL L. REV. 45 (1968).

35. 450 F.2d 157 (2d Cir. 1971).

36. The court relied upon its approach taken earlier in Blau v. Lamb, 363 F.2d 507 (2d Cir. 1966). In that case, the court stated: "[I]n deciding whether a certain transaction is a Section 16(b) 'purchase' or 'sale' it is relevant to first consider whether the transaction in any way makes possible the unfair insider trading that Section 16(b) was designed to prevent." 363 F.2d at 518.

37. *See, e.g.*, Bershad v. McDonough, 428 F.2d 693 (7th Cir. 1970).

38. 15 U.S.C. § 78p(b) (1970).

39. 232 F.2d 299 (2d Cir.), *cert. denied*, 352 U.S. 831 (1956). Defendant corporation, owning less than 10% of the outstanding stock of another corporation, purchased additional shares to raise its total holdings to 21% and then, within 6 months, sold a portion of these holdings for a profit. This case is noted in 57 COLUM. L. REV. 287 (1957); 9 STAN. L. REV. 582 (1957).

40. This position was urged not only by plaintiff, but also by the SEC, which filed an amicus

court which had pointed out that if the exemption provision were applied, "it would be possible for a person to purchase a large block of stock, sell it out until his ownership was reduced to less than 10%, and then repeat the process, ad infinitum."[41] The Second Circuit took this pragmatic approach in spite of its awareness that several commentators had noted the ambiguity of the act and had recommended that in order to escape section 16(b) liability in a sale, a more-than-ten percent owner could sell enough stock to reduce his holdings to slightly under ten percent, and then sell out the remainder.[42] The dissent in *Stella* took a more objective approach, concluding that the statute clearly exempted one who was not a ten percent owner *prior* to both the purchase and sale.[43] The dissent reasoned that since Congress had deemed ten percent ownership to be the minimum amount sufficient to provide an owner with enough control of a corporation to have access to inside information, the statute could not by its terms reach purchases made by one who was not currently in that position.[44]

After reviewing the history and purpose of section 16(b), the Supreme Court reasoned that since the arbitrary provisions of the statute apparently enable an insider to avoid liability merely by structuring his transactions to fall outside these provisions, the relevant question must be whether the *method* used to avoid liability is permitted by the statute. The Court determined that a *literal* reading of the "objective standards" of section 16(b) requires that a ten percent owner be such both at the time of the purchase and sale, and that the statute clearly contemplates that a statutory insider might sell enough shares to bring his holdings below ten percent and then—still within six months—sell additional shares free from liability.[45] Since a plan to sell which is conceived within six months of purchase would not fall within the statute if the sale were made after six months had elapsed, the Court reasoned that there is no statutory basis for arriving at a different result when the ten percent, rather than the six-month requirement is involved. The Court felt that

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curiae brief suggesting the same construction of the Act. Stella v. Graham-Paige Motors Corp., 104 F. Supp. 957 (S.D.N.Y. 1952).

41. 104 F. Supp. at 959.

42. 2 L. LOSS, SECURITIES REGULATION 1060 (2d ed. 1961); *see* Seligman, *Problems Under the Securities Exchange Act*, 21 VA. L. REV. 1, 20 (1934).

43. 232 F.2d at 303-05. The rationale of the dissent was followed in Arkansas La. Gas Co. v. W.R. Stephens Inv. Co., 141 F. Supp. 841 (W.D. Ark. 1956). For discussion of the 10% rule see Newmark v. RKO Gen., Inc., 425 F.2d 348 (2d Cir. 1970), *noted in* 84 HARV. L. REV. 1012 (1971).

44. 232 F.2d at 305.

45. The Court referred to the recommendations of securities writers who have advocated such a plan for avoiding liability. 404 U.S. 418, 423 (1972); *see* note 42 *supra*.

it would have been inconsistent with the congressional purpose of imposing liability upon an objective measure of proof to have construed the term "at the time of . . . sale" so that two sales would be treated as one upon a showing of a pre-existing intent by the seller.[46] The Court stated that if these two-step sales give rise to the evil which Congress sought to correct, then an amendment to the statute would be far more effective than a judicial inquiry into intent of the insider in each case.[47] The Court concluded that a ten percent owner who reduces his holdings to less than ten percent and then sells the remainder within six months of the purchase is not a statutory insider at the time of the second sale, and thus is not required under section 16(b) to turn over the profits from that sale to the corporation.

In a dissenting opinion, Mr. Justice Douglas pointed out that in cases resolving statutory ambiguities in section 16(b), the judiciary's approach had always been to apply the section consistently with the legislative purpose of curbing short-swing speculation by insiders.[48] Reasoning that by the division of what would ordinarily be a single transaction into two parts, a more-than-ten percent owner would be able to reap windfall profits on ten percent of his corporation's stock, he went on to suggest that the statute should be construed to allow a rebuttable presumption that a series of dispositive transactions by a beneficial owner within six months be treated as a single sale for section 16(b) purposes.[49]

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46. *See* Smolowe v. Delendo Corp., 136 F.2d 231 (2d Cir. 1943).

47. The Court also reasoned that since a less-than-10% owner would be exempt from the reporting requirements of § 16(a), under the SEC's own rules, such an owner would also be exempt from § 16(b). The SEC has used its power to grant exemptions under § 16(b) to exclude from liability any transaction that does not fall within the reporting requirements of § 16(a). SEC Rule 16(a)-10, 17 C.F.R. § 240.16a-10 (1964). A 10% owner is required by § 16(a) to report at the end of each month any changes in his holdings in the corporation during that month. The Commission interpreted this provision to require a report only if the stockholder had more than 10% of the corporation's shares at some time during the month. Form 4, SEC Securities Act Release No. 6487 (Mar. 9, 1961). The Court disposed of the SEC's argument that persons who become 10% owners "involuntarily"—by legal succession or by a reduction in the total number of outstanding shares of the corporation—should be excluded from the statute's coverage. The result of such an interpretation would be to bring within the statute's coverage all sales within 6 months by one who has gained the status of a 10% owner through voluntary purchase, regardless of the amount of his holdings at the time of the sale. The Court determined that such an interpretation was in contradiction of Form 4's requirements and that it clearly contradicts the words of the statute.

48. Mr. Justice Douglas emphasized the potential for abuse of inside information in the present case, relying on a survey taken in the *Harvard Business Review* of "reputable" businessmen. The results of that survey indicated that 42% of such businessmen stated that they would trade on inside information, and 61% believed that the "average" executive would do likewise. Baumhart, *How Ethical Are Businessmen*, 39 HARV. BUS. REV. 6, 16 (July-Aug. 1961).

49. The dissent relies upon suggestions by securities commentators to support this view. 404 U.S. at 430 (Douglas, J., dissenting).

The dissent found that the ten percent rule is prophylactic in nature and its deterrent value depends not so much on its "objectivity" as on its "thoroughgoing qualities." Douglas concluded that the six-month rule implies that inside information will be presumed useful during that time, so that all sales by a more-than-ten percent owner within the six-month period carry the "presumption of a taint," and should be held violative of section 16(b).

The decision in the instant case appears to open a loophole in section 16(b) liability by permitting insider trading when effected in a series of transactions designed to avoid the arbitrary provisions of the statute. Apparently, liability can be avoided easily by acting just outside the criteria established—selling one day after six months, or purchasing and selling 9.9 percent of the outstanding stock. In view of the intent and purpose of the statute, it is naive to anticipate that since the ten percent standard was thought to embrace those insiders who would have access to confidential information,[50] a "sell-down"[51] by such an owner within a period as short as six months prior to a second sale would remove him from the class of persons having access to inside information.[52] There is little doubt that inside information acquired after a purchase but prior to loss of insider status may still be valuable after a sell-down and might be used unfairly within the six-month period, particularly when the later sale consumates a prearranged *plan* for disposing of a shareholder's stock. In such situations the evil sought to be remedied will go unabated, since the majority opinion's literal reading of 16(b) clearly indicates that a sale by one who is not then a ten percent owner is outside the section's provisions. Whether room exists for the courts to construe the statute to prevent such transactions is debatable in light of the exemption clause of section 16(b). Such a liberal construction was urged by the dissent, which would characterize "split" sales or a "series" of related sales as one transaction, within the scope of section 16(b). Under this construction, additional ambiguity would be added to the statute by requiring a determination of when sales in fact are split, in a series, or are related. Indeed, when the dissent,[53] in characterizing the sales as a single transaction, looked to the preconceived plan that respondent followed, it overlooked the "objective" nature of section

50. *See* note 43 *supra.*

51. The term "sell-down" refers to a sale by a 10% owner in which he reduces his holdings to less than 10%.

52. This view was presented by the SEC in its amicus brief. Brief for SEC as Amicus Curiae at 26, Reliance Elec. Co. v. Emerson Elec. Co., 404 U.S. 418 (1972). It was alluded to by the dissent in the instant case. *See id.* at 609.

53. The district court used this approach also. *See* note 7 *supra.*

16(b), which enforces liability without any showing of intent.[54]

The majority, relying on the apparent legislative intent to incorporate an objective standard in the arbitrary provisions of the exemption clause, appears to be acting in contradiction of the legislative purpose of the act as a whole. The dissent, on the other hand, has disregarded the "objective proof" mandate of 16(b) to further the broader spirit of the act. Since Congress sought to give effect to "the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner,"[55] it is fair to contemplate that Congress intended to exempt those transactions in which little or no opportunity for use of inside information is available. Since the instant decision involved a transaction that occurred pursuant to respondent's negotiations for a merger, a situation not unusual in 16(b) cases, the majority's ultimate decision may have been influenced by this factual situation. Because respondent's attempt to effect the merger was rejected, it is doubtful that respondent did, in fact, have access to inside information. The reported facts indicate that respondent attempted to sell its holdings in order to disassociate itself completely from its relationship with petitioner. In such situations, when a merger is rejected by a corporation, it is very doubtful whether any inside information would be accessible to the beneficial owner who was seeking control. Since the purpose of the statute is to prevent potential profits through use of inside information, it seems that applying the statute to transactions which do not involve substantial danger of possible abuses is straining the purpose of the Act. Therefore, additional guidelines need to be set forth for applying section 16(b) in corporate acquisition transactions. It has been suggested that the SEC adopt a rule exempting certain of these transactions from the coverage of the statute.[56] Much confusion in the courts would be eliminated if such a ruling were made that would exclude from the statute transactions that involve takeovers by outsiders, proxy fights, and other situations in which the facts involved are readily available to all shareholders, and stand outside the area of insider trading. The instant decision raises the question whether the result would have been

54. *See* notes 17 & 18 *supra*. *See also* notes 33 & 34 *supra*.

55. 15 U.S.C. § 78p(b) (1970).

56. Such a rule would provide "that no purchase or sale occurs for the purposes of section 16(b) when shares are exchanged pursuant to a plan or agreement for merger, where the terms of the plan or agreement are, with the exception of statutory appraisal rights, binding upon all stockholders. . . . Where the original purchase . . . has occurred prior to the stockholder approval and public announcement of the consolidation, the exchange of such shares in connection with a merger should always constitute a 'sale' for section 16(b) purposes if accomplished within six months of the original purchase." Note, *supra* note 31, at 1061.

the same had there been no purported merger. Although the holding may be limited to its facts, it is likely that the Securities and Exchange Commission will seek an amendment to section 16(b) to prevent beneficial owners who become such *voluntarily*[57] from being excluded by the exemption clause. This action was predicted in the argument by the Commission in its amicus brief, in which it contended that the provision was not "intended to afford a more than ten percent beneficial owner, who voluntarily attains such status . . . a method by which he may structure his sale transactions within the six-month period and thereby avoid liability for a substantial portion of profits realized on such transactions."[58] To remedy the ambiguity inherent in section 16(b) one theory has been proposed under which an insider who purchases more than ten percent and then sells within six months would be held liable for profits on ten percent of his total sales.[59] Such a proposal might serve the purpose of deterring insider speculation and thwart the splitting of sales which was done as in the instant case, in order to reduce the holdings to slightly less than ten percent and to remain free from liability for the disposition of the remaining holdings. Whatever proposals are adopted to regulate insider trading, the courts will be benefited by the enactment of more explicit guidelines which would remain consistent with the spirit of the Act and also free from liability those traders who have in no way abused their positions as holders of substantial interests in corporations.

57. In a recent case involving § 16(b) liability, defendant corporation unsuccessfully based its defense on the theory that it had become a beneficial owner "involuntarily." Since the case also involved a takeover bid, the district court held that defendant's acquisition of more than 10% of the corporation's common stock unquestionably was voluntary, and defendant therefore voluntarily assumed the obligations and burdens of a statutory insider under § 16(b). Abrams v. Occidental Petroleum Corp., 323 F. Supp. 570 (S.D.N.Y. 1970). However, the case was reversed by the Second Circuit on other grounds. 450 F.2d 157 (2d Cir. 1971); *see* notes 35 & 36 *supra*. *See also* Western Auto Supply Co. v. Gamble-Skogmo, Inc., 348 F.2d 736 (8th Cir. 1965), *cert. denied*, 382 U.S. 987 (1966).

58. Brief for SEC as Amicus Curiae at 13. The Commission also argued that "the exemptive provision of Section 16(b) was designed to avoid liability for changes in 10 percent beneficial owner status resulting from other than a voluntary purchase or sale, and not in situations, like the present one, involving a voluntary assumption of insider status by a purchase and a voluntary relinquishment of that status by a series of sales." *Id.* at 34.

59. 5 L. Loss, *supra* note 42, at 3023 (Supp. 1969).