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Recent Cases

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RECENT CASES

Criminal Law—Habeas Corpus—State Prison Regulation Probibiting Prisoner from Preparing Petition for Fellow Iumates Held Iuvalid in Absence of Alternative Meaus of Assistauce

Petitioner, an inmate in the Tennessee State Penitentiary, was placed in solitary confinement for repeated violations of a prison regulation forbidding inmates from assisting other prisoners in the preparation or filing of writs of habeas corpus.[1] Petitioner filed a motion in federal district court seeking release from solitary confinement and access to law books in order to resume aiding illiterate prisoners, unable to obtain other counsel, in the preparation of their petitions. Construing the motion as a petition for habeas corpus, the district court ordered petitioner's release from solitary confinement.[2] Respondent prison officials contended that regulations for the administration of prisons, absent interference with fundamental rights, are not subject to review by the courts and that petitioner's activity constituted unauthorized practice of law, which the individual states have sole authority to regulate. On appeal, the Court of Appeals for the Sixth Circuit reversed, holding that since prisoners in a penal institution have no federally protected right to the assistance of fellow inmates in preparing or filing petitions of habeas corpus, the prison regulation did not conflict with any federal right of habeas corpus.[3] On certiorari to the United States Supreme Court, *held*, reversed. Unless the state provides some reasonable alternative to assist inmates in the preparation of petitions for post-conviction relief, it may not enforce a regulation barring inmates from furnishing assistance to other prisoners in the preparation of petitions for habeas corpus. *Johnson v. Avery*, 394 U.S. ___ (1969).

Federal courts have traditionally been reluctant to entertain

1. Tenn. State Prison Reg.: "No inmate will advise, assist or otherwise contract to aid another, either with or without a fee, to prepare Writs or other legal matters. . . . Inmates are forbidden to set themselves up as practitioners for the purpose of promoting a business of writing Writs."

2. The district court held the prison regulation invalid because it effectively barred illiterate prisoners from access to federal habeas corpus and conflicted with 28 U.S.C. § 2242 (1964). Johnson v. Avery, 252 F. Supp. 783, 789 (M.D. Tenn. 1966).

3. Johnson v. Avery, 382 F.2d 353, 356-57 (6th Cir. 1967).

prisoners' claims of civil rights violations by prison authorities.[4] This reluctance is based on the belief that the management and discipline of penal institutions is the responsibility of the executive department which "must be allowed to exercise a largely unfettered discretion in deciding what security measures are appropriate."[5] Despite this judicial unwillingness to supervise prison administration, official practices or regulations denying or obstructing prisoners' access to the courts have been invalidated[6] under the due process[7] and equal protection[8] clauses of the Constitution. However, prison regulations which merely make access to the courts more difficult[9] have generally been upheld in deference to the policy of noninterference with matters of prison discipline. Consequently, the validity of prison regulations limiting the times and places in which inmates may engage in the preparation of legal documents has been upheld.[10] Similarly, efforts to

4. *See generally* Note, *Beyond the Ken of the Courts: A Critique of Judicial Refusal to Review the Complaints of Convicts*, 72 YALE L.J. 506 (1963). Several recent decisions have shown, however, that some courts are becoming more willing to intervene. *See, e.g.*, Pierce v. La Vallee, 293 F.2d 233 (2d Cir. 1961); Jordan v. Fitzharris, 257 F. Supp. 674 (N.D. Cal. 1966); United States *ex rel.* Hancock v. Pate, 223 F. Supp. 202 (N.D. Ill. 1963); Redding v. Pate, 220 F. Supp. 124 (N.D. Ill. 1963). *See also* Note, *Constitutional Rights of Prisoners: The Developing Law*, 110 U. PA. L. REV. 985, 987 (1962).

5. Roberts v. Pegelow, 313 F.2d 548, 550 (4th Cir. 1963) (upholding prison authorities' prohibition against practice of Muslim religion by inmates); *accord*, United States v. Marchese, 341 F.2d 782 (9th Cir.), *cert. denied*, 382 U.S. 817 (1965); McCloskey v. Maryland, 337 F.2d 72 (4th Cir. 1964); Kirby v. Thomas, 336 F.2d 462 (6th Cir. 1964); Sostre v. McGinnis, 334 F.2d 906 (2d Cir.), *cert. denied*, 379 U.S. 892 (1964); Siegal v. Ragen, 180 F.2d 785 (7th Cir.), *cert. denied*, 339 U.S. 990 (1950).

6. A state may not limit the writ to prisoners able to pay a $4 filing fee, Smith v. Bennett, 365 U.S. 708 (1961). Prison authorities have been denied authority to screen habeas corpus petitions, *Ex parte* Hull, 312 U.S. 546 (1941), to surpress the filing of prison appeals, Dowd v. United States *ex rel.* Cook, 340 U.S. 206 (1951), or to require prisoners to find persons outside of prison to file habeas corpus petitions on their behalf, White v. Ragen, 324 U.S. 760, 762 n.1 (1945); United States *ex rel.* Bongiorno v. Ragen, 54 F. Supp. 973, 976 (N.D. Ill. 1944), *aff'd*, 146 F.2d 349 (7th Cir.), *cert. denied*, 325 U.S. 865 (1945).

7. *E.g.*, *Ex parte* Hull, 312 U.S. 546, 549 (1941) (court apparently relied on this clause without so stating); Stiltner v. Rhay, 322 F.2d 314 (9th Cir. 1963), *cert. denied*, 376 U.S. 920 (1964); Hatfield v. Bailleaux, 290 F.2d 632, 636 (9th Cir.), *cert. denied*, 368 U.S. 862 (1961).

8. *E.g.*, Dowd v. United States *ex rel.* Cook, 340 U.S. 206 (1951); Cochran v. Kansas, 316 U.S. 255 (1942); Haines v. Castle, 226 F.2d 591 (7th Cir. 1955) (dictum).

9. Oregon *ex rel.* Sherwood v. Gladden, 240 F.2d 910, 911 (9th Cir. 1957); Austin v. Harris, 226 F. Supp. 304, 307 (W.D. Mo. 1964) (restriction on times during which inmates may work on legal documents). The following prison regulations have been sustained: prohibition against carrying on legal work in cells, Hatfield v. Bailleaux, 290 F.2d 632, 638 (9th Cir.), *cert. denied*, 368 U.S. 862 (1961); Austin v. Harris, *supra*; limitation on the percentage of a prisoner's personal funds that may be used to purchase legal materials, Hatfield v. Bailleaux, *supra*.

10. The purpose of these regulations has been to discourage the "informal practice of law" by inmates. Hatfield v. Bailleaux, 290 F.2d 632, 639 (9th Cir.), *cert. denied*, 368 U.S. 862 (1961); Oregon *ex rel.* Sherwood v. Gladden, 240 F.2d 910 (9th Cir. 1957).

establish a right of access to legal materials have been resisted by the courts on the ground that legal materials are unnecessary for effective access to the courts,[11] since "a petition for a writ of habeas corpus properly contains allegations of fact alone, and . . . legal arguments are not a proper part thereof."[12] The Supreme Court has, however, emphasized the importance of the constitutional right of habeas corpus[13] and has insisted that post-conviction proceedings be more than a mere formality.[14]

Some authority for the proposition that inmates may aid indigent fellow prisoners in preparing habeas corpus petitions is found in section 2242 of the Judicial Code, which provides: "Application for a writ of habeas corpus shall be in writing signed and verified by the person for whose relief it is intended *or by someone acting in his behalf.*"[15] The latter phrase, added in 1948, was intended to reflect "the actual practice of the courts,"[16] which generally permitted one person to apply for habeas corpus on behalf of another where the real party in interest lacked physical access to the courts.[17] Prior to the instant case, however, federal courts had not directly faced the question of one prisoner's right to assistance from another. In *Siegel*

11. *E.g.*, Roberts v. Pepersack, 256 F. Supp. 415, 433 (D. Md. 1966); Hatfield v. Bailleaux, 290 F.2d 632, 639-40 (9th Cir.), *cert. denied*, 368 U.S. 862 (1961); Grove v. Smyth, 169 F. Supp. 852 (E.D. Va. 1958). *Compare* United States *ex rel.* Mayberry v. Prasse, 225 F. Supp. 752 (E.D. Pa. 1963) (denial of access to state procedural rules violates fourteenth amendment).

12. Oregon *ex rel.* Sherwood v. Gladden, 240 F.2d 910, 912 (9th Cir. 1957).

13. *E.g.*, Fay v. Noia, 372 U.S. 391, 400 (1963); Smith v. Bennett, 365 U.S. 708, 713 (1961); Bowen v. Johnston, 306 U.S. 19, 26 (1939); *Ex parte* Bollman & Swartwout, 8 U.S. (4 Cranch) 75, 95 (1807).

14. It has been held that the state must furnish indigent prisoners with a transcript of lower court proceedings for purposes of appeal. Long v. District Court, 385 U.S. 192 (1966); Griffin v. Illinois, 351 U.S. 12 (1956). *See also* Smith v. Bennett, 365 U.S. 708 (1961) (state statute requiring indigent prisoner to pay $4 filing fee before application for writ of habeas corpus is denial of equal proteetion); Burns v. Ohio, 360 U.S. 252 (1959).

15. 28 U.S.C. § 2242 (1964) (emphasis reflects 1948 amendment). The district court held that the prison regulation conflicted with the express words of § 2242 authorizing the filing of a petition "signed and verified by the person for whose relief it is intended or by someone acting in his behalf." The court interpreted the statute as permitting assistance from a layman in the preparation of an application for habeas corpus. Johnson v. Avery, 252 F. Supp. 783 (M.D. Tenn. 1966).

16. H.R. REP. No. 308, 80th Cong., 1st Sess. 178 (1947).

17. Thus lawyers or relatives have been allowed to prepare and verify petitions for persons threatened with extradition or deportation, Collins v. Traeger, 27 F.2d 842 (9th Cir. 1928); United States *ex rel.* Funaro v. Watchorn, 164 F. 152 (C.C.S.C.N.Y. 1908), or for members of the armed forces, United States *ex rel.* Bryant v. Houston, 273 F. 915 (2d Cir. 1921); *Ex parte* Dostal, 243 F. 664 (N.D. Ohio 1917).

18. 88 F. Supp. 996, 1000 (N.D. Ill. 1949), *aff'd*, 180 F.2d 785, 788 (7th Cir.), *cert. denied*, 339 U.S. 990 (1950).

v. Ragen,[18] a federal district court stated summarily that a prisoner has no constitutional right to practice law by way of preparing habeas corpus petitions for other prisoners. More recently, the Ninth Circuit, in *Wilson v. Dixon*,[19] refused to consider a habeas corpus petition prepared and filed by a fellow inmate. Conceding that section 2242 recognizes the right of one person to sue for habeas corpus on behalf of another, the court noted that the right exists only when the petition explains the necessity for assistance. While defining the need for counsel in pre-trial stages,[20] the Supreme Court, without regard to the possible existence of a federal right to assistance in applying for habeas corpus, has neither indicated that constitutional rights could be protected through representation by a layman, nor that representation by counsel in the post-conviction period is an indispensable element of constitutional due process.[21] Furthermore, even if the right to assistance in applying for habeas corpus were to be established, the courts have traditionally recognized the right of individual states to regulate the practice of law within their borders,[22] although the Supreme Court has recently limited this state right to some extent.[23]

The Court in the instant case began with the fundamental proposition that "access of prisoners to the courts . . . may not be denied or obstructed."[24] Admitting that the disciplinary administration of state prisons is a state function, the Court asserted

19. 256 F.2d 536 (9th Cir.), *cert. denied*, 358 U.S. 856 (1958).

20. United States v. Wade, 388 U.S. 218 (1967); Miranda v. Arizona, 384 U.S. 436 (1966); Escobedo v. Illinois, 378 U.S. 478 (1964).

21. Several circuits have stated the advisability of appointing counsel in the post-conviction period. Taylor v. Pegelow, 335 F.2d 147 (4th Cir. 1964); Dillon v. United States, 307 F.2d 445 (9th Cir. 1962); United States *ex rel* Wissenfeld v. Wilkins, 281 F.2d 707 (2d Cir. 1960). A California court has specifically stated that no federal constitutional right to counsel exists prior to the filing of a petition indicating a prima facie case. People v. Shipman, 62 Cal. 2d 226, 229, 397 P.2d 993, 996-97, 42 Cal. Rptr. 1, 4 (1965). In Barker v. Ohio, 330 F.2d 594 (6th Cir. 1964), the court denied the existence of a right to counsel in a coram nobis proceeding.

22. *E.g.*, Konigsberg v. California State Bar, 366 U.S. 36 (1961); *In re* Anastaplo, 366 U.S. 82 (1961); *In re* Lockwood, 154 U.S. 116 (1894); Emmons v. Smitt, 149 F.2d 869 (6th Cir.), *cert. denied*, 326 U.S. 746 (1945); Niklaus v. Simmons, 196 F. Supp. 691 (D. Neb. 1961).

23. United Mine Workers v. Illinois State Bar, 389 U.S. 217 (1967) (Court invalidated state bar regulation prohibiting labor union from providing legal services to union members); Brotherhood of Railroad Trainmen v. Virginia *ex rel.* Virginia State Bar, 377 U.S. 1 (1964) (state bar regulation prohibiting labor union from providing legal services infringed upon exercise of first amendment guarantees in asserting rights under the Safety Appliance Act and the Federal Employer's Liability Act); NAACP v. Button, 371 U.S. 415 (1963) (Court invalidated state regulation of legal profession which prohibited NAACP from providing legal services to Negroes contesting racial discrimination).

24. 394 U.S. ___(1969).

that in instances where state regulations applicable to inmates conflict with paramount federal constitutional or statutory rights, the regulations may be invalidated. Here Tennessee had adopted a prison regulation which, in the absence of any other source of assistance for illiterate or poorly educated prisoners, effectively prevented such prisoners from filing habeas corpus petitions. Consequently, the Supreme Court endorsed the district court's conclusion that, since the initial burden of presenting a claim for post-conviction relief usually rests upon the prisoner himself, "[f]or all practical purposes, if such prisoners cannot have the assistance of a 'jailhouse lawyer' their possibly valid constitutional claims will never be heard in any court."[25] The Court concluded that although prison "writ writers" may menace prison discipline and burden the courts with their unskillfully drafted petitions, a state may not abridge the right to apply for a writ of habeas corpus. Since Tennessee did not offer a reasonable alternative to the assistance provided by other inmates and failed to demonstrate that its regulation had not effectively deprived those unable to prepare their own petitions of the constitutional right of habeas corpus, the regulation was held invalid. Concurring, Mr. Justice Douglas asserted that when the government fails to provide a prisoner with legal counsel and the prisoner's illiteracy prevents him from acting in his own behalf, the adequate presentation of meritorious claims requires mutual prisoner assistance.[26] In dissent, Mr. Justice White conceded that without some kind of assistance prisoners will be effectively denied access to the courts but expressed concern that prisoners will still be effectively barred from the courts if the help received from other inmates is not "reasonably adequate for the task."[27] Arguing that jailhouse lawyers cause unacceptable disadvantages to their clients, create severe disciplinary problems, and impose serious burdens on the courts, he suggested that the states provide reasonably adequate assistance to prisoners preparing post-conviction papers.[28]

The instant decision is a progressive step toward recognition of the practical realities of the petitioning prisoner's situation. As

25. *Id.* at ____, *quoting from* Johnson v. Avery, 252 F. Supp. 783, 784 (M.D. Tenn. 1966).

26. 394 U.S. at ____.

27. *Id.* at ____ (White & Black, JJ., dissenting).

28. The dissent apparently ignores the fact that at present no alternative means of assistance exist. While the suggestions made are noble, they do nothing to solve the issue at hand. It seems preferable that one prisoner is helped and the rest disappointed by the jailhouse lawyer then all being disappointed by the total lack of assistance.

indicated by the district court many prisoners are incapable of preparing without assistance an intelligible petition on their own behalf.[29] Such assistance cannot readily be obtained from outside the prison because the same disabilities which prevent the preparation of a meaningful petition by inmates will also hinder their efforts to contact an attorney to represent them, and many attorneys will not voluntarily represent a convict.[30] Even if the problem of effective communication with attorneys were solved, the prisoner desiring to petition has neither the right to appointed counsel nor the capability to retain paid counsel.[31] Thus, in the absence of prisoner assistance, his ability to petition depends upon the availability of free legal services. However, public and voluntary services are already overburdened and, because they are concentrated at the pre-trial and trial stages of the judicial process, cannot therefore afford satisfactory habeas corpus assistance. Further, assistance in the preparation of habeas corpus applications is not provided when the original trial of a prisoner was not handled by the public defender.[32] Thus, the federal right to habeas corpus becomes meaningless without prisoner assistance.

Three arguments have been advanced against allowing mutual prisoner assistance. One disadvantage of such assistance is that it creates discipline problems within the prison. Prison officials have testified that "aggressive inmates of superior intelligence exploit and dominate weaker prisoners of inferior intelligence" if they are allowed to engage in law practice.[33] While the problems of discipline might

29. Johnson v. Avery, 252 F. Supp. 783, 784 (M.D. Tenn. 1966). *See also* Note, *Constitutional Law: Prison "No-Assistance" Regulations and the Indigent Lawyer*, 1968 DUKE L.J. 343, 347-48, 360-61.

30. The Supreme Court has recognized that there is a dearth of lawyers who are willing to take on unprofitable and unpopular cases. NAACP v. Button, 371 U.S. 415, 443 (1963).

31. The Supreme Court has often held that a state may not interpose any financial restrictions between an indigent prisoner and his right of access to the courts. Long v. District Court, 385 U.S. 192, 194 (1966) (state may not withhold the privilege of appellate review because a prisoner lacks funds to buy a transcript); Smith v. Bennett, 365 U.S. 708, 709 (1961) (state may not make payment of a filing fee a prerequisite to obtaining a petition for habeas corpus).

32. E. MANCUSO, THE PUBLIC DEFENDER SYSTEM IN THE STATE OF CALIFORNIA 5 (1963). *See also* Gardiner, *Defects in Present Legal Aid Services and the Remedies*, 22 TENN. L. REV. 505 (1952); Note, *The Representation of Indigent Criminal Defendants in the Federal District Courts*, 76 HARV. L. REV. 579 (1963); Note, *Representation of Indigents in California—A Field Study of the Public Defender and Assigned Counsel Systems*, 13 STAN. L. REV. 522 (1961).

33. Hatfield v. Bailleaux, 290 F.2d 632, 639 (9th Cir.), *cert. denied*, 368 U.S. 862 (1961) (this problem was cited with approval as grounds for denying prisoners access to outside legal materials). In his dissent in the instant case, Mr. Justice White stated: "[i]t is not necessarily the best amateur legal minds which are devoted to jailhouse lawyering. Rather, the most aggressive

justify the regulation of the activities of jailhouse lawyers, the complete prohibition of their activities is unjustified unless reasonable alternatives are provided. In view of the present inadequacies of free legal services there is now no such alternative. A related objection is that prisoner assistance constitutes unlawful practice of law by laymen. The traditional argument for prohibition of unauthorized practice emphasizes protection of clients from ill-trained or unscrupulous advisors, but the application of this rationale to the denial of assistance among prisoners in the preparation of habeas corpus petitions overlooks several important considerations. Prisoner assistance in this area, whatever the danger of incompetent and unscrupulous practitioners, seems preferable to the alternative of no assistance. The absence of objection to the use of lay volunteers to aid the poor in obtaining welfare and solving domestic problems seems to negate the principal argument. Considering the inadequate supply of lawyers, there are many ministerial legal functions, such as filing welfare applications and grievances and applying for habeas corpus, that could and should be performed by laymen aiding the indigent.[34] Also, since a habeas corpus petition should contain only a factual account of the petitioner's claims, an acceptable petition can be drafted by persons with no legal knowledge or training. The unauthorized practice argument, therefore, does not justify an absolute restraint on prisoner assistance. A final argument which can be raised against prisoner assistance is that it may increase federal court work-loads. While prisoner assistance would probably increase the total number of petitions, the time required to separate valid petitions from groundless claims may be reduced, if such assistance improves the intelligibility of petitions, and therefore the increased burden of sifting through many applications may be offset by the legitimate claims discovered. The court work-load problem could be alleviated if the recommendation of the Federal Judicial Conference Committee on

and domineering personalities may predominate. And it may not be those with the best claims to relief who are served as clients, but those who are weaker and more gullible. Many assert that the aim of the jailhouse lawyer is not the service of truth and justice, but rather self-aggrandizement, profit, and power." 394 U.S. at ____ . *See also* Krause, *A Lawyer Looks at Writ-Writing*, 56 CALIF. L. REV. 371 (1968); Spector, *A Prison Librarian Looks At Writ-Writing*, 56 CALIF. L. REV. 365 (1968); Note, *supra* note 29; Note, *Legal Services for Prison Inmates*, 1967 WISC. L. REV. 514, 520-22; Note, *Prisoner Assistance on Federal Habeas Corpus Petitions*, 19 STAN. L. REV. 887, 89 n.31 (1967).

34. Hackin v. Arizona, 389 U.S. 143, 145-49 (1967) (Douglas J., dissenting). *See also* Samore, *Legal Services for the Poor*, 32 ALBANY L. REV. 509, 515-16 (1968); Sparer, Thorkelson & Weiss, *The Lay Advocate*, 43 U. DET. L.J. 493, 510-14 (1966).

Habeas Corpus that district courts adopt a standardized form for habeas corpus applications to aid both the petitioner and the courts in processing the complaint was adopted.[35]

In light of the recent Supreme Court decisions invalidating state regulations of the practice of law which restrict the exercise of constitutional rights,[36] and the footnote of the Court in the instant case affirming those decisions,[37] the prohibition of prisoner assistance under the guise of the state's right to regulate the legal profession is apparently invalid if such prohibition prevents prisoners from exercising their federal right of habeas corpus. If illiteracy and substandard intelligence of prisoners does in fact prevent them from preparing their own petitions and from contacting an attorney, the prohibition of prisoner assistance has the effect of denying prisoners access to the courts. As an alternative to allowing spontaneous jailhouse lawyering the Court might have required the state to provide adequate assistance to those who cannot prepare their own petitions. Such a requirement might best be met by Mr. Justice White's suggestion of a system of regulated trustees of the prison who would advise prisoners of their legal rights.[38] A regulated system of prisoner assistance would ensure that inmate clients receive genuinely helpful advice and would reduce the disciplinary problems caused by jailhouse lawyering. Considering the advantages and disadvantages of prisoner assistance and the shortcomings of any alternatives, prisoner assistance may prove to be the only presently workable solution to the lack of legal counsel available to the prisoner. The jailhouse lawyer is readily available and is likely to be recognized as a familiar and trustworthy peer, as contrasted with an unknown attorney. On balance, therefore, until feasible alternatives for helping illiterate prisoners are devised and implemented, prisoner assistance represents the best accommodation of the requirements of effective prison administration and the needs of prisoners unable to assert their own rights because of personal disabilities.

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35. *Applications for Writs of Habeas Corpus and Post Conviction Review of Sentences in the United States Courts*, 33 F.R.D. 363, 421 (1963). For a good discussion of the standardized habeas corpus application form see Note, *Prisoner Assistance on Federal Habeas Corpus Petitions*, 19 STAN. L. REV. 887, 893-94 (1967).

36. *See* note 23 *supra*.

37. 394 U.S. at ___ n.11, *citing* NAACP v. Button, 371 U.S. 415 (1963) (*see* note 23 *supra*). The Court stated: "The power of the states to control the practice of law cannot be exercised so as to abrogate federally protected rights." *Id.*

38. 394 U.S. at ___.

Securities Regulation—Corporatiou as a Director for the Purposes of Section 16(h) of the 1934 Securities Exchange Act

Plaintiff, a shareholder of the issuer corporation,[1] sought to recover under section 16(b) of the Securities Exchange Act [2] the "short-swing" profits realized by an acquiring corporation from the purchase and sale of the issuer's stock within a six month period. The stock had been purchased in contemplation of a merger while the chief executive officer of the acquiring corporation was a director of the issuer corporation and was sold one month after his resignation as director of the issuer corporation.[3] Following the issuer's refusal to prosecute, plaintiff initated this action[4] alleging that the chief executive officer was a deputy of the acquiring corporation, and that the corporation was therefore a director within the meaning of section 16(b).[5] Although the district court agreed that liability turned on the question of deputization, it held the evidence insufficient to establish the corporation's intent that the chief executive officer represent its interest in the issuer.[6] On appeal, the Second Circuit, *held,* reversed on

1. This was not a derivative suit; the action was brought to enforce a section 16(b) remedy created by the Securities Act of 1934. Blau v. Oppenheim, 250 F. Supp. 881, 885 (S.D.N.Y. 1966).

2. 15 U.S.C. § 78p(b) (1964): "For the purpose of preventing the unfair use of information which may have been obtained by such . . . director, . . . any profit realized by him from any purchase and sale, of [a] security of such issuer . . . within any period less than six months . . . shall inure to and be recoverable by the issuer . . . . 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 the sale."

3. Defendant Bunker, chief executive officer of Martin Marietta Corp. (Martin) served as a director of Sperry Rand Corp. (Sperry) from April 29, 1963, to August 1, 1963. Martin accumulated 801,300 shares of Sperry stock; 101,300 were purchased during Bunker's directorship. Betwecn August 29, 1963 and September 6, 1963, Martin sold all of its Sperry stock. Thus the stock purchased during Bunker's directorship was sold within 6 months of the purchase date.

4. Securities Exchange Act § 16(b), 15 U.S.C. § 78p(b) (1964), provides: "Suit to recover such profit may be instituted . . . in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request.

5. Martin had not acquired more than 10% of Sperry; thus, in order to be within the ambit of § 16(b) it must be either a director or an officer of Sperry.

6. Feder v. Martin Marietta Corp., 286 F. Supp. 937 (S.D.N.Y. 1968). In arriving at the determination the court made several relevant findings of fact. A memorandum in Martin's file containing information on the condition of Sperry was determined to be nothing more than information readily available to the public, and while the memorandum was admissible, it was to he accorded little weight. The approval by Martin's board of Bunker serving on Sperry's board was only a deputization to perform director's duties, not to represent Martin's interest. Furthermore, Bunker's letter of resignation to General MacArthur only indicated that being a Sperry director was too demanding on Bunker's time. The court also noted that: Bunker had a fine reputation as an engineer; Sperry, not Martin, took the initiative to encourage Bunker to

the facts and remanded.[7] A corporation which places a director on the board of a target corporation is a director for the purposes of section 16(b) of the Securities Exchange Act and is liable for short-swing profits if it sells stock of the issuer corporation within six months of purchase. *Feder v. Martin Marietta Corp.*, [current] CCH FED. SEC. L. REP. ¶ 92,333, at 97,590 (2d Cir., Jan. 14, 1969).

Section 16(b) of the Securities Exchange Act of 1934 was enacted to protect the public and "outside" stockholders from unfair use of information by corporate "insiders" for short-swing speculation.[8] The framers based liability on an objective measure of proof.[9] Section 16(b) liability attaches automatically to any profit[10] by an insider on any short-swing transaction within the six month time limit of the statute.[11] It is not necessary to show that the insider intended to profit from the use of confidential information[12] or even that the insider was privy to any confidential information;[13] nor is it a defense to show that the corporation made a settlement.[14] The courts have broadly

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join its board 2½ months before Martin began accumulating Sperry stock; and no other Martin man was ever mentioned for the position in the event Bunker absolutely declined.

7. Since the briefs did not agree as to the exact amount of profits from the sale, the case was remanded to determine profits, with interest to be awarded at the discretion of the trial court.

8. For a discussion of the background and effect of § 16(b), see Halleran & Calderwood, *Effect of Federal Regulation on Distribution of and Trading in Securities*, 28 GEO. WASH. L. REV. 86, 115 (1959).

9. Smolowe v. Delendo Corp., 136 F.2d 231, 235 (2d Cir.), *cert. denied*, 320 U.S. 751 (1943): "Mr. Corcoran, chief spokesman for the draftsmen and proponents of the [1934] Act, [citations omitted], [stated] '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.' " This remark has been called the understatement of the 20th century. Halleran & Calderwood, *supra* note 8, at 115.

10. Since the insider is required to disgorge the profits realized and the attorney is entitled to fees payable out of the amount recovered by the corporation, Smolowe v. Delendo Corp., 136 F.2d 231, 241 (2d Cir.), *cert. denied*, 320 U.S. 751 (1943), and the plaintiff need not be a stockholder at the time of the alleged insider transaction (*see* note 16 *infra*), some attorneys will search for violations through the monthly trading reports required by § 16(a) of the 1934 Act and then find a stockholder willing to sue. For text of § 16(a), see note 34 *infra*. One court noted an attorney's numerous appearances. Fistel v. Christman, 133 F. Supp. 300, 304 n.4 (S.D.N.Y. 1955).

11. Securities Exchange Act § 16(b), 15 U.S.C. § 78p(b) (1964), excludes a transaction where "such security was acquired in good faith in connection with a debt previously contracted . . . or any transactions which the Commission by rules and regulations may exempt." For such exemptions, see 17 C.F.R. §§ 240.16a-4 to .16b-10 (1968).

12. Blau v. Lamb, 363 F.2d 507, 515 (2d Cir. 1966), *cert. denied*, 385 U.S. 1002 (1967).

13. Farraiolo v. Newman, 259 F.2d 342, 344 (6th Cir. 1958), *cert. denied*, 359 U.S. 927 (1959).

14. Blau v. Hodgkinson, 100 F. Supp. 361 (S.D.N.Y. 1951).

construed section 16(b) in order to give effect to the remedial "interpretation most consistent with the legislative purpose"[15] even when that construction appears contrary to the literal meaning.[16] Although the majority in *Rattner v. Lehman*[17] held that the other partners were not required to account for partnership short-swing profits realized by them from stock of a corporation in which one of the partners was a director, Judge Learned Hand originated the theory of deputization in his concurring opinion.[18] In *Blau v. Lehman*,[19] in dictum recognizing that 16(b) did not extend farther than directors, officers and ten per cent shareholders,[20] the Supreme Court said that "Lehman Brothers, though a partnership, could for purposes of section 16(b) be a 'director' . . . and function through a deputy . . . ."[21] The question of deputization is a factual question to be resolved in each case,[22] and appellate review is limited to whether the lower court's ruling was "clearly erroneous".[23]

In the instant case, the court looked to the district court's findings of fact[24] and the evidence in the record to ascertain whether

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15. Alder v. Klawans, 267 F.2d 840, 844 (2d Cir. 1959) (liability imposed upon a director at the time of the sale whether or not he was such at the time of the purchase).

16. *E.g.*, Ozawa v. United States, 260 U.S. 178, 194 (1922); Stella v. Graham-Paige Motors Corp., 232 F.2d 299, 302 (2d Cir.), *cert. denied*, 352 U.S. 831 (1956) (dictum; all doubts resolved against insiders); Blau v. Mission Corp., 212 F.2d 77, 79 (2d Cir. 1954) (action allowed by shareholder who acquired stock subsequent to the violation); Colby v. Klune, 178 F.2d 872, 873 (2d Cir. 1949) (person performing functions similar to officer held an officer); Park & Tilford, Inc. v. Schulte, 160 F.2d 984, 987 (2d Cir.), *cert. denied*, 332 U.S. 761 (1947) (voluntary conversion of preferred to common stock held a purchase); Smolowe v. Delendo Corp., 136 F.2d 231, 239 (2d Cir.), *cert. denied*, 320 U.S. 751 (1943) (transfer between corporate officers for pre-existing debt held a sale); Blau v. Albert, 157 F. Supp. 816, 818-19 (S.D.N.Y. 1957) (2 year statute of limitations held not to run until shareholder could get knowledge of transaction); Blau v. Hodgkinson, 100 F. Supp. 361, 373 (S.D.N.Y. 1951) (stock of parent in exchange for stock of subsidiary under simplification plan that permitted cash instead of stock held a purchase); Truneale v. Blumberg, 80 F. Supp. 387, 392 (S.D.N.Y. 1948) (dictum; a receipt of warrants by an officer pursuant to his contract described as a purchase).

17. 193 F.2d 564 (2d Cir. 1952).

18. 193 F.2d at 567: "I agree that § 16(b) does not go so far; but I wish to say nothing as to whether, if a firm deputed a partner to represent its interests as a director on the board, the other partners would not be liable."

19. 368 U.S. 403 (1962).

20. 368 U.S. at 410-11; *cf.* Ellerin v. Massachusetts Mut. Life Ins. Co., 270 F.2d 259, 263 (2d Cir. 1959).

21. 368 U.S. at 409.

22. *Id.* at 408-09; Marquette Cement Mfg. Co. v. Andreas, 239 F. Supp. 962, 967 (S.D.N.Y. 1965) (evidence insufficient to show that director was deputy of corp.).

23. FED. R. CIV. P. 52(a). After considering all the evidence, the court may reverse if it is firmly convinced that a mistake was committed. Guzman v. Pichirilo, 369 U.S. 698, 702 (1962).

24. *See* note 6 *supra*.

or not those findings were clearly erroneous.[25] Recognizing that the chief executive officer approves all of the firm's financial investments, the court noted that with his position on the issuer corporation's board, he could utilize insider information for the benefit of his corporation without disclosing such information to other personnel; thus, he could be a deputy "even in the absence of factors indicating an intention or belief on the part of both companies that he was so acting."[26] The court felt that the letter of resignation indicated that the director served as a representative of the defendant corporation.[27] In addition, the court interpreted the acquiring corporation's approval of its officer's directorship as supporting the inference of deputization, even though such approval was required by its organizational policy. As further support of the same inference, the court noted that the defendant had placed deputies with similar functions on other corporate boards for the purpose of representing its interest. The court held that section 16(b) was applicable even though the officer was not a director when the stock was sold since the statutory exemption of transactions where one is not a beneficial owner both at the time of purchase and sale applies only to ten per cent shareholders and not to officers and directors.[28] The court also held SEC Rule 16A-10 to be invalid to the extent that it exempts a transaction from the operation of section 16(b) where a director resigns his post before the sale in order to evade the reporting requirement of section 16(a).[29]

Until now there have been no restrictions on corporate ownership of less than ten per cent of another company's stock. The holding in the instant case that a corporation can be a director for the purposes of section 16(b) raises many new problems.[30] Section 16(b)

25. [Current] CCH FED. SEC. L. REP. ¶ 92,333, at 97,590, 97,592 n.2 (2d Cir. Jan. 14, 1969).

26. *Id.* at 97,593.

27. Bunker's letter of resignation to General MacArthur, the chairman of the Sperry Board of Directors stated: "When I became a member of the Board in April, it appeared to your associates that the Martin Marietta ownership of a substantial number of shares of Sperry Rand should have representation on your Board. The representation does not seem to me really necessary, and I prefer not to be involved in the affairs of Sperry Rand when there are so many other demands on my time . . . ." *Id.* at 97,593.

28. See the final sentence of § 16(b) in note 2 *supra*. *See also* 2 L. LOSS, SECURITIES REGULATION 1060 (2d ed. 1961).

29. Prior case law held that a purchase before appointment as a director, followed by a sale within 6 months of purchase but after being appointed a director was subject to liability under § 16(b). Adler v. Klawans, 267 F.2d 840, 844 (2d Cir. 1959).

30. See Stabler, *Firms as 'Insiders': Concerns Buying Stock in Other Corporations Face New Legal Peril*, Wall St. J., Feb. 24, 1969, at 1, col. 6 (Sw. ed.), where the far-reaching ramifications were described as "a whole new can of worms." For a suggestion of problems of legal ethics which may arise under 16(b), see note 10 *supra*.

liability was based on objective criteria to avoid the problem of proving intent or actual unfair use of inside information. The court here, however, has impaired the application of section 16(b) by introducing similar evidentiary problems in requiring a factual demonstration of deputization.[31] Certainty of application under section 16(b) has been moved dangerously close to the uncertainty prevalent in proceedings under section 10(b) where the courts have imposed liability on insiders without the benefit of congressionally sanctioned standards.[32] In addition to the uncertainty introduced, it seems rather unsound to hinge the likelihood of utilization of inside information on the deputization question. The court could have achieved the same result by interpreting section 3(a)(7) to include a corporation as the director and its executive officer as its agent.[33] As was evidenced by this indirect manner of action, the court was hesitant to recognize all the tacit problems created when one corporation is a director of another.

One apparent result of the case is that the deputy's corporation will be required to file insider trading reports under section 16(a) of the 1934 Act[34] and to sign securities registration materials with the concomitant liability for material misstatement or omissions in the documents.[35] Another effect of this decision is to deter corporate

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31. Although the court suggests that this decision serves the congressional purpose, "legislative history indicates that the omission of any provision [requiring partners of a director to account for profits realized by them] was intentional [, because an earlier draft] made liable any person who acted on confidential information disclosed by a director, but such a provision was eliminted from the statute as finally enacted." Rattner v. Lehman, 193 F.2d 564, 566 (2d Cir. 1952).

32. SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968); Note, *Texas Gulf Sulphur: Its Holdings and Implications*, 22 VAND.L. REV. 359 (1969).

33. Securities Exchange Act of 1934 § 3(a)(7), 15 U.S.C. § 78c(a)(7) (1964), provides: "The term 'director' means any director of a corporation or any person peforming similar functions with respect to any organization, whether incorporated or unincorporated."

Securities Exchange Act of 1934 § 3(a)(9), 15 U.S.C. § 78c(a)(9) (1964), provides: "The term 'person' means an individual, a corporation, a partnership . . . ."

34. Securities Exchange Act of 1934 § 16(a), 15 U.S.C. § 78p(a) (1964), provides: "Every person who is . . . a director or an officer of the issuer . . . shall file . . . a statement . . . of the amount of all equity securities of such issuer of which he is the beneficial owner, and . . . each calendar month thereafter, if there has been a change in such ownership during such month . . . ."

35. Liability is usually predicated on the Securities Act of 1933 §§ 11, 17(a), 15 U.S.C. §§ 77k, 77q, (1964), or Securities Exchange Act of 1934 §§ 10, 18, 20, 15 U.S.C. §§ 78j, 78r, 78t (1964). Signing such statements can be costly. One court has even allowed punitive damages against the president of the issuer corporation and the underwriter for material misstatements in the offering circular. Globus v. Law Research Service, Inc., 287 F. Supp. 188 (S.D.N.Y. 1968), *noted in* 22 VAND. L. REV. ____ (1969).

executives from serving on other boards.[36] While the instant case arose in the context of an abortive merger attempt, equally perplexing problems are presented by the presence of bank officers and underwriters on the boards of many companies.[37] The court responded to a generally recognized need for guidance in this complex and unclear area of securities law, but the adoption of an equivocal standard, despite the intended objective operation of the statute to avoid the very problems here introduced, emphasizes the need for a definitive congressional statement.

36. Gartner, *'Thanks, but . . .': Many Executives Reject Proffered Board Seats As Perils of Post Mount*, Wall St. J., March 13, 1969, at 1, col. 6 (Sw. ed.).

37. Possibly deputization would be more difficult to demonstrate in these situations, yet in the situation of a bank that requires a board position in exchange for the extension of credit to an ailing concern, it would appear that the concept of deputization would be applicable.