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RECENT CASES

Civil Rights—Exclusion of Wage Earners as a Class from Jury Service in State Courts Violates Defendants' Constitutional Rights

Negroes Edgar Labat and Clifton Poret were convicted of aggravated rape of a white woman by an all-white jury of Orleans Parish, Louisiana, criminal district court. The jury venire contained the names of Negroes, but at the time of trial no Negro had ever served on a petit jury in an Orleans Parish criminal case and the one Negro who had served on a grand jury did so by mistake.[1] A great number of potential Negro jurors were eliminated as a result of the practice of excluding the names of daily wage earners[2] from the jury wheel.[3] Since forty-seven per cent of the parish's Negro workers were within the excluded class,[4] defendants alleged that the systematic exclusion of Negroes from jury service denied them equal protection of the law under the fourteenth amendment.[5] Denying a petition for writ of

1. Eubanks v. Louisiana, 356 U.S. 584, 586 (1958).

2. LA. REV. STAT. ANN. § 15:174 (1950) allows exemption from jury service to attorneys, physicians, school teachers and other groups whose occupations serve similar public functions. There is no statutory sanction for exemptions to daily wage earners. Rather, the jury commission clerical staff avoids selecting manual laborers, daily wage earners and "outside" workers because such workers invariably ask to be excused from jury duty on the grounds that their absence from work results in a loss of money (Orleans Parish jurors were not compensated at the time of trial). Although LA. REV. STAT. ANN. § 15:192 (1950) apparently gives judges discretion to decide only upon the competency of jurors, daily wage earners on the general venire are usually excluded from the final venire if they so request due to financial hardship. See note 3 *infra*. The jury commissioners, thus, seized upon this apparent judge-made policy and eliminated daily wage earners in advance by excluding their names from the jury wheel.

3. LA. REV. STAT. ANN. § 15:194 (1950) requires maintenance of a jury wheel (general venire) with the names of at least 750 prospective jurors. From this wheel the grand jury venire is selected and the petit jury venires are drawn at random. Seventy-five names are selected from the grand jury venire from which the judge selects twelve grand jurors. The commission then draws at random 150 names for the proposed petit jury venire. From this proposed venire the judge selects a final venire of about 75, usually asking for volunteers. This is the point at which daily wage earners included in the general venire can generally ask for and be granted exemption from jury service.

4. The effect of this exclusion obviously greatly reduced the percentage of Negroes likely to be called for jury service. Whereas the Orleans Parish Negro population was 32% in the 1950 census, it was stipulated at trial in the instant case that jury commissioners since 1936 had certified Negroes as qualified for petit jury venires in numbers approximately 10% of the venire. A study of a sample of proposed jury veniremen showed even more blatant Negro underrepresentation. Of 8657 proposed veniremen studied from 1948 to 1953, an average of 6.2% were Negroes. Of this number 4094 were selected for the final venire, and of these final veniremen, only an average of 3.7% were Negro.

5. Defense made its motion to quash indictment based on improper venire three and one-half months before trial, attacking both the grand jury and general venires.

habeas corpus, a Louisiana federal district court ruled that defendants had waived their right to object to the jury composition, that race disproportions on the jury panel were due to adherence to reasonable state laws, and that there was no proof of systematic exclusion of Negroes.[6] On appeal to the Fifth Circuit Court of Appeals, *held*, reversed. The unexplained absence of Negro jurors and systematic exclusion of daily wage earners from jury service violate the equal protection and due process clauses of the fourteenth amendment. *Labat v. Bennett*, 365 F.2d 698 (5th Cir. 1966), *cert. denied*, 35 U.S. L.W. 3355 (April 11, 1967).[7]

The Supreme Court has often enunciated the broad principle that systematic exclusion of any "definable class" from jury service is a denial of equal protection of the law as guaranteed by the fourteenth amendment.[8] The cases so holding, however, have dealt solely with the exclusion of a racial class from jury service,[9] and the long-continued exclusion of any such group in any jurisdiction raises a prima facie case of discrimination.[10] Although token inclusion of members of racial groups on jury venires will not satisfy constitutional requirements,[11] proportional representation is not required[12] and an indicting

However, until a writ of habeas corpus was applied for in 1957, every reviewing court (including the United States Supreme Court, see Michel v. Louisiana, 350 U.S. 91, 96 (1955)) treated the attack as solely upon the grand jury venire. Such attack was procedurally defective as untimely under LA. REV. STAT. ANN. § 15:202 (1950) and reviewing courts so ruled. The 1957 habeas corpus petition was based in part on new evidence but also clarified the attack on the general venire. However, the general venire attack was ignored by reviewing courts until 1960 when the Supreme Court, in vacating a Fifth Circuit affirmance of denial of writ of habeas corpus, remanded to district court for "disposition of the question whether members of petitioners' race were deliberately and intentionally limited and excluded in the selection of petit jury panels. . . ." United States *ex rel.* Poret v Sigler, 361 U.S. 375 (1960).

6. U.S. *ex rel.* Poret v. Sigler, 234 F. Supp. 171 (E.D. La. 1964).

7. Along with the instant case, the Fifth Circuit sat en banc to decide six other cases involving similar contentions as to exclusion of Negroes from juries. Rabinowitz v. United States, 366 F.2d 34 (5th Cir. 1966); Jackson v. United States (considered with Rabinowitz, *supra*); Brooks v. Beto, 366 F.2d 1 (5th Cir. 1966); Davis v. Davis, 361 F.2d 770 (5th Cir. 1966); Billingsley v. Clayton, 359 F.2d 13 (5th Cir. 1966); Scott v. Walker, 358 F.2d 561 (5th Cir. 1966).

8. Strauder v. West Virginia, 100 U.S. 303 (1880). A long line of decisions has adhered to this principle. See, *e.g.*, Arnold v. North Carolina, 376 U.S. 773 (1964); Eubanks v. Louisiana, *supra* note 1 (involving Orleans Parish jury system of the instant case); Patton v. Mississippi, 332 U.S. 463 (1947); Norris v. Alabama, 294 U.S. 587 (1935). For a state court decision applying the rule, see Harper v. State, 251 Miss. 699, 171 So. 2d 129 (1965).

9. See cases cited note 8 *supra;* Hernandez v. Texas, 347 U.S. 475 (1954) (involving exclusion of those with Mexican or Latin American names).

10. Cases cited note 8 *supra.*

11. See, *e.g.*, Cassell v. Texas, 339 U.S. 282 (1950); Smith v. Texas, 311 U.S. 128 (1940).

12. See, *e.g.*, Swain v. Alabama, 380 U.S. 202 (1965); Brown v. Allen, 344 U.S. 443 (1953).

or convicting jury need not include a representative of the defendant's particular class or racial group.[13] Such disparity can be explained, and a prima facie case rebutted, whenever the state establishes that exclusion is due to reasons other than racial or class discrimination.[14] Although the rule is clear as to the exclusion of racial classes, doubt exists as to the constitutionality of class exclusions based on other factors. In *Thiel v. Southern Pacific Co.*,[15] the Supreme Court exercised its supervisory power over federal courts to strike down a jury selection system which discriminated against daily wage earners, holding that trial by jury "contemplates an impartial jury drawn from a cross-section of the community."[16] The Court has also used its supervisory power to strike down federal juries from which women were excluded because a cross-section was not represented.[17] However, while some state courts have reached similar conclusions on federal constitutional grounds,[18] the Supreme Court, except in racial cases, has not specifically held that the cross-section requirement is based on the Constitution and appears reluctant to interfere with state jury selection procedures.[19]

Ruling first that the defendants had not waived their objections to the composition of the jury venires,[20] the Fifth Circuit in the instant case then turned to a consideration of the jury selection method. Although the Louisiana jury selection law was found to be non-dis-

13. Cases cited note 12 *supra*.

14. Patton v. Mississippi, *supra* note 8.

15. 328 U.S. 217 (1946).

16. 328 U.S. at 220.

17. Ballard v. United States, 329 U.S. 187 (1946); Glasser v. United States, 315 U.S. 60 (1942). Both cases involved exclusion of women from juries. The Court also speaks of the cross-section requirement in racial exclusion cases. In *Brown v. Allen*, for example, the Court said a jury source list is proper "so long as the source reasonably reflects a cross-section of the population . . . ." 344 U.S. at 474.

18. See, *e.g.*, State v. Madison, 240 Md. 265, 213 A.2d 880 (1965); Schowgurow v. State, 240 Md. 121, 213 A.2d 475 (1965). Both cases involved exclusion from the jury of persons who refused to state they believed in God. See also Allen v. State, 110 Ca. App. 56, 137 S.E.2d 711 (1964), where a white defendant active in Negro voter registration successfully attacked an array of petit jurors on equal protection and due process grounds.

19. See Moore v. New York, 333 U.S. 565 (1948) and Fay v. New York, 332 U.S. 261 (1947), upholding convictions by New York "blue ribbon" juries. This statutory jury is composed of persons qualified by education and background to handle intricate factual situations and/or difficult legal questions. However, in *Fay* the Court did point out that the "blue ribbon" jury statute did not exclude persons on the basis of race, occupation or economic class.

20. The district court based its denial of writ of habeas corpus alternatively on waiver of objection to the jury composition and on the merits. The Fifth Circuit found the waiver question controlled by Fay v. Noia, 372 U.S. 391 (1963), and said absent an intentional by-pass of a known right, and absent deliberate passing over of a known procedural requirement, a defendant does not forego his right to assert a constitutional right in a federal habeas corpus proceeding. 365 F.2d at 710.

criminatory on its face,[21] its administration was said to have abridged petitioners' fourteenth amendment rights to due process and equal protection of the law. The court first held that the consistent absence of Negro jurors raised a prima facie case of discrimination,[22] and that the state's explanation of a benign exemption to daily wage earners was insufficient to rebut this inference.[23] Furthermore, the exemption practice itself was held to violate the defendants' right to equal protection and due process by denying them trial by a cross-section of the community. The proper test for jury selection was said to be the fairness of the system to defendants, and the economic hardship imposed upon prospective jurors was considered irrelevant to the constitutionality of the selection process. Circuit Judge Bell[24] concurred that the exclusion of daily wage earners was unconstitutional, but he attributed the absence of Negroes on parish juries to a liberal granting of excuses for hardship and the volunteer system of jury service,[25] rather than to a policy of deliberate exclusion.

Although the Fifth Circuit's holding as to the prima facie case of discrimination raised by the history of exclusion of Negroes from jury service is in line with authority,[26] the Supreme Court has never before required a cross-section jury in state courts as a matter of constitutional due process. Since the Fifth Circuit held in the instant case that the cross-section jury question goes to the very fairness of the trial,[27] however, it apparently intends to describe a broader right than

21. The court interpreted LA. REV. STAT. ANN. § 15:174 (1950) as demonstrating a public policy to require jury service of daily wage earners despite economic hardship, since the statute enumerated other occupations exempted from jury service for public policy reasons. 365 F.2d at 727.

22. "The system was neutral, principled, and—foolproof: No Negro ever sat on a grand jury or a trial jury in Orleans Parish." 365 F.2d at 725.

23. The court said the jury commission had inherited a selection system which had produced no Negro jurors; that failure to take action to produce some Negroes for jury service gave rise to a presumption of purposeful discrimination. "Its failure to change the system amounted to a deliberate decision to continue systematic limitation of Negroes on the venires." 365 F.2d at 715-16. It should be noted that a Fifth Circuit decision, Collins v. Walker, 329 F.2d 100 (5th Cir. 1964), had reversed a conviction on denial of equal protection grounds due to the purposeful inclusion of Negroes on a list from which the grand jury was selected. Such a requirement of "color blindness" would have caused consternation for commissioners faced with a jury system such as in the instant case since the commissioner would have a duty to select Negroes for the venire, but be unconscious of race in so doing. The Fifth Circuit rescued commissioners from such a dilemma in a case handed down along with the instant case reversing *Collins v. Walker*. See Brooks v. Beto, *supra* note 7 (purposeful inclusion of Negroes on grand jury held not to violate due process or equal protection).

24. 365 F.2d at 739. Circuit Judge Coleman joined in Judge Bell's concurring opinion.

25. See notes 2 & 3 *supra*.

26. Cases cited note 8 *supra*.

27. "The 'very integrity of the fact-finding process' depends on impartial venires representative of the community as a whole." 365 F.2d at 723.

that protected by the equal protection clause in the racial exclusion cases.[28] Although *Thiel*[29] made the jury standard clear for federal courts, the subsequent enactment of 28 U.S.C. sec. 1863(b) gives a district judge discretion to excuse a class or group where there is a finding that jury service would entail undue hardship. This discretion was vested in district judges in order to conserve court time by allowing class exclusions to be handled administratively rather than on a case-by-case basis by judges themselves.[30] Orleans Parish commissioners apparently had such judicial time-saving in mind in the instant case, but the class exemption here was held to violate the traditional ideal of a "judgment of [one's] . . . peers."[31] The problem is thus presented of how to assure trial by one's peers, now defined as a cross-section of the community, without imposing hardship on jurors or unduly burdening courts with numerous hearings on exemptions from jury service. The best solution, of course, is to raise juror pay and thereby eliminate the hardship problem. Unfortunately, most states are not fiscally able to meet such a burden.[32] Until such a solution is possible, the better alternatives would seem to be either to disallow the class exclusion and require excuses to be on an individual basis; or, as in the federal courts, to allow class exclusion on a judge's finding which is open to review.[33] The former procedure would still involve some inconvenience to a hardship class, and both alternatives would require court time. Either method, however, would protect the cross-section standard better than

28. Under the Fifth Circuit reasoning, anyone would have standing to attack a jury system which systematically excluded a class or group; whereas, in the equal protection cases, the courts have difficulty in finding standing to challenge an array for one not a member of the class or group discriminated against. See Allen v. State, *supra* note 18.

29. *Supra* note 15.

30. United States v. Flynn, 216 F.2d 354 (2d Cir. 1954).

31. Magna Carta ch. 39.

32. Current per diem rates paid jurors in Southern states are: Alabama, $6 per day, ALA. CODE tit. 11, § 98 (1959); Arkansas, $7.50 per day, ARK. STAT. ANN. § 39-301 (1956); Florida, $5 per day, FLA. STAT. ANN § 40.24 (1961); Georgia, $2 to $10 per day (rate fixed by first grand jury of court term), GA. CODE ANN. § 59-120 (1965); Louisiana still lets each parish set juror compensation, LA. REV. STAT. ANN. § 15:529.8 (1950); Mississippi, $8 per day, MISS. CODE ANN. § 3959 (Supp. 1964); North Carolina, $3 to $8 per day (rate fixed by jury commissioners), N.C. GEN. STAT. § 9-5 (Supp. 1965); South Carolina provides for juror compensation on a county-by-county basis with rates ranging from $2 to $7.50 per day with one county paying $10 per day, S.C. CODE ANN. § 38-308 (Supp. 1965); Tennessee, $8 per day, TENN. CODE ANN. § 22-401 (Supp. 1966); Virginia, $5 per day, VA. CODE ANN. § 8-204 (Supp. 1966). In addition, most states allow jurors minimal travel and some other expenses.

33. 28 U.S.C. § 1863(b) (1964). The Fifth Circuit in a companion case to the instant case said the daily wage earner class could possibly be exempted from jury service on the basis of this statute, but that such exemption would require an appropriate finding and with appropriate limitations. Rabinowitz v. United States, *supra* note 7, at 54 n.49.

a selection system similar to that of the instant case. If a cross-section venire is indeed a constitutional requirement, the additional problem arises as to how representative the cross-section selection must be.[34] Although city directories, telephone books, voter lists, tax records and other similar compilations are used by state jury commissioners, none assure a perfect cross-section of the community.[35] The Supreme Court noted the problem in *Brown v. Allen*[36] where it approved a tax list as juror source since it was the most comprehensive list available short of a census or required registration; and in its most recent decision in the area,[37] the Court refused to impose a rigid source list standard, stating that an imperfect jury selection system was not equivalent to discrimination. Therefore, although it was quite possible for the instant case to be used to impose on state courts the cross-section requirement now demanded of federal juries, it was unlikely that the Court would use this case to require a higher source list standard. However, since the Fifth Circuit's instant decision as to exclusion of Negroes from jury service was clearly correct, it is not surprising that the Supreme Court forewent a resolution of even the cross-section issue by denying certiorari.

34. Even federal courts have not required that the jury venire be a perfect cross-section of the community. See Padgett v. Buxton-Smith Mercantile Co., 283 F.2d 597 (10th Cir. 1960).

35. Non-city residents are not included in city directories, not all persons have telephones, nor are all registered to vote, nor do all pay taxes. Another popular source of prospective jurors, the 'key man' system, is limited by the number of acquaintances of several 'key men' from different sections of a state, district or county who are asked to suggest names of prospective jurors. This system is described in Padgett v. Buxton-Smith Mercantile Co., *supra* note 34.

36. 344 U.S. 443 (1953).

37. Swain v. Alabama, 380 U.S. 202 (1965).

International Law and Trademark Infringement—Rights of Former Owners of Confiscated Cuban Businesses Under Hickenlooper Amendment

The interventors[1] of five confiscated Cuban cigar companies brought suit to restrain the prosecution of actions instituted on behalf of the former owners of the cigar companies, and to have the interventors' attorneys substituted as counsel for plaintiffs in each of the actions. The suits had been brought against the United States importers[2] to recover the value of Cuban cigars sold and delivered to the importers after the confiscation, and for alleged trademark infringement. The former owners contended that they were entitled to the money due on the goods because the Cuban decrees under which the businesses were confiscated violated international law, thereby permitting recovery under the Hickenlooper amendment[3] on the merits of the claim. The interventors urged restraint of the suits on the grounds that the federal act of state doctrine[4] precluded a determination of the validity of the Cuban decrees or the trademark rights of the businesses involved. On a motion for summary judgment in the federal district court, *held,* confiscation by a state of the property of its own nationals does not constitute a violation of international law under the Hicken-

1. The interventors (spelling adopted from the Cuban Decree) were designated by the Cuban government to operate the businesses taken over by the government on Sept. 15, 1960. The former owners were ousted from control under Cuban Law No. 647, Nov. 24, 1959, as amended by Law No. 843, July 6, 1960.

2. Apparently apprehensive of double liability, the importers in the United States failed to pay the purchase price for cigars shipped after the take-over.

3. Foreign Assistance Act of 1964, § 301(d)(4), 78 Stat. 1009, 22 U.S.C. § 2370(e)(2) (1964): "Notwithstanding any other provision of law, no court in the United States shall decline on the ground of the federal act of state doctrine to make a determination on the merits giving effect to the principles of international law in a case in which a claim of title or other right is asserted by any party including a foreign state (or a party claiming through such state) based upon (or traced through) a confiscation or other taking after January 1, 1959, by an act of that state in violation of the principles of international law, including the principles of compensation and the other standards set out in this subsection: *Provided,* that this subparagraph shall not be applicable (1) in any case in which an act of a foreign state is not contrary to international law or with respect to a claim of title or other right acquired pursuant to an irrevocable letter of credit of not more than 180 days duration issued in good faith prior to the time of the confiscation or other taking, or (2) in any case with respect to which the President determines that application of the act of state doctrine is required in that particular case by the foreign policy interests of the United States and a suggestion to this effect is filed on his behalf in that case with the court, or (3) in any case in which the proceedings are commenced after January 1, 1966."

4. The most frequently quoted statement of this doctrine is: "[E]very sovereign State is bound to respect the independence of every other sovereign State, and the courts of one country will not sit in judgment on the acts of the government of another done within its own territory." Underhill v. Hernandez, 168 U.S. 250, 252 (1897).

looper amendment and interventors are entitled to enjoin the suit of the former owners challenging the validity of the Cuban decrees.[5] Similar confiscation of trademark benefits, however, is not protected by the act of state doctrine where the situs[6] of the trademark and the good will symbolized by it are in the United States, and previous owners may therefore proceed in the United States with the suit for trademark infringement. *F. Palicio y Compania, S.A. v. Brush,* 256 F. Supp. 481 (S.D.N.Y. 1966).

In its simplest terms, the act of state doctrine provides that the courts of one country will not sit in judgment on the public acts of another country committed within its own territory.[7] The original reason for the doctrine appears to be deference to the principle of the absolute sovereignty of nations,[8] but courts in the United States have also considered international comity, domestic separation of powers, and possible embarrassment to the executive in its conduct of foreign affairs as reasons for application of the doctrine.[9] The major criticism

5. The Hickenlooper amendment excludes application "in any case in which an act of a foreign state is not contrary to international law." Foreign Assistance Act of 1964, § 301(d)(4), 78 Stat. 1009, 22 U.S.C. § 2370(e)(2) (1964).

6. Here situs means location with regard to whether the trademark is located in the country of the main foreign business or whether it is located in the country in which it is registered and where its good will exists.

7. Underhill v. Hernandez, 168 U.S. 250 (1897).

8. American Banana Co. v. United Fruit Co., 213 U.S. 347, 358 (1909); The Schooner Exch. v. McFaddon, 11 U.S. (7 Cranch) 116, 135 (1812); Reeves, *The Sabbatino Case: The Supreme Court of the United States Rejects a Proposed New Theory of Sovereign Relations and Restores the Act of State Doctrine,* 32 FORDHAM L. REV. 631, 633 (1964); Note, 44 N.C.L. REV. 466, 468 (1966). The act of state doctrine and the doctrine of sovereign immunity are distinguishable. The act of state doctrine is open as a defense to private litigants who may have obtained expropriated property from the acting government. The defense of sovereign immunity, however, is not open to the private litigant and can only be used by the sovereign or one of its agents who has acted in his official capacity. House, *The Law Gone Awry: Bernstein v. Van Heyghen Freres,* 37 CALIF. L. REV. 38, 50 (1949).

9. The doctrine rests on comity or "courtesy among nations," and not to apply it may "vex the peace of nations." United States v. Belmont, 301 U.S. 324, 328 (1937); Shapleigh v. Mier, 83 F.2d 673, 676 (5th Cir. 1936). Foreign relations is a "political question" requiring judicial restraint. Oetjen v. Central Leather Co., 246 U.S. 297 (1918). In American Banana Co. v. United Fruit Co., 213 U.S. 347 (1909), and Ricaud v. American Metal Co., 246 U.S. 304 (1918), the Court applied the doctrine and denied recovery, taking judicial notice of the State Department's political recognition of the foreign governments involved, which had the effect of retroactively validating the previous acts of the foreign governments. See 110 CONG. REC. 19546 (1964) (remarks of Senator Hickenlooper). The "Bernstein exception" to the act of state doctrine, arising initially out of confiscations by Nazi Germany, permits the judiciary to pass on the validity of foreign confiscatory decrees where the executive branch of the government has authorized them to do so. Bernstein v. N. V. Nederllandsche-Amerikaansche Stoomvaart-Maatshappij, 210 F.2d 375 (2d Cir. 1954). The act of state doctrine with the "Bernstein exception" was apparently controlling until 1964. Kane v. National Institute of Agrarian Reform, 18 Fla. Supp. 116 (Cir. Ct. 1961). As is indicated in Note, 44 N.C.L. REV. 466, 471 (1966), the full effect of *Bernstein* was never known since it was not appealed to the Supreme Court because of an approved

of the doctrine has been that it permits decrees of foreign countries which are contrary to the public policy and laws of the United States to go unchallenged in United States' courts.[10] In 1964 the Supreme Court of the United States, in *Banco Nacional de Cuba v. Sabbatino*,[11] extended the act of state doctrine to apply even where there was a possible violation of international law.[12] Dissatisfied with this result, Congress enacted the Hickenlooper amendment[13] which

settlement. Cases applying the doctrine prior to *Bernstein* include: Underhill v. Hernandez, *supra* note 7 (Venezuelan revolutionary government); Banco de Espana v. Federal Reserve Bank, 114 F.2d 438 (2d Cir. 1940) (Spanish Loyalist government); Salimoff & Co. v. Standard Oil Co., 237 App. Div. 686, 262 N.Y.S. 693 (1st Dep't 1933) (Russian revolution).

10. A decree under which there is confiscation without compensation is obviously contrary to the public policy of the United States. In discussing the original *Bernstein* case, in which Bernstein was denied recovery on the act of state doctrine, Zander argues: "Though there was no international delinquency in question (as the plaintiff was a German citizen at the time of the forced transfer), surely this was a case when the doctrine of public policy would have been safely and opportunely applied to strike out the defense based on the objectionable law. . . ." Zander, *The Act of State Doctrine*, 53 AM. J. INT'L L. 826, 833 (1959); Bernstein v. Van Heyghen Frères Société Anonymeé, 163 F.2d 246 (2d Cir.), *cert. denied*, 332 U.S. 772 (1947). The act of state doctrine has also been criticized from the standpoint that it is based on questionable precedents. It is argued that most of the early decisions on which the courts rely involved only sovereign's immunity from personal suit, not the *acts* of a foreign state. See 57 YALE L.J. 108 (1947).

11. 376 U.S. 398 (1964). All aspects of the *Sabbatino* litigation, from the time of worsening relations with Cuba and the United States to the decision by the Supreme Court are discussed in Reeves, *supra* note 8. Reeves commends the result reached by the Supreme Court, concluding that the new rule of law adopted by the lower courts would have "impaired the sovereignty" of the United States. Snyder, *Banco Nacional de Cuba v. Sabbatino: The Supreme Court Speaks*, 16 SYRACUSE L. REV. 15 (1964) criticizes the result reached by the Supreme Court, emphasizing the harmful effects the decision may have on future investments in newly developing foreign nations. The decision is also criticized in Stevenson, *The State Department and Sabbatino: "Ev'n Victors Are by Victories Undone,"* 58 AM. J. INT'L L. 707 (1964). The constitutional aspects of the Supreme Court's decision are discussed in Henkin, *The Foreign Affairs Power of the Federal Courts: Sabbatino*, 64 COLUM. L. REV. 805 (1964). The decisions of the lower courts are discussed in Falk, *Toward a Theory of the Participation of Domestic Courts in the International Legal Order: A Critique of Banco Nacional de Cuba v. Sabbatino*, 16 RUTGERS L. REV. 1 (1961) (district court), and Stevenson, *The Sabbatino Case—Three Steps Forward and Two Steps Back*, 57 AM. J. INT'L L. 97 (1963) (court of appeals). See also Lillich, *A Pyrrhic Victory at Foley Square: The Second Circuit and Sabbatino*, 8 VILL. L. REV. 155 (1963); Paul, *The Act of State Doctrine: Revived but Suspended*, 113 U. PA. L. REV. 691 (1965).

12. The district court found the confiscatory decrees to be in violation of international law. Banco Nacional de Cuba v. Sabbatino, 193 F. Supp. 375 (S.D.N.Y. 1961). The court pointed out that no court in the United States has passed on the question of whether a court could examine the validity of the act under international law and refuse recognition to the act if it were in violation of international law. The court went on to hold that the Cuban act violated international law because it was retaliatory, discriminatory, and without compensation. The court of appeals affirmed. 307 F.2d 845 (2d Cir. 1962).

13. Foreign Assistance Act of 1964, § 301(d)(4), 78 Stat. 1009, 22 U.S.C. § 2370(e)(2) (1964). The amendment originally applied to the period January 1, 1959, to January 1, 1966. It is now permanent law. 79 Stat. 653, § 301(d)(2) (1965).

encouraged the courts to determine on the merits cases involving foreign confiscation of property of American citizens. On remand of *Sabbatino*, the district court held the amendment constitutional and, applying it retroactively to the facts of the case,[14] found a violation of international law and held for the defendants.[15] The amendment is not to be applied, however, when the court determines there is no violation of the "principles of international law, including principles of compensation,"[16] but the "principles" referred to have not as yet been clearly defined.[17]

When a foreign manufacturer whose business has been confiscated attempts to enforce a claim for trademark infringement[18] in the United States, the defense usually offered is that any right in the trademark and its good will passed to the foreign government when the business was nationalized. Courts agreeing with this defense apply the indivisible or unitary theory of good will,[19] reasoning that American trademarks originate from use, not registration, and that the trademarks in question are symbolic of the good will of the main foreign

14. Banco Nacional de Cuba v. Farr, 243 F. Supp. 957 (S.D.N.Y. 1965). For a good discussion of this case, see Note, 44 N.C.L. REV. 466 (1966). The court applied the amendment retroactively even though Senator Hickenlooper stated that "It does not change the result in that [*Sabbatino*] case. . . ." 110 CONG. REC. 19557 (1964).

15. The Cuban representatives were plaintiffs seeking to recover the money due for sugar to which they had obtained title under a decree the court found in violation of international law. Therefore, the defense based on the Hickenlooper amendment was held valid, and the complaint of the Cuban representatives dismissed.

16. Foreign Assistance Act of 1964, § 301(d)(4), 78 Stat. 1009, 22 U.S.C. § 2370 (e)(2) (1964).

17. The instant case is the third interpretation of the amendment. American Hawaiian Ventures, Inc. v. Latuharhary, 257 F. Supp. 622 (D.N.J. 1966) was a libel in admiralty for alleged tortious conversion. The libelant asserted that the Hickenlooper amendment deprived Indonesia of any claim to sovereign immunity. The court did not discuss the amendment in any detail, and held that it did not bear on the real question of whether the court's jurisdiction over Indonesia would be defeated by its right to sovereign immunity for acts *jure imperii*. See also Banco Nacional de Cuba v. Farr, *supra* note 14.

18. The primary and proper purpose of a trademark is to identify the origin of the article to which the trademark is affixed, and protect the good will established in the particular trade or business. Hanover Star Milling Co. v. Metcalf, 240 U.S. 403, 412 (1915). In order to assert the right to enjoin others from using a trademark in the United States, a person must establish his ownership rights in the trademark through use in a United States business. Rogers v. Ercona Camera Corp., 277 F.2d 94 (D.C. Cir. 1960). This requirement is met for a foreign manufacturer when he gives an importer formal rights in trademark registration. E. Leitz, Inc. v. Watson, 152 F. Supp. 631 (D.D.C. 1957). See Callmann, *Worldmarks and the Antitrust Law*, 11 VAND. L. REV. 515, 520 (1958).

19. Callmann, *supra* note 18. "Good will can no more be separated from a business that reputation from a person. Good will *is* the business as it is viewed by others. . . . Good will may be wider in scope than the business itself. The good will of a business may embrace territories where neither the business nor its salesmen have ever been. The situs of the good will, wherever it may be, is the situs of the business." 1 CALLMANN, UNFAIR COMPETITION AND TRADE-MARKS 26 (2d ed. 1950).

business and not of the American establishment or branch. The situs of the trademark and its good will is therefore the situs of the foreign business.[20] However, the "indivisible unity" theory has not been applied in the more recent cases, and there is some indication that it has been abandoned.[21] Courts rejecting the "unity" theory hold that trademarks registered in the United States Patent Office, and the good will symbolized by them, have their situs in the territory where United States law is enforceable.[22] It is felt that to hold otherwise, particularly in a case of confiscation without compensation, would give extraterritorial effect to the foreign law, which is a violation of the public policy and law of the United States.[23]

The court in the instant case found that the confiscations of the property of Cuban nationals[24] was not a violation of international law, thereby limiting a determination of a violation of international law for the purposes of the Hickenlooper amendment to traditional interpretations of that field. The court noted that such decrees are contrary to the public policy of the United States,[25] but, notwithstanding the equities of the case, it felt constrained under *Sabbatino* to apply the act of state doctrine.[26] The court further concluded that the former owners' right to conduct business in the United States includes the right to make use of the good will already established in the United States, of which the trademarks are an integral part.[27] To allow the trademark rights to be detached from the good will would be to give an impermissible extraterritorial effect to the Cuban decrees. The former owners, therefore, could pursue claims for trademark infringement, although final determination would not be made on this motion.

20. Société Vinicole de Champagne v. Mumm Champagne & Importation Co., 10 F. Supp. 289 (S.D.N.Y. 1935).

21. Abel, *Confiscation and Trademarks*, 44 TRADEMARK REP. 1279 (1954).

22. Roger & Gallet v. Janmarie, Inc., 245 F.2d 505 (C.C.P.A. 1957).

23. Baglin v. Cusenier Co., 221 U.S. 580, 596 (1911). See also Collinson, *Sabbatino: The Treatment of International Law in the United States Courts*, 3 COLUM. J. TRANSNAT'L L. 27, 35 (1964).

24. The court noted that all five businesses were Cuban entities, organized under Cuban law and doing business in Cuba, and that none of the shareholders or officers was a citizen of the United States at the time of the intervention. F. Palicio y Compania, S.A. v. Brush, 256 F. Supp. 481, 487 (S.D.N.Y. 1966).

25. With regard to the possibility of giving extraterritorial effect to the decrees, the court said that because the interventors were claiming only the price of cigars shipped after the intervention, there was no property involved that was within the United States at the time of the confiscation which would have presented any danger of giving extraterritorial effect to the decrees. *Id.* at 492.

26. The court acknowledged that by allowing the interventors to sue it was "implementing and enforcing decrees which are abhorrent to our own policy and laws." 256 F. Supp. at 489.

27. The court noted that the former owners had continued to carry on some business in the United States in the names of their expropriated businesses, and had taken "prompt steps to enforce any trademark rights they might have." 256 F. Supp. at 492.

The court in *Brush* rejected a potentially extensive application of the Hickenlooper amendment and applied an accepted principle of international law in holding that the legality of the Cuban government's actions with regard to its own nationals could not be tested by international legal standards. The court's holding indicates that the acts of the confiscating country must be more than merely contrary to public policy of the United States in order to constitute a violation of international law under the Hickeulooper amendment. While the result reached by the court on the additional issue of trademark infringement was correct, it might better have based its decision solely upon grounds of federal trademark policy,[28] rather than upon a determination of the situs of the trademark. Even though the former owners have attempted to continue business under the same name in the United States, the existing trademark and good will are based on the use of Cuban tobacco, a commodity no longer available to the former owners. The actual situs of the trademark should be with the business able to produce the cigars with Cuban tobacco, *i.e.*, the business now run by the interventors. However, since the interventors now control the business under a decree contrary to the policy and laws of the United States, they should not be able to take advantage of trademark good will developed in the United States and to create confusion in the American public as to the source of the goods. Under this reasoning, the former owners may enjoin the importation of cigars bearing the old trademark not because they maintain rights to the trademark, but because utilization of it by the interventors violates federal trademark policy.

Jurisdiction—Minimum Contacts—First Amendment Requires a Greater Showing of Contact in a Libel Action To Satisfy Due Process Than Is Necessary in Other Types of Actions

Plaintiff, a public official,[1] sued the *New York Times* for libel in an Alabama federal district court as a result of a story which had been "gathered" in Alabama by a full-time reporter of the defendant. The defendant objected to the court's jurisdiction on the grounds that its

28. See 1 NIMS, UNFAIR COMPETITION AND TRADEMARKS 36 (4th ed. 1947).

1. The plaintiff, Mr. Eugene "Bull" Conner, was a City Commissioner of Birmingham, Alabama.

limited advertising solicitation,[2] news-gathering activities,[3] and distribution procedures[4] in Alabama fell short of the minimum contacts required for purposes of judicial jurisdiction under the due process clause and the first amendment.[5] The district court upheld service of process under Alabama's long-arm statute[6] and entered judgment upon a jury verdict for plaintiff. On appeal[7] to the Court of Appeals for the Fifth Circuit, *held*, reversed. When jurisdiction is asserted over a foreign newspaper corporation in a libel action, the first amendment requires a greater degree of contact with the forum state to satisfy due process than is required in suits arising from other tortious activities.[8] *New York Times Co. v. Conner*, 365 F.2d 567 (5th Cir. 1966).

The modern trend toward expansion of judicial jurisdiction began with *International Shoe Co. v. Washington*,[9] in which the Supreme Court held that jurisdiction over a foreign corporation would be upheld upon a finding of sufficient "minimum contacts" so as not to offend traditional notions of "fair play and substantial justice."[10] While the corporate activity in *International Shoe* was "continuous" and "systematic," issuance of a single re-insurance policy was later held sufficient to satisfy due process in *McGee v. International Life Insurance Co.*[11] A year after its decision in *McGee*, however, the Court cautioned that "It is a mistake to assume that this trend . . . [of liberality] heralds the

2. Advertising solicitation in Alabama represented from 25/1000 to 46/1000 of 1% of total advertising revenue.

3. Staff correspondents had been to Alabama seven times during the period in dispute (April 1, 1959 to August 22, 1960), in addition to the 5-day visit by Harrison Salisbury to gather the information for the allegedly libellous story.

4. Average daily circulation in Alabama was 395 copies of a total of 650,000. Alabama accounted for 2455 of 1,300,000 copies of the Sunday *Times*. New York Times Co. v. Conner, 365 F.2d 567, 570 (5th Cir. 1966).

5. *Id.* at 569.

6. ALA. CODE tit. 7, § 199(1) (Supp. 1965) provides: "Service on nonresident doing business or performing work or service in state.—Any . . . corporation not qualified under the . . . laws of this state as to doing business herein, who shall do any business . . . in this state shall, by the doing of such business . . . be deemed to have appointed the secretary of state . . . to be the true and lawful attorney or agent of such nonresident, upon whom process may be served in any action accrued or accruing, or resulting from the doing of such business . . . or as an incident thereof by any such nonresident, or his, its or their agent, servant or employee."

7. This is the third appeal of this case to the Fifth Circuit. For the prior history see 365 F.2d at 568-69.

8. Defendant's second contention on appeal was that the jury's finding of actual malice was not supported by any evidence. The Fifth Circuit recognized that the jury was properly instructed under the standard of New York Times Co. v. Sullivan, 376 U.S. 254 (1964), but after examining the evidence in detail, it concluded that "it is obvious that such evidence does not even approach the stringent requirements for showing actionable libel of a public official." 365 F.2d at 576.

9. 326 U.S. 310 (1945).

10. *Id.* at 320.

11. 355 U.S. 220 (1957).

eventual demise of all restrictions on the personal jurisdiction of state courts."[12] Despite this word of warning, courts have continued to construe state long-arm statutes liberally, and have held a single plane crash[13] and the shipment of a single defective product into the state[14] to be sufficient contact to establish jurisdiction under the *International Shoe* test. However, courts have generally required more than a single contact where jurisdiction over a newspaper corporation is in issue;[15] for example, several courts have indicated that distribution of a small percentage of the publication in the forum state will not alone subject the publisher to extra-territorial jurisdiction.[16] Where such factors as advertising and news solicitation are present in addition to distribution, there is a conflict as to whether there has been sufficient contact within the state. On the premise that its statute was as broad as due process would permit, the Alabama Supreme Court in *New York Times Co. v. Sullivan*,[17] held that jurisdiction based upon such contacts did not violate due process.[18] Yet the Fifth Circuit in *Buckley v. New York Times Co.*,[19] found insufficient contact under similar circumstances even though the Louisiana long-arm statute[20] was as broad as permissible under due process.[21] Until the instant case, however, no court had relied upon the first amendment as a basis for invalidating extra-territorial jurisdiction over a newspaper corporation.

In examining the contacts of the defendant with Alabama in the instant case, the court concluded that the *Buckley* decision, which had

12. Hanson v. Denckla, 357 U.S. 235, 251 (1958).

13. Elkhart Eng'r Corp. v. Dornier Werke, 343 F.2d 861 (5th Cir. 1965).

14. Gray v. American Radiator & Standard Sanitary Corp., 2 Ill. 2d 432, 176 N.E.2d 761 (1961).

15. The Supreme Court has had the opportunity to decide this question on two occasions. Polizzi v. Cowles Magazines, Inc., 345 U.S. 663 (1953); New York Times Co. v. Sullivan, *supra* note 8. In *Polizzi* the majority chose to rest its decision on a general venue statute. Mr. Justice Black, joined by Mr. Justice Jackson in dissent, would have found the defendant publisher doing business in the state sufficient for jurisdiction. However, the defendant had a circulation in the state of nearly 50,000 copies, in addition to a full time agent. 345 U.S. at 667-70. In *Sullivan* the Court felt foreclosed from reviewing the jurisdictional issue since the Alabama Supreme Court had held that the *Times* had put in a general appearance. 376 U.S. at 264 n.4.

16. See, *e.g.*, Insull v. New York World-Telegram Corp., 273 F.2d 166, 170 (7th Cir. 1959); Street & Smith Publications, Inc. v. Spikes, 120 F.2d 895, 897 (5th Cir.), *cert. denied*, 314 U.S. 653 (1941); Putnam v. Triangle Publications, Inc., 245 N.C. 432, 441, 96 S.E.2d 445, 452-53 (1957).

17. 273 Ala. 656, 670, 144 So. 2d 25, 34 (1962), *rev'd on other grounds*, 376 U.S. 254 (1964).

18. *Id.* at 669, 144 So. 2d at 33. The activities of the *Times* in *Sullivan* were almost identieal to those in the instant case. See *id.* at 665-66, 144 So. 2d at 29-30.

19. 338 F.2d 470 (5th Cir. 1964).

20. La. Rev. Stat. Ann. § 13:3471(1) (Supp. 1965).

21. Buekley v. New York Times Co., 338 F.2d 470, 475 (5th Cir. 1964). For the *Times'* circulation and solicitation activities in Louisiana, see *id.* at 473-74. For a comparison with those in Alabama, see note 3 *supra*.

held similar contacts insufficient to satisfy due process, was controlling.[22] The court rejected the contention that the Alabama statute was broader than the Louisiana statute since *Buckley* had defined the outer limits of due process; the court said this delimitation could not be expanded by the Alabama court's interpretation of its statute in *Sullivan*.[23] Furthermore, in distinguishing an Alabama tort case where jurisdiction was based upon a single plane crash,[24] the court held that first amendment considerations in a libel action required a greater showing of contacts to support jurisdiction than in a normal tort situation.[25] To support this conclusion, it examined two cases in which the Supreme Court invalidated state regulation in areas where possible abuse by the state would encroach on first amendment freedoms.[26] The majority felt that "the restriction on the exercise of jurisdiction over non-resident newspaper corporations imposed by *Buckley* should be viewed in the same light."[27] The dissent urged that *Buckley* was not controlling and emphasized that in *Buckley* the Associated Press had gathered the material, while in the instant case a *Times* reporter was sent to Alabama expressly to report the story. Since the dissent concluded that the Associated Press was not an agent of the *Times*,[28] the only contact with Louisiana in *Buckley* was the distribution of papers there, while in the instant case the alleged libel "grew out of the calculated and directed activities of an accredited agent of the *Times* within the State of Alabama."[29]

The effect of the decision in the instant case is to present the plaintiff in a libel action with significant jurisdictional barriers where the defendant is an out-of-state newspaper corporation. While the United States Supreme Court decision in *Sullivan* prevents public officials from using the substantive law of libel to thwart the first amendment freedoms of expression and criticism, the instant case goes even further by discouraging the very initiation of a libel action.[30] In reaching its decision, the Fifth Circuit could have relied upon an examination of

22. 365 F.2d at 571.

23. *Ibid.* Application of a federal interpretation of a state statute is correct when the interpretation given it by the state court infringes on constitutional rights. Arrowsmith v. United Press Int'l, 320 F.2d 219, 223 (2d Cir. 1963).

24. Elkhart Eng'r Corp. v. Dornier Werke, *supra* note 13, at 865.

25. 365 F.2d at 572.

26. NAACP v. Button, 371 U.S. 415 (1963) (Virginia statute regulating business solicitation by the legal profession); Grosjean v. American Press Co., 297 U.S. 233 (1936) (state taxation of non-resident newspaper corporations).

27. 365 F.2d at 573.

28. The majority felt that AP was as much an agent of defendant as one of its own reporters. *Id.* at 570.

29. *Id.* at 581.

30. Thus plaintiff loses the harrassment value of a libel action.

other factors typically considered in determining jurisdiction,[31] but instead it chose to make explicit the role of the first amendment in deciding the question.[32] The court may well have reached the correct result, since a literal application of the single contact rule often used in personal injury actions[33] would subject the publisher to long-arm jurisdiction upon the shipment into a state of a single newspaper. Applying the rule of the instant case, therefore, protects both the publisher, and the public's interest in reading critical expressions on the conduct of public officials.[34] In its zeal to protect first amendment rights, however, the court failed to articulate the answers to questions posed by the existence of significant competing values. Certainly at some point a public official should be allowed to sue a foreign newspaper corporation.[35] Since the court provided no guidance as to when such a point might be reached, however, a plaintiff with a meritorious cause of action may be denied access to a convenient tribunal. In addition, the court's reliance upon the first amendment presents the question of whether its decision is to be limited to suits involving public officials,[36] or whether the same considerations apply in every

31. For application of some of these factors, see McGee v. International Life Ins. Co., 355 U.S. 220, 223-24 (1957) (interest of the state in providing a forum for its residents and availability of witnesses and evidence); Travelers Health Ass'n v. Virginia, 339 U.S. 643, 647-49 (1950) (interest of the state in regulating the business involved and ease of access to an alternative forum); International Shoe Co. v. Washington, 326 U.S. 310, 319 (1945) (extent to which the cause of action arose out of defendant's local activities); Buckley v. New York Times Co., *supra* note 19, at 474-75 (character of the parties); Allied Finance Co. v. Prosser, 103 Ga. App. 538, 119 S.E.2d 813 (1961) (character of the parties).

32. To justify applying the first amendment to broaden due process requirements in libel actions, the court advanced a series of cases in which the Supreme Court had used the first amendment as a limitation on state power. Since the acquisition of jurisdiction over a non-resident is an exercise of power by the state, these cases may be at least analogous. See Hanson v. Denckla, *supra* note 12, at 251; Comment, 26 TENN. L. REV. 379 (1959).

33. See Gray v. American Radiator & Standard Sanitary Corp., *supra* note 14.

34. The instant court indicated that to hold otherwise would " 'freeze out of existence' the distribution on a limited basis of publications espousing unpopular positions . . . ." 365 F.2d at 573.

35. This follows logically from the *Sullivan* case itself, which would permit a public official to recover once the conduct and intent of the defendant dropped below a certain level.

36. It would seem that some of the reasons advanced in the opinion would lose their significance when applied to such a situation. The whole concept of liberality of expression provided by the *Sullivan* decision is based on the premise that the public should have the fullest information about their public officials. This problem is vividly illustrated in a statement by Judge Friendly, speaking for the Second Circuit in Buckley v. New York Post Corp., 35 U.S.L. WEEK 2427 (2d Cir. Jan. 10, 1967): "We cannot but wonder whether the Conner court would have felt the same way if the dramatis personae, instead of being 'Bull' Conner and a newspaper internationally known for its high standards, had been an esteemed local educator or clergyman and an out-of-state journal with a taste for seandal which had circulated 395 copies of a libel stating he had corrupted the morals of the young."

libel action against a foreign newspaper corporation.[37] It should be noted that subsequent to the instant decision, the Second Circuit, in *Buckley v. New York Post Corp.*,[38] rejected the contention that in a libel action the first amendment required greater contacts to satisfy due process. The court indicated that if publishers were to receive procedural protections in addition to substantive ones, these protections should not go to jurisdiction, "which must exist quite as much when . . . [the defendant] circulates a libel within the state as when he sends a leaking can of poison there . . . ."[39] Rather, the first amendment would be employed to decide if a state could exercise this jurisdiction in a particular case. It is submitted that a more logical approach would be to discard entirely the use of the first amendment in determining jurisdiction, and adopt an *International Shoe* approach.[40] It would seem that when the defendant has engaged in a reasonable amount of activity within the state, it should expect to accept the burdens of a lawsuit as an incident of doing business. Applying this test to the instant case, there is no reason why a newspaper should be treated any differently for jurisdictional purposes than any other business, particularly in light of the substantive protections already afforded newspapers under the case law.[41]

37. Additionally, the court seems to have failed to give sufficient consideration to whether it was necessary to apply the first amendment to strengthen the jurisdictional barriers to a libel suit, since the publisher has already the substantive protection of the *Sullivan* case. The single publication rule, adopted in a majority of states, prevides some added protection by treating the publication as complete when the publisher finishes and releases the publication. Thus there is no re-publication when it goes into another state. PROSSER, TORTS 788 (3d ed. 1964). New York has excluded non-resident publishers from the operation of its long-arm statute. N.Y. CIV. PRAC. § 302(a) (1963).

38. 35 U.S.L. WEEK 2427 (2d Cir. Jan. 10, 1967).

39. This appears to be a distinction without a difference. The Fifth Circuit would use the first amendment to expand the minimum contacts required by due process, while the Second Circuit would apply a uniform rule for contacts but would use the first amendment as a limitation of the exercise of this admitted jurisdiction. Both approaches arrive at the same result: the nature of the cause of action and the character of the parties cause the contacts necessary for jurisdiction to vacillate.

40. Increasing the contacts necessary for a public official to bring a libel action seems to create a presumption that the paper acted properly, and thus should not be faced with the task of defending a lawsuit, and that the plaintiff has really sustained no injury and thus should be denied access to court.

41. New York Times Co. v. Sullivan, 376 U.S. at 254; New York Times Co. v. Conner, 365 F.2d at 567 (decision on the merits).

Labor Law—Attorney Undertaking Persuader Activity on Behalf of Employer Must Report Such Activity Under LMRDA

Plaintiff attorneys engaged in various activities on behalf of employer clients designed to persuade employees not to unionize. The plaintiffs' activities included speaking to assembled groups of employees, interrogating them about their sympathies, and generally conducting anti-union campaigns for employers. The attorneys sought a declartory judgment in federal district court that they not be required to file reports of these "persuader activities" under the Labor-Management Reporting and Disclosure Act of 1959.[1] Plaintiffs conceded that they had engaged in persuader activities as defined in section 203(b) of the act, but contended that their activities were within the exceptions provided in sections 203(c) and 204. The Secretary of Labor counterclaimed to require the attorneys to file a section 203(b) report, contending that neither of the above sections exempted the attorneys from the act's reporting requirements. The district court rejected the Secretary's position and granted the plaintiffs' motion for summary judgment.[2] On appeal to the Court of Appeals for the Fifth Circuit,

1. 73 Stat. 519-46 (1959), 29 U.S.C. §§ 401-531 (1959). Pertinent portions of the LMRDA (popularly known as the Landrum-Griffin Act) are as follows:

Section 203:

"(b) Every person who pursuant to any agreement or arrangement with an employer undertakes activities where an object thereof is, directly or indirectly—

"(1) to persuade employees to exercise or not to exercise, or to persuade employees as to the manner of exercising, the right to organize and bargain collectively through representatives of their own choosing; or

"(2) to supply an employer with information concerning the activities of employees or a labor organization in connection with a labor dispute. . . .

"shall file within thirty days after entering into such agreement or arrangement a report with the Secretary . . . containing the name under which such person is engaged in doing business and the address of its principal office, and a detailed statement of the terms and conditions of such agreement or arrangement. Every such person shall file annually, with respect to each fiscal year during which payments were made as a result of such an agreement or arrangement, a report with the Secretary . . . containing a statement (A) of its receipts of any kind from employers on account of labor relations advice or services, designating the sources thereof, and (B) of its disbursements of any kind, in connection with such services and the purposes thereof. . . .

"(c) Nothing in this section shall be consrued to require any employer or any other person to file a report covering the services of such person by reason of his giving or agreeing to give advice to such employer or representing or agreeing to represent such employer before any court, administrative agency, or tribunal of arbitration or engaging or agreeing to engage in collective bargaining on behalf of such employer. . . ."

Section 204:

"Nothing contained in this Act shall be construed to require an attorney . . . to include in any report . . . any information which was lawfully communicated to such attorney by any of his clients in the course of a legitimate attorney-client relationship."

2. Fowler v. Wirtz, 236 F. Supp. 22 (S.D. Fla. 1964). Finding that the attorneys were at all times reprcsenting employers on legal matters within the attorney-client

held, reversed in part. Attorneys who undertake, on behalf of employers, to dissuade employees from joining a union must file a report required by section 203(b); but the reporting requirement does not extend to dealings with other labor clients for whom they have rendered no persuader services. *Wirtz v. Fowler,* 4 CCH LAB. L. REP. (54 CCH Lab. Cas.) ¶ 11514, at 17661 (5th Cir. Oct. 19, 1966).

Although the greatest significance of the Labor-Management Reporting and Disclosure Act of 1959 lies in its regulation of internal affairs of labor unions,[3] certain provisions of the act also regulate labor relations activities of employers and their consultants.[4] Section 203(b) requires labor relations consultants who undertake "persuader activities" on behalf of employer clients to report the arrangement to the Secretary of Labor within thirty days. The report must include a "detailed statement of the terms and conditions of such agreement or arrangement," and must specify the amount the consultant is receiving for such services, who is paying him, how much he is spending in connection with the services, and for what purposes it is being spent. In addition, section 203(b) requires that an annual report be submitted. Sections 203(c) and 204 enumerate the exceptions to the general reporting requirement. The mere giving of advice to an employer or the representation of an employer in an arbitration, administrative, or judicial proceeding need not be reported under section 203(c); and information protected by the attorney-client privilege is exempted under section 204.[5] In *Douglas v. Wirtz*[6] and *Price v. Wirtz,*[7] the attorneys conceded that they performed some reportable persuader activities under section 203(b), but argued that they were not re-

relationship and that the affected employees were apprised that the attorneys represented their employers, the district court concluded that the attorneys were "expressly exempted" from the reporting requirements because of the "explicit provisions" of § 203(c) and § 204.

3. Beaird, *Reporting Requirements For Employers and Labor Relations Consultants in the Labor-Management Reporting and Disclosure Act of 1959,* 53 GEO. L.J. 267 (1965).

4. The term "consultant" as used in the act includes all attorneys engaged in labor-relations work. A contrary interpretation of the term would render § 204 (which exempts an attorney from reporting matters within the attorney-client relationship) meaningless. Also, a proposed amendment which would have specifically excluded an attorney engaged in the practice of law from the reporting requirements was rejected. 105 CONG. REC. 6555-56 (1959).

5. A similar reporting provision of the Federal Lobbying Act of 1946, 60 Stat. 839 (1946), 2 U.S.C. § 261 (1958), was upheld as constitutional in United States v. Harriss, 347 U.S. 612 (1954). The instant court cited this case in rejecting the plaintiffs' contention that the act's reporting requirement voilated their freedom of speech. For a discussion of the lower court's decision in the instant case and its "inordinate concern" with free speech, see Comment, 40 N.Y.U.L. REV. 366 (1965).

6. 353 F.2d 30 (4th Cir.), *cert. denied,* 383 U.S. 909 (1966).

7. 51 CCH Lab. Cas. ¶ 33279 (N.D. Tex. 1965).

quired to file reports covering all labor relations services, both persuader and nonpersuader, rendered to all clients. In both cases it was held that once any persuader activity was performed, the attorneys were then required to report information about all labor relations services rendered to all clients for that annual reporting period.[8] Prior to the instant case, however, no court had considered the applicability of the 203(c) and 204 exclusionary sections to persuader activities clearly within section 203(b).

In the instant case, the court first addressed itself to the issue of whether the admitted[9] persuader activities of the plaintiffs were subject to the reporting requirements of section 203(b). The court dismissed the plaintiffs' contention that section 203(b) was not intended to apply to contemporaneously disclosed and open persuader activity.[10] After having determined that the plaintiffs' activities were clearly within the letter of section 203(b), the court turned to a consideration of the applicability of the exemptions provided in sections 203(c) and 204. The court first determined that the legislative history[11] of section 203(c) reflected Congress' view that persuader activity is readily distinguishable from other forms of labor relations services, and that this section was not intended to exempt activities clearly within the persuader classification. Turning next to section 204, the court again relied on legislative history to conclude that the section protected the employer-client relationship only against the disclosure of confidential information falling within the traditional bounds of the attorney-client privilege. Since the plaintiffs' admittedly open persuader activities could not be considered privileged,[12] the court found no barrier in section 204 to the disclosure of such information. Having found that the attorneys' persuader activities were not exempted by sections 203(c) or 204, the court then turned to the issue of whether the an-

8. The court in Douglas v. Wirtz, *supra* note 6, read the act to mean that the rendering of any non-exempted persuader services "triggered" the reporting requirement as to all labor services for all clients.

9. Plaintiffs' activities in question were conceded to be persuader activities for the purposes of reviewing the lower court's summary judgment.

10. 4 CCH LAB. L. REP. (54 CCH Lab. Cas.) ¶ 11514, at 17668. See S. REP. No. 187, 86th Cong., 1st Sess. 12 (1959); 99 CONG. REC. 5976 (1959).

11. 4 CCH LAB. L. REP. (54 CCH Lab. Cas.) ¶ 11514, at 17667. See 105 CONG. REC. 6558 (1959).

12. Consultants must report the name of their client, the receipts and disbursements pursuant to persuader arrangements and the general nature of their activities in behalf of these clients. *Supra* note 1. This information cannot be brought within the traditional common law privilege which attaches to certain confidential information communicated from client to attorney. 8 WIGMORE, EVIDENCE § 2313, at 609 (McNaughton rev. 1961). This is particularly true in the instant case in light of the plaintiffs' own assertion that they were performing their persuader activities openly.

nual report[13] had to include services performed for nonpersuader clients. The court unanimously agreed that the thirty-day reporting provision did not require reports as to nonpersuader clients, but split on the issue of whether the annual reporting provision required such reports.[14] The majority refused to follow the holdings in *Douglas v. Wirtz* and *Price v. Wirtz*, feeling that legislative history required a contrary decision. It was decided that the annual report need include only those agreements covered by the thirty-day report. Since the act clearly did not require the inclusion of information regarding nonpersuader clients in the thirty-day report, the majority concluded that nonpersuader services need not be reported in the annual report.[15]

The act clearly requires that all persuader activities must be reported, but there is no certainty as to whether any nonpersuader activity need be reported. The lack of conclusive congressional history and the lack of agreement among commentators[16] is reflected in the split between the two circuits that have now considered the issue. Interpreting the language of section 203(b) in light of its stated purposes,[17] it appears the act requires a reporting of nonpersuader ac-

13. Section 203(b) requires both a thirty-day report and an annual report. As explained in the text *infra*, one issue in the instant case concerns the construction of the annual reporting provision; the language of the thirty-day reporting provision quite clearly does not require reports as to all employers, and was not an issue here. See note 1 *supra*.

14. The dissenting member of the court would follow Douglas v. Wirtz, *supra* note 6, and hold that the performance of persuader activities requires an annual report of all labor relations advice and services rendered on behalf of all clients. For an argument supporting this view, see Loomis, *Employer and Consultant Reporting Requirements*, in SYMPOSIUM ON THE LABOR-MANAGEMENT REPORTING AND DISCLOSURE ACT OF 1959 391, 399 (Slovenko ed. 1961). The specific problem of statutory construction is whether the term "employers" found in § 203(b)(2)(A) refers back to the same class of employers indicated earlier in § 203(b)(2); or whether "employers" is a general term embracing all employers for whom labor relations activities were performed, without reference back to the persuader employers discussed earlier. Under the latter construction, the § 203(b)(2)(A) annual reporting provision applies to all employer-clients, including nonpersuader clients. See Comment, 40 N.Y.U.L. REV. 366, at 371 (1965).

15. Also, the majority felt that if one or more instances of persuader activity trigger the reporting requirement as to all labor relations activity on behalf of nonpersuader clients, the act would operate unduly harshly upon employer clients and upon attorneys who rendered ouly very few persuader services.

16. See Levy, *Comment*, in SYMPOSIUM ON THE LABOR-MANAGEMENT REPORTING AND DISCLOSURE ACT OF 1959 417 (Slovenko ed. 1961).

17. There are three purposes of the section as stated in the Senate committee report. The first is "to prevent, discourage, and make unprofitable improper conduct on the part of . . . employers, and their representatives by requiring reporting of arrangements, actions and interests which are questionable." S. REP. No. 187, *supra* note 10, at 12. The second is to enable employees to make objective evaluations of the diverse pressures being applied to them. *Id.* at 11. The third is to provide a sound factual basis for further legislative action if deemed necessary. *Id.* at 12, 26. While Congress considered surreptitious persuader activity improper conduct, it did not consider all persuader activity improper. However, since most persuader activity is "disruptive of harmonious labor relations, the committee believes . . . all should be reported." *Id.* at 12.

tivities performed for persuader clients[18] but this does necessitate reporting nonpersuader activities as to clients for whom no persuader activity was undertaken.[19] Substantially, this is the conclusion of the court in the instant case, but the opinion is unclear in regard to nonpersuader activities for persuader clients.[20] A problem certain to arise in future litigation under the act is that of distinguishing between "indirect persuasion" reportable under section 203(b) and "advice" exempted under section 203(c). For example, it is obvious that when a lawyer undertakes on behalf of an employer client to address the client's assembled employees and urges them not to unionize (as was done in the instant case), he is engaged in reportable activity. It becomes less obvious when the lawyer merely drafts a letter to be sent to the employees urging nonunionization, still less when a lawyer simply encourages the employer to draft his own letter while setting forth ideas as to its contents. Most of the activities in the instant case were clearly persuader, as they were in *Douglas* and *Price*, and the court did not have cause to consider the issue. Legislative history is inconclusive and affords no guidelines, but the problem may become a frequent one if the act's reporting requirements are stringently enforced by the Secretary of Labor.

18. This view gives meaning to the requirement in § 203(b)(2)(A) that the annual report contain a statement of "receipts of any kind from employers on account of labor relations advice or services . . . ." For the view that the term "employers" refers to the same employers mentioned earlier in the section (*i.e.*, those with whom persuader agreements were undertaken) see note 19 *infra*.

19. Such an interpretation necessarily presupposes that the term "employers" in § 203(b)(2)(A) refers to those employers who were mentioned earlier in the section (*i.e.*, those with whom persuader agreements were undertaken). Since nonpersuader activities were not questionable activities under the statute, and since it is not clear how disclosure of information as to nonpersuader clients would further the stated purposes of the provisions, it is submitted that there is no need to require reports of any attorney as to nonpersuader clients.

20. The instant court merely footnoted the proposition that nonpersuader activity undertaken in behalf of persuader clients must be reported.

Labor Law—Employer Must Bargain About an Economically Motivated Decision To Close a Portion of Its Operations

Ozark Trailers, Inc., was a member of a multi-corporate, integrated enterprise[1] primarily engaged in the manufacture, sale, and service of refrigerated truck bodies. In January of 1964,[2] Ozark's board of directors decided that economic considerations[3] required the termination of the operations of the Ozark plant. No notice of this was given the union, and no opportunity was afforded the union to bargain as to the decision to close or its consequent effects upon the employees. After closure, the manufacturing operations previously performed by Ozark were subcontracted to another company.[4] The union filed unfair labor practice charges, alleging violations of sections 8(a)(1),[5] 8(a)(3),[6] and 8(a)(5)[7] of the National Labor Relations Act. The Trial Examiner dismissed the 8(a)(3) charge but found Ozark's refusal to bargain with the union in regard to the decision and its

1. Ozark Trailers, Inc., a Missouri Corporation, was engaged in the business of manufacturing truck semi-trailers. Mobilefreeze Co. sold custom-built refrigerated truck bodies. Hutco Equipment Co. engaged in the sale, service, and repair of truck semi-trailers. Mobilefreeze was the principal source of materials for Ozark; Ozark, in turn, was engaged almost exclusively in the manufacture of truck bodies for Mobilefreeze. Hutco provided service and repair work for Mobilefreeze. Three individuals owned all the common stock of the three corporations, held all their offices, and comprised their boards of directors. These three jointly made the decision to terminate Ozark's operations.

2. On March 1, 1963, Local 770, Allied Industrial Workers, won a Board-conducted election held at the Ozark plant. This union was subsequently certified as the exclusive bargaining representative of the Ozark employees on March 11, 1963. The union and the company formulated a collective bargaining agreement, which was executed on April 16, 1963, for a term of one year. The decision to close the Ozark plant was made near the end of January 1964.

3. "[E]xcessive man hours were required for the production of custom refrigerated truck bodies; the truck bodies produced and sold would not perform properly because of defective workmanship, necessitating a return of the bodies to the plant at disastrous expense to Respondents; and the plant facilities were not efficiently laid out." Ozark Trailers, Inc., 63 L.R.R.M. 1264, 1268 (1966).

4. After the closure, Mobilefreeze contracted out the manufacture of refrigerated truck bodies, previously done by Ozark, to the Schodorf Body Company of Columbus, Ohio.

5. 49 Stat. 452 (1935), as amended, 29 U.S.C. § 158(a)(1) (1964): "It shall be an unfair labor practice for an employer—(1) to interfere with, restrain, or coerce employees in the exercise of their rights guaranted in § 7."

6. 49 Stat. 452 (1935), as amended, 29 U.S.C. § 158(a)(3) (1964): "It shall be an unfair labor practice for an employer—(3) by discrimination in regard to hire or tenure of employment or any term or condition of employment to encourage or discourage membership in any labor organization . . . ."

7. 49 Stat. 453 (1935), 29 U.S.C. § 158(a)(5) (1964): "It shall be an unfair labor practice for an employer—(5) to refuse to bargain collectively with the representatives of his employees . . . ."

attendant effects violative of sections 8(a)(1) and 8(a)(5). Upon recommendation to the NLRB, *held*, Trial Examiner's findings of unfair labor practices adopted.[8] The employer's economically motivated decision to terminate a portion of its operations and the subsequent effect of this decision upon the employees are mandatory subjects of collective bargaining within the meaning of section 8(a)(5) of the NLRA. *Ozark Trailers, Inc.*, 63 L.R.R.M. 1264 (N.L.R.B. 1966).

Section 8(a)(5) of the NLRA provides that it shall be an unfair labor practice for an employer "to refuse to bargain collectively with the representatives of his employees. . . ."[9] Section 8(d) defines collective bargaining as "the performance of the mutual obligation of the employer and the . . . union to meet . . . and confer in good faith with respect to wages, hours, and other terms and conditions of employment. . . ."[10] While court decisions[11] have established that the phrase "other terms and conditions of employment" is to be given a broad construction, the issue of whether economically motivated operational changes are within the ambit of this phrase has not been clearly resolved. This basic question may be subdivided into the employer's duty to bargain about the effects of an operational change upon employees and the duty to bargain about the actual decisions to make such a change. As to the first of these, the Board and the courts have concluded that the impact upon employee rights resulting from an operational change is indeed a mandatory subject of collective bargaining, and that the employer must negotiate such issues as severance pay, seniority, and pension rights. This was clearly stated in *NLRB v. Rapid Bindery, Inc.*,[12] and is based upon the proposition that a curtailment of work directly affects "conditions of employment."[13] Although *Rapid Bindery* specifically settled the first problem, it has proved much more difficult to resolve whether the employer is obligated to bargain about the actual decision to make an operational change. Beginning in 1962 with *Town & Country Mfg. Co.*,[14] the

8. For the full text of the Board's order, see 63 L.R.R.M. 1264, 1270 (1966).

9. 49 State. 453 (1935), 29 U.S.C. § 158(a)(5) (1964).

10. 61 Stat. 142 (1947), 29 U.S.C. § 158(d) (1964).

11. See, *e.g.*, Inland Steel Co. v. NLRB, 170 F.2d 247 (7th Cir. 1948).

12. "[O]nce that decision [to make an operational change] was made, § 8(a)(5) requires that notice be given to the union so that the negotiators could then consider the treatment due to those employees whose conditions of employment would be radically changed by the move." NLRB v. Rapid Bindery, Inc., 293 F.2d 170, 176 (2d Cir. 1961).

13. *Ibid.*

14. 136 N.L.R.B. 1022 (1962), *enforced*, 316 F.2d 846 (5th Cir. 1963). The employer subcontracted his hauling operations to deliver trailers to customers. This was done shortly after the employer learned of the drivers' interest in the union. The Board found that the decision was based on discriminatory motives and therefore violative of §§ 8(a)(3) and 8(a)(5). In a significant dictum the Board announced

Board established its position that an employer must bargain about a decision to subcontract a part of his operations, despite legitimate economic motivation. The focal point of the decision was that since the decision to subcontract resulted in the elimination of jobs, "conditions of employment" were substantially affected.[15] Despite the Board's consistent application of the *Town & Country* rule, the courts which have considered the question have limited the scope of this doctrine.[16] In the leading case of *Fibreboard Paper Prods. Corp. v. NLRB*,[17] the Supreme Court held that the obligation to bargain included bargaining about the decision to subcontract, but limited its holding to situations where the employer had replaced existing employees with those of an independent contractor to do the same work under similar conditions of employment. Furthermore, the Court noted that: "the Company's decision to contract out the . . . work did not alter the Company's basic operation. The . . . work still had to be performed in the plant. No capital investment was contemplated. . . ."[18] In a significant concurring opinion, Justice Stewart asserted that the type of subcontracting presented in the case fell short of such larger entrepreneurial decisions as determining the goods to be produced, the investment of capital, and the scope of the enterprise. Such decisions, he maintained, do not primarily concern conditions of employment, even though the effect of such decisions bear an incidental relation to employment security. Attempting to delineate the scope of *Fibreboard*, the Eighth Circuit in *Adams Dairy*[19] and the

that even if the employer subcontracted his operations for purely economic (and thus nondiscriminatory) motives, he was still required by § 8(a)(5) to bargain with the union over his decision to subcontract.

15. "[T]he elimination of unit jobs, albeit for economic reasons, is a matter within the . . . meaning of Section 8(a)(5) of the Act." *Id.* at 1027. See Bart & Kingston *The Specter of Darlington—Restrictions on an Employer's Right to Make a Change in His Business Operations*, 8 B. C. IND. & COMM. L. REV. 55, 57-64 (1966).

16. Royal Plating & Polishing Co., 148 N.L.R.B. 545 (1964), *remanded*, 350 F.2d 191 (3d Cir. 1965), *aff'd on remand*, 152 N.L.R.B. 619 (1965); Hawaii Meat Co., 139 N.L.R.B. 966 (1962), *enforcement denied*, 321 F.2d 397 (9th Cir. 1963); Adams Dairy, Inc., 137 N.L.R.B. 815 (1962), *modified and enforced in part*, 322 F.2d 553 (8th Cir. 1963), *vacated and remanded*, 379 U.S. 644 (1965), *modified*, 350 F.2d 108 (8th Cir. 1965), *cert. denied*, 382 U.S. 1011 (1966).

17. 130 N.L.R.B. 1558 (1961), *rev'd on rehearing*, 138 N.L.R.B. 550 (1962), *enforced*, 322 F.2d 411 (D.C. Cir. 1963), *aff'd*, 379 U.S. 203 (1964).

18. 379 U.S. at 213.

19. NLRB v. Adams Dairy, Inc., 350 F.2d 108 (8th Cir. 1965). The dairy decided to liquidate the part of its business which handled the distribution of its milk products and to distribute its products through independent contractors. The Board held that the employer was required by § 8(a)(5) to bargain about the decision. On appeal, the Eighth Circuit held that the dairy's decision to subcontract was not a mandatory subject of collective bargaining. The court concluded that the case was factually distinguishable from *Fibreboard* in that a basic operational change was involved, that the work was not performed in the Adams plant, and that there was a partial liquidation and recoup of capital investment.

Third Circuit in *Royal Plating*[20] recently rejected the Board's reliance on *Town & Country*. In these two decisions the courts held that section 8(a)(5) does not proscribe unilateral operational changes which effect "a major change in the economic direction of the company;"[21] or which involve "a management decision to recommit and reinvest funds in the business,"[22] or which result in a "partial liquidation and a recoup of capital investment."[23]

The Board in the instant case initially determined that the respondent constituted a single employer within the meaning of the NLRA, and that, therefore, the closing was a partial, rather than a complete, termination of operations.[24] The Board then considered the question of whether the employer was obligated to bargain the effects of the partial closure upon the employees and cited *Rapid Bindery* in holding that the employer did have such a duty. In considering whether the decision to close was itself a mandatory bargaining subject, the Board reviewed the decisions in *Fibreboard, Adams Dairy*, and *Royal Plating* and determined that the rationale of *Fibreboard* did not compel the limitations imposed by the two circuit courts. In support of this conclusion, the Board reasoned that since the Supreme Court in *Fibreboard* had regarded the termination of unit jobs as significantly affecting "conditions of employment," an employer's decision to close a part of its operations should not be exempt from the requirement to bargain solely because the decision also concerned the employer's investment structure.[25]

20. NLRB v. Royal Plating & Polishing Co., 350 F.2d 191 (3d Cir. 1965). The employer decided to sell a plant and liquidate. No opportunity was given the union to bargain about this decision. The Board concluded that the employer's conduct resulted in an 8(a)(5) refusal to bargain over the closing of the plant. The Third Circuit, however, took the contrary view that the employer was not obligated to bargain over the decision. The court distinguished *Fibreboard* in noting that the instant situation involved a managerial decision to recommit and reinvest funds in the enterprise and a major change in the economic direction of the company.

21. *Id.* at 196.

22. *Ibid.*

23. NLRB v. Adams Dairy, Inc., *supra* note 19, at 111.

24. Regarding the closing as only a partial termination, the Board concluded that the *Darlington* principle was not determinative of the issues presented. See Textile Workers Union v. Darlington Mfg. Co., 380 U.S. 263 (1965), where it was held that an employer's decision to close its plant due to unionization is not an unfair labor practice when the employer goes completely out of business and the sale of the corporation's plant is entire, bona fide, and irrevocable.

25. "[W]e do not believe that the question whether a particular management decision must be bargained about should turn on whether the decision involves the commitment of investment capital, or on whether it may be characterized as involving 'major' or 'basic' change in the nature of the employer's business. True it is that decisions of this nature are, by definition, of significance for the employer. It is equally true, however . . . that an employer's decision to make a 'major' change in the nature of his business . . . is also of siguificanee for those employees whose jobs

Analytically, the Board's reasoning in the instant case is compelling. Since a partial closure necessarily involves a loss of jobs and erosion of seniority rights, there is a direct and legitimate employee interest in the decision. Moreover, it is irrelevant to this interest that the decision also involves an alteration in the investment structure of the company or a basic change in the employer's business. However, in emphasizing only employee rights, the Board has adopted an approach which seems inappropriate for meeting the essential problem: how to accommodate the conflicting interests of labor and management so as to assure the protection of employee rights, while preserving the management flexibility and initiative essential to efficient and economic operation. Proper resolution of this delicate problem requires both a realistic appraisal of the practical considerations and a balancing of the competing interests and policies involved. However, the Board's decision succeeds only in securing the interests of the employees at the expense of management's freedom to exercise its entrepreneurial discretion. The requirement that each managerial decision affecting "conditions of employment" be submitted to the collective bargaining process would indeed be an intrusion into a province reserved for employer discretion and would constitute a significant restraint upon the exercise of management flexibility. A more appropriate reconciliation of the conflicting employer-employee interests would require bargaining only as to the effects of an economically motivated partial closure and thus limit the negotiations to such issues as severance pay, seniority, and pension rights.[26] This compromise would serve as a more adequate resolution of the essential problem since it would assure management flexibility while still affording a meaningful measure of protection to the rights of the employees whose interests are affected by the decision.

will be lost by the termination. . . . [T]he employee has invested years of his working life, accumulating seniority, accruing pension rights, and developing skills . . . ." 63 L.R.R.M. 1264, 1267 (1966).

26. This view is suggested by the implications of the concurring opinion in *Fibreboard, supra* note 17, and by the recent decisions in *Adams Dairy, supra* note 16, and *Royal Plating, supra* note 16.

Labor Law—Employer's Duty To Bargain When Authorization Cards Are Presented Within Twelve Months of a Prior Valid Election

Nine months after losing a representation election, the Retail Clerks Employees Union presented authorization cards from a majority of the employees of the Great Scott Supermarket and demanded recognition from the employer as the exclusive bargaining representative of his employees. Upon the employer's refusal to bargain, the union filed unfair labor practice charges with the National Labor Relations Board, claiming the employer had violated section 8(a)(5)[1] of the National Labor Relations Act.[2] Since a valid election had been conducted nine months prior to the union's demand for recognition, the employer contended that his duty to bargain was eliminated by section 9(c)(3)[3] of the act, which permits only one valid election to be held in any twelve-month period. The Board held that the employer's refusal to bargain constituted a violation of section 8(a)(5) of the act and issued an order to bargain.[4] On appeal, the Court of Appeals for the Seventh Circuit, *held*, enforced. Where a union demands recognition on the basis of authorization cards signed by a majority of the employees in the bargaining unit, the employer has a duty to bargain under section 8(a)(5) of the NLRA regardless of a prior valid election within the preceeding twelve-months. *Conren, Inc. v. NLRB*, 368 F.2d 173 (7th Cir. 1966).

Prior to the enactment of the Tart-Hartley amendments to the NLRA, a union which had lost a representation election could petition the Board for another election at any time upon a showing of substantial employee support.[5] On the other hand, in the absence of unusual circumstances,[6] a union which had been certified on the basis of a Board election could not have its majority status challenged

1. Section 8(a)(5) provides: "It shall be an unfair labor practice for an employer to refuse to bargain collectively with the representatives of his employees, subject to the provisions of section 9(a)." 61 Stat. 141 (1947), 29 U.S.C. § 158(a)(5) (1964).

2. The Board also found violations of sections 8(a)(1),(2) and (3) as alleged by the union. The court of appeals affirmed these conclusions on the ground that there was substantial evidence to support the Board's findings.

3. In pertinent part section 9(c)(3) provides: "No election shall be directed in any bargaining unit or any subdivision within which, in the precedng twelve-month period, a valid election shall have been held." 61 Stat. 144 (1947), 29 U.S.C. § 159(c)(3) (1964).

4. Conren, Iuc., 61 L.R.R.M. 1090 (1966).

5. *E.g.*, American Tri-State Paper Box Co., 63 N.L.R.B. 126 (1945) (election directed upon presentation of authorization cards 8 months after prior election); Carolina Panel Co., 62 N.L.R.B. 418 (1945).

6. Century Oxford Mfg. Co., 47 N.L.R.B. 835 (1943). See also Neary, *The Union's Loss of Majority Status and the Employer's Obligation to Bargain*, 36 TEXAS L. REV. 878 (1958).

by another election for a reasonable time after the date of its certification,[7] generally a year.[8] An employer who refused to bargain with such a union within the certification year committed an unfair labor practice, even though the union had lost its majority status during that time.[9] By adopting this certification-year rule, the Board attempted to balance the NLRA's policy of promoting industrial stability through collective bargaining with its equally important policy of guaranteeing the freedom of choice to employees.[10] However, in cases of unusual circumstances, such as where a newly certified union had become defunct,[11] or where a schism had occurred,[12] an exception was made allowing the employees to exercise their freedom of choice in another election during the certification year.[13] After the enactment of the Taft-Hartley amendments, which incorporated section 9(c)(3) into the act, the Board continued to apply its certification-year rule.[14] Even though the Board has stated that the validity of the certification-year rule does not depend upon the statutory provision of section 9(c)(3),[15] that section has placed two pertinent limitations upon the Board's previous practices. Where a union loses an election, another election cannot be held in the same unit within a twelve-month period.[16] Also, in cases involving unusual circumstances, the harsh effects of the Board's certification-year rule can no longer be remedied

7. This rule which made the date of the certification the beginning of the certification year rather than the date of the election was given approval in Brooks v. NLRB, 348 U.S. 96 (1954).

8. After the enactment of the Taft-Hartley amendments, the Board held that in all cases a reasonable time would be one year from the date of certification. Lift Trucks, Inc., 75 N.L.R.B. 998 (1948).

9. Century Oxford Mfg. Co., *supra* note 6. In Celanese Corp. of America, 95 N.L.R.B. 664, 672 (1951), the Board defined its certification-year rule. In the absence of unusual circumstances, there exists an irrebuttable presumption that a union maintains its majority status for a period of one year from the date of its certification. After a year, the presumption of majority status still exists, but it is rebuttable by the employer. For the interrelation of this rule with the Board's contract bar rules see Neary, *supra* note 6.

10. Century Oxford Mfg. Co., *supra* note 6; Neary, *supra* note 6.

11. Public Service Elec. & Gas Co., 59 N.L.R.B. 325 (1944) (NLRA purposes defeated if election bar applied when certified union defunct).

12. Brightwater Paper Co., 54 N.L.R.B. 1102 (1944) (certification-year rule no bar where schism occurs).

13. Subsequent elections were also granted where the size of the bargaining unit had changed substantially during the certification year. Electric Sprayit Co., 67 N.L.R.B. 780 (1946).

14. Mar-Jac Poultry Co., 136 N.L.R.B. 785 (1962) (union granted one year of bargaining from date of settlement agreement); John Vilicich, 133 N.L.R.B. 238 (1961).

15. Ecko Products Co., 117 N.L.R.B. 137 (1957) (certification-year rule within Board's administrative discretion). See also Brooks v. NLRB, *supra* note 6.

16. American Bridge Division, United States Steel Corp., 61 L.R.R.M. 1237 (1966) (§ 9(c)(3) prohibits more than one election per year either for certification or decertification). However, the first election must be valid before a subsequent election will be prohibited. NLRB v. Blades Mfg. Co., 344 F.2d 998 (8th Cir. 1965).

by a subsequent election during the election-year.[17] However, in *Rocky Mountain Phosphates, Inc.*,[18] where the previously elected union had become defunct, the election prohibition of section 9(c)(3) was held not to apply to other less formal means of selecting a new collective bargaining representative. The Board held that the outside union's presentation of authorization cards from a majority of the employees in the unit placed the employer under a duty to bargain, regardless of the fact that a valid election had been held in the same unit within the preceding twelve-month period.[19] The Board reasoned that neither the legislative history[20] nor the language of section 9(c)(3) could be interpreted as precluding anything other than a second election within twelve months of a prior valid election.[21] This interpretation, viewed in conjunction with a 1956 Supreme Court decision[22] which noted that recognition could be gained by means other than an election, made it clear to the Board that section 9(c)(3) did not preclude a union, in cases of unusual circumstances, from gaining representative status on the basis of authorization cards submitted during the election year.

In the instant case, the court found that the language and legislative history of section 9(c)(3) clearly indicated congressional awareness of means other than an election by which bargaining representatives could be chosen. By limiting the applicability of section 9(c)(3) to cases involving elections, Congress had therefore tacitly sanctioned the establishment of the union's majority status within the election

17. Brooks v. NLRB, *supra* note 7. The Court stated that the remedy of the employer or the employees in such situations is with the Board and until such a remedy can be obtained, the employer is under a duty to bargain in good faith with the certified union.

18. 138 N.L.R.B. 292 (1962).

19. *Accord*, Majestic Lamp Mfg. Corp., 143 N.L.R.B. 180, 186 (1963) (prohibition of § 9(c)(3) does not affect the "vitality of section 7 and sections 8 (a)(1) and (5) and other sections"); Ecko Products Co., *supra* note 15 (§ 9(c)(3) does not accord employer a one-year period of "quiet enjoyment").

20. The legislative history of this section is of little assistance in determining its intended scope. "Section 9(c)(3): This Amendment prevents the Board from holding elections more often than once a year in any given bargaining unit unless the results of the first election are inconclusive by reason of none of the competing unions having received a majority. At present, if the union loses, it may on presentation of additional membership cards secure another election within a short time, but if it wins its majority cannot be challenged for a year." S. REP. No. 105, 80th Cong., 1st Sess. 25 (1947).

21. Compare the reasoning of the trial examiners in Strydel, Inc., 156 N.L.R.B. No. 114, 61 L.R.R.M. 1230 (1966), and Dow Chemical Co., 152 N.L.R.B. 1150, 1965 CCH LAB. L. REP. T390. The Board did not adopt either examiner's view of the applicability of section 9(c)(3), but disposed of the cases without reaching the section 9(c)(3) questions.

22. United Mine Workers v. Arkansas Oak Flooring Co., 351 U.S. 62, 70-72 (1956) (that union was not eligible under §§ 9(f),(g), and (h) for certification was no defense to refusal to bargain charge since union had a majority).

year by such other means as authorization cards. Thus, the court concluded that the employer's refusal to bargain with the representative established by the authorization cards violated section 8(a)(5) of the act. In his dissenting opinion, Judge Kiley contended that informal methods of selecting a bargaining representative have been found to be unreliable due to the sensitive situation that prevails shortly after an election. Thus, he urged that the maintenance of industrial peace and the protection of the employees' freedom of choice required that the result of a prior election be given priority over authorization cards obtained shortly thereafter.

The *Conren* court has extended judicial approval of the Board's policy of permitting authorization cards to be used as the basis of an order to bargain pursuant to section 8(a)(5) of the act. Previously, the Board held that an order to bargain could be issued on the basis of a majority of authorization cards presented prior to a lost election.[23] According to the doctrine of this earlier case, if the employer engages in unfair labor practices during the period between a demand for recognition and the election, a presumption may be established that the employer's initial refusal to bargain was made in bad faith as an attempt to undermine the union's majority. If the employer fails to rebut this presumption, an order to bargain will issue.[24] The instant case now permits a union to seek an order to bargain on the basis of authorization cards presented within one year *after* a valid election, even though the employer has not engaged in unfair labor practices prior to this election. If an employer has a good faith doubt of the union's majority status as shown by authorization cards presented within twelve months of a prior valid election, he is prevented by section 9(c)(3) from resolving his doubt by insisting on a subsequent election and is thus placed in the dilemma of risking a violation of section 8(a)(5) by refusing to bargain or bargaining regardless of his good faith doubt. His situation is made more difficult by the doubtful reliability of the use of authorization cards[25] and the

23. Bernel Foam Products Co., 146 N.L.R.B. 1277 (1964).

24. Drug King, Inc., 61 L.R.R.M. 1359 (1966). To give rise to the presumption of bad faith, the employer's unfair labor practice must be of a substantial nature. Duther, Inc., 61 L.R.R.M. 1305 (1966). See also Randall, *The NLRB's New Policy on Bargaining Orders Following Representation Elections*, 52 A.B.A.J. 1038 (1966); Shuman, *Requiring a Union to Demonstrate Its Majority Status By Means of an Election Becomes Riskier*, 16 LAB. L.J. 426 (1965); Note, *Refusal-to-Recognize Charges Under Section 8(a)(5) of the NLRA: Card Checks and Employee Free Choice*, 33 U. CHI. L. REV. 387 (1966); Note, *Union Authorization Cards*, 75 YALE L.J. 805 (1966).

25. The reliability of using authorization cards to reflect the employee's choice has been a subject of much doubt. The open solicitation of such cards presents many opportunities for coercion and misunderstanding. Employees may be subjected to "bandwagon" psychology and other conditions which prevent them from making an en-

Board's liberal policy in validating these cards.[26] Aside from its practical difficulties, this decision also presents a questionable interpretation of section 9(c)(3) of the act. Congress has attempted in section 9(c)(3) to promote industrial peace by preventing the "constant stirring up of excitement by continual elections";[27] and to accomplish this purpose, Congress has chosen to require twelve months between elections. This time period was also used when section 8(b)(7)(B),[28] which prevents recognitional or organizational picketing by a union within a year of a prior election, was added to the act. Thus, there appears to be a congressional policy to promote industrial peace and protect the freedom of choice of the employees by requiring the expiration of a particular period of time after a valid election before another opportunity to select a bargaining representative is offered employees. The use of authorization cards within twelve months of a prior election conflicts with this policy as much as a subsequent election since both methods may lead to industrial unrest and jeopardize the employees' freedom of choice.

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lightened choice. Thus, this method of designating a representative does not afford the employee the privacy and freedom of the secret ballot in making his choice. Viewing these inherent defects in conjunction with the Board's liberal view in validating these cards, as expressed in Cumberland Shoe Corp., 144 N.L.R.B. 1268 (1963), many of the doubts may be well founded. See, *e.g.*, Lewis, *The Use and Abuse of Authorization Cards in Determining Union Majority*, 16 LAB. L.J. 434 (1965); Note, *Refusal-to-Recognize Charges Under Section 8(a)(5) of the NLRA: Card Checks and Employee Free Choice*, *supra* note 24.

26. See Cumberland Shoe Corp., *supra* note 25 (use of same authorization cards for election and designation of representatives).

27. Statement by Senator Taft, 93 CONG. REC. 3838 (1947).

28. 73 Stat. 544 (1959), 29 U.S.C. § 158(b)(7)(B) (1964).

Taxation—Computation of Corporate Earnings and Profits—Cash Basis Corporation Cannot Deduct Federal Taxes Due but Yet Unpaid

In 1959, total rental payments of 132,592.57 dollars were received by petitioner's real estate corporation and an "experimental department," an organization solely owned and controlled by petitioner.[1] Neither the real estate corporation nor the petitioner reported such amounts in their 1959 return. Respondent asserted a deficiency for the total amount, claiming that all sums received by the department and the real estate corporation were received by petitioner as a constructive dividend and therefore taxable to him as ordinary income. Taxpayer contended that 1959 current year's earnings and profits must be reduced by the amount of corporate income tax due in order to determine the amount actually received by him as a dividend.[2] Respondent argued that since the real estate corporation was a cash basis taxpayer it could not reduce current year's earnings and profits by income taxes paid in subsequent years. *Held*, judgment for respondent. A cash basis corporation cannot deduct federal taxes due but not yet paid in computing current year's earnings and profits. *Joseph B. Ferguson*, 47 T.C. 11 (1966).

Although the law is fairly well settled that an accrual basis corporation may reduce current year's earnings and profits by the amount of federal taxes due but not yet paid,[3] and may even deduct the amount of a contested tax liability[4] or a subsequently determined deficiency,[5]

1. Petitioner owned an automobile dealership and all the stock of a corporation which owned certain real estate used in the automobile business. Petitioner sold his automobile business to "Enterprises," a corporation owned by unrelated persons, under an agreement requiring Enterprises to pay a minimum of $75,000 annually to petitioner's real estate corporation with any excess up to 3% of Enterprises' gross sales to be paid to an "experimental department." The Tax Court found that the "experimental department" was solely owned and controlled by petitioner on the basis of his complete control and discretion over the use of department funds and the fact that he could terminate the department at will and receive all its assets. The owners of Enterprises also testified that they considered the so-called department as in substance owned by petitioner and the percentage of gross sales payments as rent.

2. Petitioner argued alternatively that the real estate corporation was an accrual basis taxpayer but that even if it was a cash basis taxpayer 1959 earnings and profits should still be reduced by 1959 taxes. The court determined that the real estate corporation was in fact a cash basis taxpayer.

3. *E.g.*, Fawcus Mach. Co. v. United States, 282 U.S. 375, 378 (1931); United States v. Anderson, 269 U.S. 422, 441 (1926).

4. *E.g.*, Stern Bros. & Co., 16 T.C. 295 (1951), *acq.*, 1951-2 CUM. BULL. 4.

5. Estate of Esther M. Stein, 25 T.C. 940 (1956), *acq.*, 1957-1 CUM. BULL. 5, 1957-2 CUM. BULL. 7 (taxpayer allowed to reduce earnings and profits by the subsequently determined deficiency and the 50% fraud additions). The Commissioner has adopted *Stein*, Rev. Rul. 57-332, 1957-2 CUM. BULL. 231, revoking Rev. Rul. 107, 1953-1 CUM. BULL. 178. *But see* Bernstein v. United States, 234 F.2d 475, 482 (5th Cir. 1956) (dictum, criticizing *Stein*).

the cases dealing with cash basis corporations are in conflict. The Commissioner has long asserted that a cash basis corporation cannot deduct federal taxes in determining current year's earnings and profits.[6] However, the first case to consider this issue held that a cash basis corporation could deduct the tentative tax liability in determining the amount of earnings available for distribution of dividends.[7] The Board of Tax Appeals followed this decision in *M. H. Alworth Trust*,[8] reasoning that the purpose of the rule allowing dividends to be distributed only out of earnings and profits was to prevent impairment of capital and that "to permit the distribution of gross earnings and profits without making allowance for outstanding obligations would leave such obligations as a charge on capital regardless of the method by which the corporation keeps its books and reports its income."[9] The Board noted that earnings and profits have never been computed in the same manner as gross income and concluded that there was nothing in the statute to indicate that Congress intended to depart from the commonly accepted meaning given to earnings and profits under general corporation law.[10] The Eighth Circuit reversed the Board[11] stating that the Board's decision amounted to a limitation on the statute[12] to the effect that taxable dividends could arise only if there were earnings and profits remaining after deducting federal taxes for that year; it concluded that such a limitation was not intended by Congress. This decision was subsequently followed without question by the Tax Court.[13] The Sixth Circuit, however, took the opposite view in *Drybrough v. Commissioner*.[14] There the court stated that "whether

6. G. C. M. 2951, VII-1 CUM. BULL. 160 (1928). The Commissioner's assertion is based upon Treas. Reg. § 1.312-6(a) (1955): "Earnings and Profits. (a) . . . the amount of earnings and profits in any case will be dependent upon the method of accounting properly employed in computing taxable income . . . . For instance, *a corporation keeping its books and filing its income tax returns . . . on the cash receipts and disbursements basis may not use the accrual basis in determining earnings and profits . . . .*" (Emphasis added.)

7. Hadden v. Commissioner, 49 F.2d 709 (2d Cir. 1931).

8. 46 B.T.A. 1045 (1942), *rev'd*, 136 F.2d 812 (8th Cir.), *cert. denied*, 320 U.S. 784 (1943).

9. 46 B.T.A. at 1047.

10. *M. H. Alworth* was followed in John H. Wheeler, 1 T.C. 640 (1943), *rev'd*, 143 F.2d 162 (9th Cir. 1944) (without discussion of this issue), *rev'd*, 324 U.S. 542 (1945) (without discussion of this issue). It should be noted that *Wheeler* was decided while *Alworth* was pending appeal in the Eighth Circuit.

11. Helvering v. Alworth, 136 F.2d 812 (8th Cir. 1943). The court refuted the Board's reliance on general corporate law concepts stating that the statute does not refer to the power of a corporation to distribute its earnings to shareholders, but relates only to what must be included in the shareholder's gross income.

12. INT. REV. CODE OF 1939, § 115(a) (now INT. REV. CODE OF 1954, § 316(a)).

13. United Mercantile Agencies, 23 T.C. 1105 (1955), *rev'd sub nom.*, Drybrough v. Commissioner, 238 F.2d 735 (6th Cir. 1956); Paulina duPont Dean, 9 T.C. 256 (1947).

14. 238 F.2d 735, 32 NOTRE DAME LAW. 739 (1957).

a corporation keeps its accounts and makes its returns on the cash or accrual basis is a question generally relevant only in determining its own income and deductions as a taxpayer," but not in computing earnings and profits.[15] The court adopted the reasoning of the Board's opinion in *Alworth* and concluded that to hold otherwise would constitute a tax on the distribution of capital.[16] *Drybrough* was subsequently followed in three jurisdictions,[17] including the Tax Court[18] and the Eighth Circuit.[19] However, just when it appeared that all the courts were finally in agreement on this issue, the Tax Court again reversed its position and in *Newark Amusement Corp.*[20] specifically followed the Eighth Circuit's decision in *Alworth.* The most recent case to consider the issue was *Demmon v. United States,*[21] which introduced a new argument as to why cash basis corporations should be allowed to deduct accrued but unpaid taxes from earnings and profits. The court quoted Internal Revenue Code section 316(a)[22] and stated that this

15. 238 F.2d at 738.

16. The court concluded that "both common sense and realism require the conclusion that corporate taxes . . . should be excluded from the corporation's earnings and profits under the circumstances of this case." 238 F.2d at 740. The court also allowed the fraud additions to be deducted.

17. Demmon v. United States, 321 F.2d 203 (7th Cir. 1963), 5 B.C. IND. & COM. L. REV. 470 (1963); Simon v. Commissioner, 248 F.2d 869 (8th Cir. 1957), *reversing* United States Packing Co., 24 P-H Tax Ct. Mem. 653 (1955); Thompson v. United States, 214 F. Supp. 97 (N.D. Ohio 1962); Robert L. Bender, 16 CCH Tax Ct. Mem. 502, 518 (1957).

18. Robert L. Bender, *supra* note 17. Although the Tax Court followed *Drybrough* and *Stein* in allowing deduction of a subsequently determined deficiency and fraud additions, the court did not indicate what method of accounting the corporation was using. *Thompson v. United States* notes this fact in citing *Bender* but states that "the long discussion does appear to indicate that it was on a cash basis." *Supra* note 17, at 100. Also, the type of business (taxicab and limousine service) and the fact that the principal shareholder-officer kept cash receipts books would indicate cash basis.

19. Simon v. Commissioner, *supra* note 17. The court did not mention *Alworth* but specifically followed *Drybrough* in holding that a cash basis corporation could deduct fraud additions.

20. 19 CCH Tax Ct. Mem. 705 (1960).

21. *Supra* note 17. In *Demmon* the Commissioner relied upon the following language in Commissioner v. South Texas Lumber Co., 333 U.S. 496, 501 (1948), upholding the validity and reasonableness of what is now Treas. Reg. 1-312(6)(a) (1955): "This regulation is in harmony with the long-established congressional policy that a taxpayer generally cannot compute income taxes by reporting annual income on a cash basis and deductions on an accrual basis." However, the *Demmon* court distinguished *South Texas Lumber Co.* stating that that case pertained to computation of the corporate income taxes while *Demmon* and similar cases deal only with the computation of earnings and profits. Demmon v. United States, *supra* note 17, at 206. This narrow construction of *South Texas Lumber Co.* has been criticized. Gardner, *The Tax Consequences of Shareholder Diversions in Close Corporations,* 21 TAX L. REV. 223, 249 n.99 (1966).

22. INT. REV. CODE OF 1954, § 316(a): "Dividend Defined. . . . any distribution made by a corporation . . . out of its earnings and profits of the taxable year (*computed as of* the close of the taxable year . . .)". (Emphasis added.)

statute requires all corporations to compute earnings and profits as of one time regardless of their method of accounting.[23]

In the instant case the Tax Court conceded that current year's earnings and profits are not necessarily synonymous with taxable income[24] and that "there is no statute or inescapable rule of logic which *requires* strict adherence to the cash basis for earnings and profits purposes."[25] Nevertheless, the court reasoned, the provisions of Treasury Regulation 1.312-6(a) do establish this requirement. Since the regulation has a "sound basis in administrative policy," and since there are no persuasive reasons for departing from the cash basis method for purposes of computing earnings and profits, the regulation should not be ignored.[26]

The Tax Court in the instant case has firmly committed itself to a position contrary to that taken by the majority of the federal courts which have considered this issue.[27] The opinion is subject to the same basic deficiency found in nearly every decision rendered since the Board's decision in *Alworth,* that is, it states the desired conclusion without advancing adequate reasons or analysis in support. A major reason for the present dilemma is that neither the statute, the regulations nor the court decisions give a comprehensive definition of "earnings and profits," thereby placing the burden on the individual taxpayer to determine, often at his peril, the composition of earnings and

23. "These words must mean that all corporations whether cash, accrual or hybrid, compute earnings and profits *as of one time*—the close of the taxable year. Such words imply accrual—'as of' means tax relating to the year, and not tax incidentally paid during the year involved for some previous year or years." Demmon v. United States, *supra* note 17, at 206. The court did not expand on this argument, and as a result this statement has been criticized for stating a conclusion without an analysis of the items which compose earnings and profits. Merely "requiring all corporations to compute earnings and profits at one time is not the same as requiring all corporations to treat each item in that computation in the same manner." Gardner, *supra* note 21, at 249.

24. The court noted exceptions contained in Treas. Reg. 1.312-6(b)(c) (1955), such as interest received on tax exempt bonds which are not included in taxable income yet must be included in earnings and profits. Nearly all authorities agree that taxable income and earnings and profits are not synonymous; see, *e.g.,* Commissioner v. Wheeler, 324 U.S. 542, 546 (1945).

25. 47 T.C. at 33.

26. The court noted the split of authority and reviewed the decisions considering the primary issue, concluding that after being reversed by the Eighth Circuit in *Alworth* the Tax Court has consistently followed the reversal and that there was no reason why it should not adhere to the same view in this case. However, the court completely ignored its prior decision in Robert L. Bender, *supra* note 17, just as it did in Newark Amusement Corp., *supra* note 20.

27. It is difficult to determine just what the present position of the Eighth Circuit is in view of its decision in Simon v. Commissioner, *supra* note 17. The *Simon* court ignored *Alworth* just as the Tax Court has ignored *Bender.*

profits.[28] There is also disagreement as to whether "earnings and profits" is primarily a statutory concept[29] or an accounting concept subject to general accounting principles.[30] As one writer has observed: "The sum of the issue is a conflict between the Treasury's desire to have conformity within a given corporate entity for all purposes related to taxation; and the businessman's drive to reflect as clearly as possible, at any given point in time, present net worth of the corporation."[31] There appears to be no logical reason why the method of accounting utilized should dictate the deduction of tax liability in determining earnings and profits. General accounting practice and common sense would seem to require deduction of tax liability in determining the amount of distributable dividends out of current year's earnings and profits.[32] Moreover, the policy of not allowing a cash basis corporation to deduct due but unpaid taxes promotes a gross unfairness among taxpayers in that such a policy allows the government to collect a double tax on the total amount of current year's earnings and profits by first taxing the cash basis corporation on the total amount at corporate rates and then taxing the shareholder on the same amount as ordinary income.[33] No such harsh result obtains for corpora-

28. See, *e.g.*, BITTKER & EUSTICE, FEDERAL INCOME TAXATION OF CORPORATIONS AND SHAREHOLDERS ¶ 5.03 (2d ed. 1966); Schwanbeck, *The Accountant's Problem in Working With "Earnings and Profits" for Tax Purposes*, 10 J. TAXATION 22 (1959). One authority often cited for a general discussion of earnings and profits is Rudick, *"Dividends" and "Earnings or Profits" Under the Income Tax Law: Corporate Non-Liquidating Distributions*, 89 U. PA. L. REV. 865 (1941). See also Albrecht, *"Dividends" and "Earnings or Profits,"* 7 TAX L. REV. 157 (1952).

29. 1 MERTENS, FEDERAL INCOME TAXATION ¶ 9.28 (rev. ed. 1962); Zarky & Biblin, *The Role of Earnings and Profits in the Tax Law*, 1966 So. CAL. TAX INST. 145, 159; 19 J. TAXATION 263 (1963).

30. Commissioner v. James, 49 F.2d 707, 708 (2d Cir. 1931): "In employing the phrase 'earnings and profits' . . . we think Congress intended the use of the term in the ordinary accounting understanding . . . ." This statement has been criticized as "unquestionably too broad." 1 MERTENS, *op. cit supra* note 29 n.78; SURREY & WARREN, FEDERAL INCOME TAXATION 1238 (1960 ed.) ("The earnings and profits of a year . . . are based upon actual net income and expenses. The concept is much closer to the actual increase in earned surplus determined by the accountant than to taxable income."); Emmanuel, *Earnings and Profits; an Accounting Concept?*, 4 TAX L. REV. 494, 498 (1949).

31. Gardner, *supra* note 21, at 250.

32. Faweus Mach. Co. v. United States, *supra* note 3, at 378: "[W]hile the taxes for any year are not payable until the following year, good accounting practice requires an accrual of them as a liability of the current year's business. . . ." See also Commissioner v. James, *supra* note 30, at 708. It should be noted that both these cases concerned accrual basis taxpayers. *But see* Hadden v. Commissioner, *supra* note 7, at 712 (same reasoning with respect to a cash basis taxpayer).

33. Assuming no deductions or credits, suppose a corporation has current year's earnings and profits of $100,000 and the corporate tax liability is $40,000. The shareholder of a cash basis corporation (who receives the whole amount as a constructive dividend) would have to pay taxes on $100,000 as ordinary income or approximately $55,500, whereas the shareholder of an accrual basis corporation would pay taxes on

tions employing the accrual method. Finally, this policy may result in impairment of capital.[34] As the Tax Court and the circuit courts appear hopelessly split on the issue, a comprehensive definition of "earnings and profits" is badly needed. However, it appears that any effective definition will properly have to come from Congress and not the courts.

only $60,000 ($100,000 less $40,000) or approximately $28,800, a difference of $26,300. Unless earnings and profits are the same amount each year, a distortion will always exist as to the actual earnings and profits for the cash basis corporation.

34. *E.g.*, Drybrough v. Commissioner, *supra* note 13. Had the corporation not been allowed to deduct the deficiencies and fraud additions from current year's earnings and profits, it would have been rendered insolvent.