2-1-1979

Student Comments

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Abstention—Under the Pullman Doctrine a Federal District Court May Not Abstain from Determining the Constitutionality of a State Statute Unless Sufficiently "Persuasive" Reasons Are Articulated for Deferring to State Adjudication.

Lister v. Lucey

I. Introduction

The abstention doctrine grants a federal court the discretion to postpone adjudication of a matter properly within its jurisdiction in order to effect a balance between the rights of an individual litigant and the interests of the state judiciary. When the objectives of federalism underlying abstention allow this deference for state proceedings to work inequitably, a critical review of the abstention is necessary. Lister v. Lucey presented the Court of Appeals for the Seventh Circuit with such a situation. Although the Seventh Circuit discussed at length the reasons supporting a firm limitation of abstention, the court hesitated to promulgate specific guidelines thus minimizing the precedential value of its opinion.

II. Statement of Facts

In October, 1971, four state university students brought a class action in the Federal District Court for the Western District of Wisconsin contesting the constitutionality of a Wisconsin statute which classified students as residents or nonresidents. The pertinent part of the statute is as follows:

36.16 Nonresident tuition at university: [exceptions] (1) (a) Any adult student who has been a bona fide resident of the state for one year next preceding the beginning of any semester for which such student registers at the university, or any minor student whose parents have been bona fide residents of the state for one year next preceding the beginning of any semester for which such student registers at the university, or any minor student whose natural parents are divorced or legally separated who has resided substantially in this state during his years of minority and at least one year next preceding the beginning of any semester for which such student registers at the university, or whose mother or father has been a bona fide resident for one year next preceding the beginning of any semester for which such student registers at the university, or any minor student who is an orphan and who has resided substantially in this state during his years of minority and at least one year next preceding the beginning of any semester for which such student registers at the university, or whose legal guardian if a person has been a bona fide resident of the state for one year next preceding the beginning of any semester for which such student registers at the university, shall while he continues a resident of the state be entitled to exemption from nonresident tuition, but not from incidental or other fees and tuition in the university.

(ab) Nonresident members of the armed forces who are stationed in this state and their wives and children shall be entitled to the exemptions provided in par. (a) during the period that such member of the armed forces is stationed in this state.

(ae) Any female who marries a bona fide resident shall be entitled to the exemptions

* 575 F.2d 1325 (7th Cir. 1978).
1 Wis. Stat. Ann §§ 36.16, 36.16(1) (a), (ab), (ae), (3) (West 1966) provides in pertinent part:
nonresidents for the purpose of determining tuition. The original complaint alleged that the statute deprived the plaintiffs of their civil rights under 42 U.S.C. § 1983. Subsequently, in December, 1972, the plaintiffs amended their complaint to contest the constitutionality of the statute on two additional grounds: vagueness, and arbitrary and irrational administration. Over a year later the district court determined that proper adjudication of the plaintiffs' constitutional claim required a state court clarification of the statutory language in question. The district court, therefore, abstained on the authority of Railroad Commission of Texas v. Pullman Co. and retained jurisdiction awaiting the state court interpretation.

The plaintiffs chose not to appeal the abstention order and immediately filed a complaint in the Circuit Court for Dane County, Wisconsin. In May, 1974, the plaintiffs' state claim was dismissed for lack of subject matter jurisdiction. The state circuit court reasoned that the plaintiffs failed to exhaust the legislative claims procedure which was an established prerequisite to the commencement of a suit in the Wisconsin courts. The plaintiffs appealed this decision and simultaneously returned to the federal forum with a motion to vacate the district court's stay order since no speedy means for clarification remained in the state system.

provided in par. (a) effective the semester following her marriage and while continuing to reside in this state.

(3) In determining bona fide residence, filing of state income tax returns in Wisconsin, eligibility for voting in the state of Wisconsin, motor vehicle registration in Wisconsin, and employment in Wisconsin shall be considered. Notwithstanding the provisions of par. (1)(a), a student from another state who is in this state principally to obtain an education will not be considered to have established a residence in Wisconsin by virtue of attendance at educational institutions.

Every person, who under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory, subjects or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress.

3 The plaintiffs filed two amended complaints. The first added several defendants, including those then serving as Governor of Wisconsin, Regents of the University of Wisconsin, the President of the University of Wisconsin and the Chancellor, Registrar, Residency Examiner, and members of the Committee on Appeals from Non-Resident Tuition of the University of Wisconsin, Madison campus. All the defendants were sued in both their individual and official capacities and the Regents were also sued as a collective body. 575 F.2d at 1328.

4 The concept of "vagueness" or indefiniteness of a statute rests on the constitutional principle that procedural due process requires fair notice and proper standards for adjudication. Landry v. Daley, 280 F. Supp. 938, 951 (N.D. Ill. 1968).

5 An "arbitrary act" or decision is one that is arrived at through the exercise of will or by caprice, one supported by mere option or discretion and not by a fair or substantial reason. Bedford Inv. Co. v. Folb, 79 Cal. App. 2d 363 180 P. 2d 361, 362, (1947).

6 312 U.S. 496 (1941).

7 An abstention order has been determined to be sufficiently final for the purpose of appeal. Drexler v. Southwest Dubois School Corp., 504 F. 2d 836, 838 (7th Cir. 1974).

8 Wis. STAT. ANN. § 283.01 (West 1958) provides:
Actions against state, bond. Upon the refusal of the legislature to allow a claim against the state, the claimant may commence an action against the state by service as provided in § 262.06(3) and by filing with the clerk of court a bond, not exceeding $1,000, with two or more sureties, to be approved by the attorney-general, to the effect that he will indemnify the state against all costs that may accrue in such action and pay to the clerk of court all costs, in case he shall fail to obtain judgment against the state.

9 The plaintiffs also argued that a recent and very similar case offered sufficient clarification of the statute in question. In that case, Hancock v. Regents of Univ. of Wisconsin, 61 Wis.
The federal court motion was still pending two years later, when the Wisconsin Supreme Court affirmed the circuit court ruling. The plaintiffs again moved to vacate the abstention order because no feasible means for clarification remained. The district court, nevertheless, refused to hear the case stating that "the reasons for abstention were undiminished" and that the plaintiffs must bear the burden of their improper pursuit of state remedies.

Upon dismissal by the district court, *Lister v. Lucey* came before the Seventh Circuit. On appeal, the court considered two main issues rooted in the application of the federal abstention doctrine: (1) the appropriateness of the district court's initial abstention and (2) the district court's *de facto* requirement that the plaintiffs exhaust state non-judicial remedies before seeking relief in the federal courts. Ultimately, the Seventh Circuit reversed and remanded the case for a determination on the merits.

### III. The Propriety of the Initial Abstention

In *Lister*, the plaintiffs exercised their right under § 28 U.S.C. 1343 to contest the validity of an allegedly unconstitutional state statute in the federal forum. The federal judiciary has an inherent obligation to adjudicate such controversies. An exception to this obligation arises, however, when an accurate interpretation of a state legal question may substantially facilitate the disposition of a case. If a claim presents a significant question of state law, the judicial doctrine of "abstention" empowers a federal court to retain jurisdiction yet postpone adjudication pending state clarification of that issue.

This exception to the exercise of federal jurisdiction gained prominence in the landmark decision of *Railroad Commission of Texas v. Pullman Co.* The plaintiff in that case contested a state railroad commission order as a violation of both Texas law and the federal Constitution. The Federal District Court of Texas enjoined the order. Subsequently, the Supreme Court unanimously reversed. Justice Frankfurter, a major proponent of the abstention doctrine and the author of the *Pullman* opinion, described the district court's action as an improper interference in a matter which in the best interest of federalism and equitable ad-

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2d 434, 213 N.W.2d 45 (1973), the Wisconsin Supreme Court held, however, the claim not justiciable without discussing whether the plaintiff had made a claim to the legislature pursuant to § 285.01.

10 575 F.2d at 1332.

11 28 U.S.C. § 1343 (1948) provides:

> The district courts shall have original jurisdiction of any civil action authorized by law to be commenced by any person: ... (3) to redress the deprivation, under color of any State law, statute, ordinance, regulation, custom or usage, of any right, privilege, or immunity secured by the Constitution of the United States or by any Act of Congress providing for equal rights of citizens or of all persons within the jurisdiction of the United States.

*See* note 2 *supra.*

12 The federal courts have been held to have a "virtually unflagging obligation" to exercise the jurisdiction given them. Colorado River Water Cons. Dist. v. United States, 424 U.S. 800, 817 (1976). *See also* England v. Medical Examiners, 375 U.S. 411, 415 (1964); Cohens v. Virginia, 19 U.S. (6 Wheat.) 264 (1821).

13 280 F. Supp. 938.


judication demanded the perspective of a state tribunal. The Supreme Court, therefore, instructed the federal court to "stay its hand" in deference to the independent state process. The Court characterized such restraint as imperative to the harmonious interaction of the federal and state judiciaries.

The Wisconsin district court perhaps sought to exhibit such restraint by abstaining in *Lister*. ThePullman doctrine, however, purports to be a very narrow exception to the federal judiciary's jurisdictional obligation and demands very specific circumstances in order that its operation will not thwart its equitable purpose. The original *Pullman* decision, for instance, insisted that the abstention doctrine should be invoked only where "easy and ample means" for clarification were readily available in the state courts. The importance of this prerequisite has been repeatedly emphasized by decisions illustrating the adverse effects accompanying abstention. Cases involving *Pullman* indicate that the doctrine has been consistently plagued by concomitant problems of delay, expense and piecemeal adjudication. A federal court should only invoke abstention, therefore, when proper adjudication obviously necessitates, and the state system clearly affords, clarification.

The statute challenged in *Lister*, however, did not present a situation appropriate for *Pullman* abstention as the availability of clarification was not evident. Rather, the *Lister* case fell into a category of circumstances described in *Pullman* and subsequent holdings, as particularly inappropriate for abstention. Specifically, the Seventh Circuit found "relatively unpersuasive" the district court's conclusion that certain ambiguities in the Wisconsin statute required state clarification. Even if such vagueness existed, however, a substantial body of case law has established that abstention is inappropriate in cases, such as *Lister*, in which the statute is challenged as vague in the abstract.

Finally, the Seventh Circuit criticized the alternative statutory construction proffered by the district court as implausible. Although the court's construction would, indeed, provide a basis for abstention by suggesting ambiguity within the broad statutory language, such an interpretation appears wholly unfounded.

The Seventh Circuit's outline of the faulty logic underlying the district court's abstention amply buttressed its decision to reverse. *Lister*, then, is actually a narrowly drawn opinion which hinges solely upon the abstention issue.

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16 312 U.S. at 501.
18 312 U.S. at 501.
20 575 F.2d at 1332.
21 *See* 280 F. Supp. 938.
22 575 F.2d at 1332.
23 *See* text accompanying note 4 *supra*.
24 The district court suggested that the broad language of § 36.16 (3) might be construed to require that males who marry bona fide female residents are entitled to residency status as are females who marry bona fide male residents. The Seventh Circuit found that such a broad construction is unsupported by the language of the statute and would render unnecessary § 36.16 (1) (ae) thereby violating fundamental principles of statutory construction. 575 F.2d at 1333. *See also* Johnson v. State, 76 Wis. 2d 672, 251 N.W.2d 834 (1977).
for disposition. As such, the case basically represents a remonstration of a federal court’s abuse of discretion.

IV. The Potential for Limitation of *Pullman*

The Seventh Circuit did not limit its discussion in *Lister* to the dispositive abstention issue, but extended it to encompass a more specific procedural question. Essentially, the district court’s dismissal in *Lister* created a requirement that, upon abstention, the federal litigant exhaust state non-judicial remedies, such as the legislative claims procedure, if the state courts refuse to clarify the law until those non-judicial remedies are pursued. This provocative ruling allowed mere procedural prerequisites to eclipse the rights of a federal litigant. Thus, the district court’s ruling in *Lister* clearly raised a question concerning the proper prerequisites for regaining the federal forum after the abstention doctrine has been invoked. Specifically, *Lister* squarely presented the issue whether this unprecedented extension of *Pullman* abstention could, under any circumstances, further the doctrine’s original goals of judicial economy and equitable adjudication.

The Seventh Circuit’s analysis focused on the consequences which would result from an imposition of the exhaustion requirement, such as delay and piecemeal adjudication. The exhaustion requirement, in essence, forces a plaintiff to pursue all available “legislative” or “administrative” remedies before presenting a claim in the courts. This principle operates expeditiously when nonjudicial proceedings dispose of a particular claim completely and competently.\(^{26}\) Exhaustion of such remedies, however, may not provide the judicial clarification sought by abstention. The Seventh Circuit acknowledged, therefore, that a concurrent imposition of the exhaustion requirement and federal abstention would result in unwarranted delay and resort to a process which could not grant the requested relief. As further support, the court noted that the inequity worked by such delay has even been held to outweigh the need for clarification in appropriate circumstances.\(^ {27}\) The Seventh Circuit’s reasoning, then, logically leads to the conclusion that a procedural prerequisite perpetuating delay without the possibility of affording clarification should never be required.

In addition to these problems of adjudication, the court examined the current trend toward the abolition of exhaustion in § 1983 cases.\(^ {28}\) The Supreme Court affirmed this trend by specifically holding that a requirement of exhaustion in § 1983 cases would circumvent the expedient equitable solution sought by the statute.\(^ {28}\) The litigant’s right to contest a deprivation of his civil rights in the federal forum, then, is imperative to the determination of a § 1983 action. In


the *Lister* case, this right had already been postponed by the district court's abstention. Although the abstention doctrine cannot be wholly excised as a procedural alternative in § 1983 cases, there is no ascertainable reason for further dissipation of the litigant's right to federal jurisdiction. The requirement of exhaustion would have that precise effect, and therefore contradicts contemporary judicial policy in § 1983 actions.

Finally, the Seventh Circuit recognized the absence of substantial comity concerns which normally reinforce an abstention order. The state trial court in *Lister* evinced total disinterest in the opportunity to determine the statutory question posed by the case. The Seventh Circuit noted that if the state judiciary had a significant interest in the resolution of the *Lister* question, the state supreme court could have exercised its inherent authority to hear the case absent the procedural prerequisites. Furthermore, the Wisconsin Supreme Court reacted differently to the district court's explicit request for a construction of the statute. The factors outlined in the Seventh Circuit opinion stress the need for a precise limitation of the expansion of *Pullman* doctrine created by the Wisconsin district court. Unfortunately, the Seventh Circuit failed to provide new direction in the area. The court specifically acknowledged the "powerful case" that these reasons presented for promulgating a general rule against prolonging abstention when a state court requires exhaustion; however, it stopped short of establishing any concrete procedural reform. Rather, the court stated that it "need not go so far here," thereby relegating its pointed discussion to mere dicta.

Undeniably, the *Lister* court could not have used unfettered discretion in establishing new limits on abstention. In view of recent Supreme Court rulings, for example, the Seventh Circuit could not have abrogated the application of abstention in § 1983 cases altogether. It could, however, have conformed with current judicial policy declaring the exhaustion requirement wholly inappropriate in § 1983 cases such as *Lister*. Despite the Seventh Circuit's refusal to rule on this ground alone, the court clearly evinced an interest in limiting the district court's discretion to deny a litigant his right to the federal forum. Yet by not providing a decisive resolution to this conflict, the *Lister* court lost an opportunity to effect a valuable limitation. The unrealized potential of *Lister* suggests that the Seventh Circuit did not fulfill its judicial obligation to provide fundamental guidelines in such an unrefined area of the law as abstention.

V. The Right to Abstain and the Obligation to Adjudicate: A Proposed Balance

The narrow holding rendered in *Lister v. Lucey* reveals strong strains of judicial conservatism. The opinion was effective to the extent that it focused on the impropriety of the district court's initial abstention. *Lister*, however, involved

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30 575 F.2d at 1332.
31 Id.
32 Id.
33 See text accompanying note 29 supra.
34 See text accompanying notes 27-28 supra.
an extraordinary example of federal judicial procrastination which the courts of appeal, upon review, cannot continue to ignore. An establishment of reasonable guidelines designed to preclude future recurrences of the *Lister* problem is essential. Such reform could easily have been accomplished by the Seventh Circuit since several alternatives are suggested by a reexamination of the origin and development of the abstention doctrine.

Theoretically, the *Pullman* doctrine seeks clarification in order to effect equitable adjudication and judicial economy as well as the furtherance of federalism.\(^{35}\) To realize these goals in a situation such as *Lister*, therefore, the Seventh Circuit should require district courts to make a specific finding of fact that the clarification sought through abstention could be easily and amply provided by the state courts. A party opposing the abstention should have the right to appeal such an assertion. Since an abstention order has already been held to be a sufficiently final determination for the purposes of an appeal,\(^{36}\) this avenue would simply be extended to encompass an additional basis of non-expedient clarification. If the federal court can confidently ascertain, in this initial stage, not only that the appropriate grounds for abstention exist but that the state court can completely and fairly dispose of the issue, the federal court should dismiss the action and direct the plaintiff to the state court without an anticipation of returning to the federal forum. As a procedural safeguard, the dismissal should be without prejudice so that the litigant’s right to a judicial forum is not irretrievably canceled.\(^{37}\)

Although such guidelines may shock the ardent advocates of the right to a federal forum, they offer an honest, practical alternative to the inequitable federal forum-shuffling evinced in *Lister v. Lucey*. The promulgation of such guidelines would emphasize the substantial obligation of a federal district court to direct a jurisdictionally questionable controversy to the proper forum initially in order to insure the most expeditious and equitable resolution.

VI. Conclusion

Although the judiciary must exercise caution in establishing general rules of law, it has an obligation to prevent unnecessary recurrences of injustice. *Lister v. Lucey* presented the Seventh Circuit with an opportunity to limit a clearly inequitable operation of the federal abstention doctrine. The court, by limiting its holding, failed to establish such a specific limitation on the discretionary invocation of abstention. Although this action may be defended as an exercise in judicial restraint, *Lister* illustrates the blatant inequity of juggling a federal litigant through a myriad of judicial and non-judicial channels for more than six years. Such an illustration challenges the proposition that *Lister* was an appropriate case for restraint; indeed, it suggests an affirmative obligation on the part of the judiciary to curtail such abuse. Both equitable adjudication and

\(^{35}\) 312 U.S. at 500-01.

\(^{36}\) Drexler v. Southwest Dubois School Corp., 504 F.2d 836, 838 (7th Cir. 1974).

judicial economy, the original objectives of the abstention doctrine, demand more precise and fully articulated guidelines than those suggested in *Lister*. With dockets overflowing, federal district courts may tend to seize any opportunity to shift their burden to another forum. As the abstention doctrine, in effect, endorses such action, the potential for judicial abuse is great. In order to curb this abuse, the Seventh Circuit should have defined and limited not only the circumstances appropriate for abstention but also the reasonable duration of its operation.

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38 In *Thermatron Products, Inc. v. Hermansdorfer*, 423 U.S. 336 (1976), the Supreme Court held that a district court had exceeded its authority by remanding the case before it on the sole ground that its docket was overcrowded.
Commerce Clause—Congress Has the Power Under the Commerce Clause to Extend the Equal Pay Act to State and Local Governmental Employees.

Marshall v. City of Sheboygan*

I. Introduction

Relying on its Commerce Clause power,1 Congress enacted the Fair Labor Standards Act of 19382 (FLSA) in an attempt to eliminate the exploitation of labor.3 Through its regulations, Congress intended to “correct labor conditions detrimental to the maintenance of the minimum standard of living for health, efficiency, and general well-being of workers. . . .”4 To achieve this goal, the Act provided minimum wage5 and maximum hour6 regulations.

In National League of Cities v. Usery,7 the Supreme Court held that the FLSA minimum wage and hour provisions were inapplicable to certain state employees. The Court proclaimed that the promulgation of such regulations was an improper exercise of congressional power under the Commerce Clause. The tenth amendment8 was interpreted by the Court to limit Congress’ authority under the Commerce Clause to interfere with traditional state governmental functions.9

In 1963, Congress amended the Equal Pay Act10 (EPA) to the FLSA. The purpose of the equal pay amendment was to correct the discriminatory practice of sex-based wage differentials. Again, the Commerce Clause was relied upon by Congress as the constitutional authority for enacting the amendment.11

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* 577 F.2d 1 (7th Cir. 1978).
3 83 Cong. Rec. 9256 (1938).
8 “The powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people.” U.S. Const. amend. X.
9 426 U.S. at 845.
   (1) No employer having employees subject to any provisions of this section shall discriminate, within an establishment in which such employees are employed, between employees on the basis of sex by paying wages to employees in such establishment at a rate less than the rate at which he pays wages to employees of the opposite sex in such establishment for equal work on jobs the performance of which requires equal skill, effort, and responsibility, and which are performed under similar working conditions except where such payment is made pursuant to (i) a seniority system; (ii) a merit system; (iii) a system which measures earnings by quantity of quality of production; or (iv) a differential based on any other factor other than sex: Provided, that an employer who is paying a wage rate differential in violation of this subsection shall not, in order to comply with the provisions of this subsection, reduce the wage rate of any employee.
In *Marshall v. City of Sheboygan,*\(^{12}\) the Seventh Circuit sought to determine whether Congress has the power under the Commerce Clause to extend the Equal Pay Act to state and local governmental employees. Following a discussion of the *National League of Cities* decision, the court held that the Supreme Court's ruling did not preclude an Equal Pay Act suit against the states or their political subdivisions.

This comment will demonstrate how the Seventh Circuit has overgeneralized with respect to its holding that Congress has the power to extend the EPA to state and local governments, despite the tenth amendment limitation on Commerce Clause regulation announced in *National League of Cities.* Such a demonstration will be accomplished through an analysis of the vague guidelines set out in *National League of Cities,*\(^{13}\) and an explanation of the potentially undesirable effects of applying the equal pay law to the states.\(^{14}\) This comment will also suggest that cases such as the *City of Sheboygan* should, rather, be decided under section five of the fourteenth amendment,\(^{15}\) for such an approach would allow courts to avoid the confusion inherent in applying the vague guidelines announced in *National League of Cities.*\(^{16}\)

II. Statement of the Facts

On March 26, 1976, the Secretary of Labor commenced an action to enjoin the City of Sheboygan, Wisconsin, from violating the equal pay provision of the Fair Labor Standards Act.\(^{17}\) The Secretary alleged that a violation had occurred when the City discriminated against women employed as custodians in its public schools by paying them lower wages than were paid men doing "equal work on jobs the performance of which requires equal skill, effort, and responsibility and which are performed under similar working conditions."\(^{18}\) The City promptly filed a motion for judgment on the pleadings maintaining that pursuant to *National League of Cities,* Congress had exceeded its constitutional authority by regulating the compensation paid by state and local governments to its employees.\(^{19}\) The district court denied the motion and the City appealed to the Seventh Circuit.

The court of appeals held that Congress has the power under the Commerce Clause to extend the Equal Pay Act to state and local governmental employees.\(^{20}\) In reaching its decision, the Seventh Circuit distinguished *National League of Cities* and held that the tenth amendment did not bar an action by the Secretary to enforce the Equal Pay Act against state and local governments.

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12 577 F.2d 1 (7th Cir. 1978).
13 See text accompanying notes 24-64 infra.
14 See text accompanying notes 71-76 infra.
15 "The Congress shall have power to enforce, by appropriate legislation, the provisions of this article." U.S. Const. amend. XIV, § 5.
16 See text accompanying notes 94-109 infra.
17 577 F.2d at 2.
19 577 F.2d at 2.
20 Id. at 1.
III. Scope of the FLSA

When the Fair Labor Standards Act was first enacted, § 3(d) specifically excluded states and their political subdivisions from coverage. With the 1966 amendments to the FLSA, however, expansive changes in coverage and exemptions were effectuated. For the first time, state and local governmental employees associated with hospitals, institutions, and schools fell within the purview of the Act. After an additional four-year effort to further expand coverage under the FLSA, amendments were passed in 1974 which extended the scope of the Act to include state and local governments and their political subdivisions. Under the 1974 amendments, public employers are subject to wage and hour requirements that are equivalent to those which private employers had been subject previously.

IV. National League of Cities

In National League of Cities, the Supreme Court was faced with the question of the constitutionality of the 1974 amendments. Adhering to its policy of restricting federal power while expanding the "sovereign" powers of the states, the Court held the extension of the scope of the FLSA to the states unconstitutional under the facts of National League of Cities. Accordingly, in Sheboygan the City filed a motion for a judgment on the pleadings contending that under National League of Cities, Congress does not have the constitutional authority to regulate the compensation paid by a state or local government to its employees. The Seventh Circuit also used National League of Cities to conclude that the EPA was constitutionally applicable to the states. In an effort to evaluate the Seventh Circuit's decision in Sheboygan, an analysis of National League of Cities is required.

A. The Commerce Clause and the Tenth Amendment

Under the Commerce Clause, Congress has been granted the power to regulate interstate commerce. This grant of "plenary authority" has been declared "an affirmative power commensurate with the nation's needs." Limits exist, however, upon the power of Congress to override state sovereignty. In Fry v. United States, the Court recognized an express declaration of these limitations in the tenth amendment. In a footnote to the main opinion the Court proclaimed:

21 Act of June 25, 1938, ch. 676, § 3(d), 52 Stat. 1060 (current version at 29 U.S.C. § 203(d) (1970)) reads: “'Employer' includes any person acting directly or indirectly in the interest of an employer in relation to an employee but shall not include the United States or political subdivisions of a state.”
24 577 F.2d at 2.
While the Tenth Amendment has been characterized as a "truism," stating merely that "all is retained which has not been surrendered," United States v. Darby, 312 U.S. 100, 124 (1941), it is not without significance. The Amendment expressly declares the constitutional policy that Congress may not exercise power in a fashion that impairs the States' integrity or their ability to function effectively in a federal system.28

After the passage of the 1974 amendments to the FLSA, the National League of Cities, the National Governors Conference, and several state and local governments challenged the constitutionality of the amendments when applied to the states.29

The challenge in National League of Cities was not directed toward the scope of authority granted Congress under the commerce power, but rather towards the validity of the 1974 amendments to the extent they transgress the affirmative limitations contained in the Constitution.30 Specifically, the League contended that the 1974 amendments to the FLSA were inapplicable to them due to a tenth amendment limitation on the commerce power of Congress.31

B. The Lower Court's Ruling

Plaintiffs sought both declaratory and injunctive relief against the amendments' application to them. A three-judge court granted the Secretary of Labor's motion to dismiss for failure to state a claim upon which relief could be granted because it felt compelled to follow precedent laid down in Maryland v. Wirtz.32 In Wirtz, the Supreme Court sustained the constitutionality of the 1966 amendments and held that the amendments did not infringe upon areas of state sovereignty protected by the tenth amendment.

C. The Supreme Court Ruling

The appellants' position was adopted by the Supreme Court and, as a result, the tenth amendment was applied as a limitation upon federal commerce power regulation of state activities. The Court stated that "insofar as the challenged amendments operate to directly displace the States' freedom to structure integral operations in areas of traditional governmental functions, they are not within the authority granted Congress by Article I, § 8, cl. 3."33 The Supreme Court limited its opinion, however, by stating that the minimum wage and overtime provisions were not held to be inapplicable to the states in all situations, but only

28 Id. at 547 n.7.
29 National League of Cities v. Brennan, 406 F.Supp. 826, (D.D.C. 1974). The state and local governments which were parties to the action are as follows: the states of Arizona, Indiana, Iowa, Maryland, Massachusetts, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, Oklahoma, Oregon, South Carolina, South Dakota, Texas, Utah, Washington, Wyoming, the Metropolitan Government of Nashville and Davidson County, Tenn., and the cities of Cape Girardeau, Mo., Lompac, Cal., and Salt Lake City, Utah.
30 426 U.S. at 841.
31 Id. (Appellants noting instances when the Commerce Clause had been found invalid because it offended a constitutional right.) See United States v. Jackson, 390 U.S. 570 (1968) (sixth amendment) and Leary v. United States, 395 U.S. 6 (1969) (fifth amendment).
33 426 U.S. at 852.
"insofar" as they interfere with the sovereignty of the states in areas of "traditional" governmental functions.\textsuperscript{34}

The Court acknowledged the limitations of its decision by refusing to overrule \textit{United States v. California},\textsuperscript{35} in which the Safety Appliance Act was held applicable to the State of California because it had engaged in interstate commerce by rail.\textsuperscript{36} In that opinion, the Court stated:

We look to the activities in which the states have traditionally engaged as marking the boundary of the restriction upon the federal taxing power. But there is no such limitation upon the plenary power to regulate commerce. The state can no more deny the power if its exercise has been authorized by Congress than can an individual.\textsuperscript{37}

In reference to the above statement, the Court in \textit{National League of Cities} asserted the following: "We think the dicta from \textit{United States v. California} simply wrong. Congress may not exercise that power so as to force directly upon the states its choices as to how essential decisions regarding the conduct of integral governmental functions are to be made."\textsuperscript{38} In addition, however, the \textit{National League of Cities} Court declared: "The holding of \textit{United States v. California}, as opposed to the language quoted in the text, is quite consistent with our holding today. There California's activity, to which the congressional command was directed was not in an area that the states have regarded as integral parts of their governmental activities."\textsuperscript{39} The Court, therefore, held that regulations were unconstitutional as applied to the states only in areas of "traditional operations" or "integral governmental functions."\textsuperscript{40} Congressional interferences with state activities of a routine proprietary sort were expressly excluded from the scope of state autonomy.\textsuperscript{41}

Unfortunately, the Court did not define those activities which fall within the concept of "traditional operations."\textsuperscript{42} As a result, lower courts must decide in each case whether the target of regulation is, as the Supreme Court described, an activity which is "typical of those performed by state and local governments in discharging their dual functions of administering the public laws and furnishing public services."\textsuperscript{43}

In addition to requiring that the regulation be aimed at integral governmental functions before the tenth amendment limitation on Commerce Clause regulations is operative, the Court insisted that the regulation must deal with an attribute of state sovereignty.\textsuperscript{44} Without explanation, the Court stated: "One

\textsuperscript{34} \textit{Id.}
\textsuperscript{35} 297 U.S. 175 (1936).
\textsuperscript{36} \textit{Id.} at 185.
\textsuperscript{37} \textit{Id.}
\textsuperscript{38} 426 U.S. at 854-55.
\textsuperscript{39} \textit{Id.} n.18.
\textsuperscript{40} \textit{Id.} at 852.
\textsuperscript{41} For an argument taking the position that such a holding is inconsistent, see Tribe, \textit{Unraveling National League of Cities: The New Federalism and Affirmative Rights to Essential Government Services}, 90 Harv. L. Rev. 1065 (1977).
\textsuperscript{43} 426 U.S. at 851.
\textsuperscript{44} \textit{Id.} at 845.
undoubted attribute of state sovereignty is the states' power to determine wages. . . .

The Court proceeded to state that determinations which are attributes of state sovereignty must also be "functions essential to a separate and independent existence" of the state. To establish guidelines for rendering such decisions, the Court stated that the determinations (in this case wages and hours) must be ones upon which the government's performance of the traditional governmental functions rests.

National League of Cities is further limited by the Court's discussion of what constitutes a displacement of the states' freedom to structure integral operations. After a brief examination of the financial impact of the imposition of a minimum wage, the Court noted that it was not preoccupied with actual impact. The Court did not dwell on actual financial impact because even if the appellee's assessments concerning the impact of the amendments were accepted, the application of the provisions would "nonetheless significantly alter or displace the states' abilities to structure employer-employee relationships. . . ." As discussed previously, the degree of financial impact needed to qualify as significantly altering or displacing the states' abilities to structure employer-employee relationships must be determined on a case-by-case basis.

In National League of Cities, due to the financial impact of the wage law, the state would be left with the choice of "either attempt[ing] to increase their revenue to meet the additional financial burden imposed upon them by paying congressionally prescribed wages to their existing complement of employees, or reduc[ing] that complement to a number which can be paid the federal minimum wage without increasing revenue." As a result of the dilemma presented by the minimum wage restriction, the Court believed such a regulation would constitute an impermissible interference with state sovereignty. This conclusion was reached on the basis that such a dilemma would lead to the "forced relinquishment" of important governmental activities and services which their citizens require. Thus, the Court had determined that under the facts of National League of Cities, the states' power to determine the wages which shall be paid to their employees in order to carry out their governmental functions is a determination which is a function "essential to [a] separate and independent existence, so that Congress may not abrogate the states' otherwise plenary authority to make them."

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45 Id.
46 Id.
47 Id. at 851. After a discussion of the characteristics of a traditional governmental function, the court states: "If Congress may withdraw from the States the authority to make those fundamental employment decisions (such as wages) upon which their systems for performance of their functions must rest, we think there would be little left to the States' separate and independent existence." Id.
48 Id. at 846.
49 Id. at 851.
50 Id. at 848.
51 Id. at 851.
52 Id. at 847.
53 The Court made specific reference to instances in which the regulations would force relinquishment of important governmental activities by pointing to the allegations contained in appellants' complaints. Id. at 847.
54 Id. at 845-46 (quoting Coyle v. Oklahoma, 22 U.S. 559, 580 (1911) which in turn quoted Lane County v. Oregon, 74 U.S. (7 Wall.) 71 (1869)).
In addition to the guidelines set forth above, the Court attached another limitation upon the use of a state sovereignty defense. The degree of interference with a state's sovereignty must be weighed against the magnitude of the problem compelling the federal enactment. As discussed by Justice Blackmun in his concurring opinion, the Court adopted a balancing approach such that when "the federal interest is demonstrably greater and where state facility compliance with imposed federal standards would be essential," the regulation is upheld.

A potential application of the balancing test was made apparent by the National League of Cities Court by comparing the minimum wage and hour regulations of the FLSA with the Economic Stabilization Act upheld in Fry v. United States. In Fry, the Court upheld the constitutionality of the Economic Stabilization Act of 1970, which temporarily froze the wages of state and local governmental employees in order to combat a severe inflation that threatened our national economy. In reference to Fry, the Court made clear that Commerce Clause regulations would be allowed even though a state's sovereignty was affected when the regulation was occasioned by an extremely serious problem which "endangered the well-being of all the component parts of our federal system."

In effect, National League of Cities gave the States an affirmative defense to actions by the Secretary of Labor to enforce the minimum wage and hour provisions of the FLSA against state employers. When the provisions operate to directly displace the states' freedom to structure integral operations in areas of traditional governmental functions, the tenth amendment prohibits their application to the states. To determine whether the tenth amendment limitation is available, the facts must be applied to the test implicit in the National League of Cities decision.

D. National League of Cities' Test for Constitutionality of Commerce Clause Regulations

A test by which the constitutionality of Commerce Clause regulations of state and local governmental activity may be determined is implicit in the Court's decision in National League of Cities. The test may be constructed from the limitations described in the plurality opinion and Justice Blackmun's concurring opinion. First, it must be determined whether the congressional command inherent in the regulation is directed toward an activity which is "typical of those performed by state and local governments in discharging their dual functions of

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55 426 U.S. at 856.
57 Id. at 548.
58 426 U.S. at 856. Other than a mention by Justice Blackmun of environmental protection, the Court left no other guidelines for the lower courts to determine what constitutes a "demonstrably greater" federal interest. Thus, from the opinion it appears the Court intended such an interest to exist only when "the well-being of all the component parts of our federal system" is threatened. Id. at 856.
59 See Usery v. Allegheny County Inst. 544 F.2d 148, 155 n.11 (3rd Cir. 1976), cert. denied, 430 U.S. 946 (1977). Here, the Third Circuit concluded that rather than striking down the 1974 amendments for all purposes, National League of Cities is limited and merely gives the states an affirmative defense against actions by the Secretary of Labor to enforce the minimum wage and hour provisions of the FLSA.
60 426 U.S. at 849.
administering the public law and furnishing public services. Second, whether the regulation interferes with "functions essential to [a] separate and independent existence" of the state must be determined. Third, the inquiry must inquire whether the regulation "displaces state policies regarding the manner in which [the state] will structure delivery of those governmental services which their citizens require."

If the burdens imposed by the regulation lead to affirmative responses to the above inquiries, then the court must attempt to balance the federal interest with the degree of interference. If the interference with state sovereignty can be justified by a sufficiently strong federal interest, as defined by the Court, then the regulation causing such interference is permissible.

Although National League of Cities arose in the context of the minimum wage and overtime provisions, the reasoning employed in the decision is applicable in any case involving a regulation directed toward the state under the commerce power. Thus, a court must determine whether the particular regulation, under the particular facts presented, passes the test provided in National League of Cities. After such an analysis, if it is found that the regulation does not "displace the state's freedom to structure integral operations," then the tenth amendment limitation on the enactment is ineffectual.

Since the Equal Pay Act was passed under the authority of the Commerce Clause, when a lower court is faced with a situation in which the Act is being sought to be applied against the state, the court must follow the guidelines provided in National League of Cities to determine the constitutionality of its applicability as a Commerce Clause regulation. The manner in which the Seventh Circuit has followed those guidelines will be the basis upon which this comment will evaluate the Sheboygan decision.

V. The Seventh Circuit Decision in Sheboygan

In Marshall v. City of Sheboygan, the issue addressed by the Seventh Circuit was "whether Congress has the power under the Commerce Clause to extend the Equal Pay Act to state and local governmental employees." Holding in the affirmative, the court sought to support its decision with an analysis of National League of Cities as well as with a statement concerning its beliefs regarding the effects of the Equal Pay Act.

The Seventh Circuit acknowledged that National League of Cities did not vitiate entirely the applicability of the minimum wage and overtime provisions to the states. States and their subdivisions still possess an affirmative defense when "integral parts of [their] governmental activities" are challenged. The Seventh Circuit, however, failed to examine properly the Sheboygan facts and did not follow the guidelines established by National League of Cities. Rather, reliance

61 Id. at 851.
62 Id. at 845.
63 Id. at 847.
64 Id. at 852.
65 577 F.2d at 1.
66 Id. at 3.
67 Id. at 4 (quoting 426 U.S. at 854 n.18).
was placed on a generalized interpretation of the effects of the Equal Pay Act.

The court summarized the basis for its decision as follows:

Unlike the minimum wage and overtime provisions addressed in *National League of Cities*, the prerogative to pay women unequal wages for equal work is not a "fundamental employment decision." The ability to discriminate solely on the basis of sex cannot be considered an attribute of sovereignty necessary to a separate and independent existence. The equal pay provision does not interfere with a state's ability to "structure employer-employee relationships." States are free to set all substantive terms of employment. The Equal Pay Act requires only that the substantive terms of employment not be determined arbitrarily or in a discriminatory fashion. Equally important, the Equal Pay Act does not displace any State policies regarding the manner in which a State may structure delivery of its services.

The court proceeded to conclude that the 1974 extension of the Equal Pay Act to the states is a valid exercise of Congress' power under the Commerce Clause. Yet, such a broad contention is unjustified, for as will be demonstrated, the equal-pay law could have the effect of infringing upon the states' freedom to a degree which would force the state to restructure its sovereign affairs in the same manner as could the minimum wage and overtime provisions. The Seventh Circuit's refusal to acknowledge this possibility accounts for its failure to apply the guidelines outlined in *National League of Cities*.

VI. The EPA Viewed as a Wage Regulation

The Equal Pay Act was not instituted only as an anti-discrimination measure. Like the Minimum Wage Law, the EPA sought to correct adverse living conditions by correcting the discriminatory practice of sex-based wage differentials.

To achieve this goal, the Equal Pay Act stipulates that "an employer who is paying a wage differential in violation of this subsection shall not, in order to comply with the provisions of this subsection, reduce the wage rate of any employee." With the inclusion of this provision, the Equal Pay Act prescribes essentially the same requirement as that of the Minimum Wage Law—wages of certain workers must be increased.

If discrimination by the states is found to be widespread, the requirement of raising wages in the face of discrimination could lead to significantly increased costs in the dispensing of state services and could place the States in the same dilemma as that posed by the minimum wage provisions in *National League of Cities*.

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68 Id. at 6.
69 Id.
70 The FLSA provided minimum wage and maximum hour regulations to "correct labor conditions detrimental to the maintenance of the minimum standard of living for health, efficiency, and the general well-being of workers...." 29 U.S.C. § 202 (a) (1970). The Equal Pay Act also served to correct adverse conditions resulting from wage differentials based on sex such as depressed wages and living conditions, ineffective utilization of the available resources, labor disputes, the disrupted flow of goods in commerce, and the use of an unfair method of competition. See Act of June 10, 1963, Pub. L. 88-38, § 2, 77 Stat. 56 (codified at 29 U.S.C. § 206(d) (1970)).
That is, the imposition of the Equal Pay Act's sanctions could leave the states with two choices, namely "either to attempt to increase their revenue to meet the additional financial burden imposed upon them by paying congressionally prescribed wages to their existing complement of employees, or to reduce that complement" to a number which could be paid the wages received by the nondiscriminated worker. This dilemma is precisely the reason the Supreme Court held in *National League of Cities* that the power to determine wages is an attribute of state sovereignty with which federal regulation may not substantially interfere. As a result, the Equal Pay Act is also constitutionally inapplicable to the states "insofar as it operates to directly displace the states' freedom to structure integral operations. . . ." Thus, to judge the constitutionality of the EPA as applied to the states, the lower courts must employ the guidelines prescribed by the Supreme Court in *National League of Cities*.

VII. Application of the *National League of Cities*’ Guidelines to Sheboygan

A. "Traditional Operation"

Applying the *National League of Cities*’ test to the facts in *Sheboygan*, the first inquiry must be whether the Equal Pay Act is directed toward an activity which is "typical of those performed by state and local governments in discharging their dual functions of administering the public law and furnishing public services." The regulation at issue in *Sheboygan* was directed toward a public school. Thus, the first part of the test is satisfied, for it is indisputable that education is a service which governments are created to provide and which states have traditionally afforded their citizens.

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72 See Note, note 42 supra. The author therein recognizes the fact that the Equal Pay Act contains the same constitutional infirmities as the wage and hour provisions. That effect is overstated, however, by declaring the EPA an unconstitutional exercise on Congress' commerce power when applied to the states.

It is argued in the present comment that since the EPA has these similar infirmities, it must be subjected to the same tests as the minimum wage provisions. The minimum wage laws were not declared inapplicable in all situations by the decision in *National League of Cities* and the same should hold true for the EPA.

The financial impact of the EPA has been found to be quite significant. With the increase in violations found by the Wage and Hour Division beginning in 1971, this has been particularly true. For statistics on EPA judgments, see *Handbook of Labor Statistics*, U.S. Department of Labor Bulletin 1905 (1976). For a general discussion of the significance of the EPA, see Greenberger & Gutman, *Legal Remedies Beyond Title VII to Combat Sex Discrimination in Employment*, Joint Economic Committee Report (1977).

73 426 U.S. at 848. When the Court used the phrase "congressionally prescribed wages," it was referring to the minimum wage. With the Equal Pay Act as it stands, however, any wages of women which were raised in order to comply with the law should likewise be considered "congressionally prescribed wages."

74 With the minimum wage law, the states may have had to reduce their number of employees in order to comply with the minimum wage law. In the case of the Equal Pay Act, however, it is possible that any reduction in employees would be disallowed, especially if the employees released were the ones against whom the original discrimination was directed. Therefore, it may be that the only recourse left to the states would be to cut back on governmental services or somehow increase revenues.

75 426 U.S. 852.

76 Id. at 851.

77 Id. Although education was not specifically listed in the NLC opinion as in the area of traditional operations, Justice Rehnquist did point out the following in a footnote to the opinion: "These examples are obviously not an exhaustive catalogue of the numerous line and support activities which are well within the area of traditional operations of state and local operations." Id.
B. "Functions Essential to Separate and Independent Existence"

Second, whether the EPA interferes with an activity which is essential to the states' separate and independent existence must be determined. In National League of Cities, the Supreme Court decided that the power to determine wages is undoubtedly an attribute of state sovereignty and is a fundamental employment decision which is essential to the states' separate and independent existence. Since the Equal Pay Act is a wage regulation which prescribes wages, as does the Minimum Wage Law, when a violation of the act has been found an interference with a fundamental employment decision essential to the states' separate and independent existence has also occurred.

Although the Seventh Circuit was correct in maintaining that the prerogative to pay women employees unequal wages for equal work is neither a "fundamental employment decision," nor an attribute of sovereignty necessary to a separate and independent existence, the court failed to recognize that the provision requiring an increase in the wages of discriminated workers is in effect a wage regulation in the same sense as the minimum wage law.

If the Equal Pay Act allowed the states to equalize the wages of men and women by lowering the wages of men and raising the wages of women in order to avoid budgetary pressures, then the argument that the EPA prescribes wages would be lost. If such flexibility were allowed, there would be no interference with a state's decision on the amount of funds it allocates to employee wages. In such cases, the Act's only effect would be to eliminate discrimination. It would not produce a budgetary squeeze upon the states which would lead to the dilemma prohibited by the Court in National League of Cities.

C. Displacement of State Policies

Third, in an effort to evaluate the applicability of the EPA in Sheboygan, it must be determined whether the regulation displaces the City's policies regarding the manner in which it will provide education to its citizens.

In a footnote, the Sheboygan court states:

While the City must suffer increased costs as a result of complying with the EPA it may not lower wages paid to men to comply with the Act, 29 USC § 206 (d) (1), the effect of that impact is minimal when compared to the potential costs in the minimum wage and overtime provisions. Furthermore, we cannot ignore the fact that the City has not alleged that it will have to raise taxes, or, alternatively, release employees to comply with the EPA.

By stating that the impact would be minimal when compared with the minimum wage and overtime provisions, the Seventh Circuit oversimplified the financial impact of the EPA.

78 Id. at 845.
79 Id.
80 Id. at 851.
81 See note 74 supra.
82 577 F.2d at 6.
83 Id. n.18.
The Supreme Court in *National League of Cities* did not specify what degree of impact would constitute a significant alteration or displacement of the states' ability to structure employer-employee relationships. Nor did the Court confine its decision to require a degree of impact similar in magnitude to that of the minimum wage and overtime provisions. Rather, the Court intended future cases to be decided on an ad hoc basis, with the lower courts assessing the financial impact under a particular fact setting and then judging whether it "appears likely" that the impact will "significantly alter or displace the states' abilities to structure employer-employee relationships" in areas of traditional operations. Without such a finding by the trial court, the issue of whether the tenth amendment limitation on the Commerce Clause power applies to the EPA under the facts of this case could not be determined by the Seventh Circuit.

D. Balancing Test

Had the facts indicated that the EPA appeared likely to substantially affect the City of Sheboygan's integral operations, the analysis would then have been directed toward the qualifier to the principle test—the balancing test.

The Court in *National League of Cities* did not doubt the "salutary" results of the minimum wage and hour provisions. The Court refused, however, to accept the exploitation of labor as a sufficient federal interest to allow any interference with state sovereignty. Since the EPA sought to achieve relatively the same goals as the Minimum Wage Law, arguably, the purpose of the EPA also will not qualify as a "demonstrably greater" federal interest. Thus, due to the special status the states enjoy pursuant to the tenth amendment when regulation is enacted pursuant to Commerce Clause powers, it may have been desirable for the Seventh Circuit to decide the question of the EPA's applicability to the states on a more certain and better-defined ground.

VIII. Section Five of the Fourteenth Amendment

The plurality opinion in *National League of Cities* avoided the question of whether Congress might affect the integral operations of state governments by exercising other constitutional powers. In a footnote, the plurality took the following stance concerning other constitutional predicates for enforcing regula-

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84 426 U.S. at 851.
85 *Id.* at 850. Although this phrase was used in reference to the hour provisions, it was a criterion the Court was using to explain its opinion as to when interference with state sovereignty is substantial.
86 *Id.* at 851.
87 See note 72 *supra* concerning the significance of the financial impact of the EPA.
88 *Id.*
89 *Id.* at 849.
90 This was the purpose behind minimum wage and hour provisions of the Fair Labor Standards Act. See note 71 *supra*.
91 See note 71 *supra*.
92 Even when viewed as an anti-discrimination measure, the *National League of Cities* requirement as to what constitutes a "demonstrably greater" federal interest is not satisfied: That is, discrimination in pay scales cannot be said to threaten "the well-being of all the component parts of our federal system." 426 U.S. at 851.
ition against the states and their political subdivisions: "We express no view as to whether different results might obtain if Congress seeks to affect integral operations of state governments by exercising authority granted it under other sections of the Constitution such as the spending power, Art. 1, § 8, cl. 1, or § 5 of the Fourteenth Amendment."\textsuperscript{93}

The fourteenth amendment seeks to assure equal protection of the laws and to prevent deprivation of life, liberty, and property.\textsuperscript{94} Section five of the fourteenth amendment provides: "The Congress shall have power to enforce, by appropriate legislation, the provisions of this article." The fourteenth amendment's substantive provisions embody significant limitations on state authority. As the Supreme Court noted in \textit{Ex Parte Virginia},\textsuperscript{95} "the prohibitions of the Fourteenth Amendment are directed to the States, and they are to a degree restrictions of State power. It is these which Congress is empowered to enforce. . . . Such enforcement is not invasion of State Sovereignty."\textsuperscript{96}

Since \textit{Ex Parte Virginia}, the Court has sanctioned intrusions by Congress into spheres of autonomy previously reserved to the states.\textsuperscript{97} The trend recently culminated in a decision rendered four days after \textit{National League of Cities}. In \textit{Fitzpatrick v. Bitzer},\textsuperscript{98} the Court upheld the constitutionality of Title VII's prohibition against sex discrimination as applied to state and local governments. The decision granted Congress the authority to abrogate a state's sovereignty, despite the shield of the eleventh amendment, which prohibits federal court suits against states by citizens of other states.

Unlike the minimum wage and hour provisions of the FLSA, the EPA is also an anti-discrimination measure. Since the EPA serves the same fundamental purpose as Title VII of the Civil Rights Act of 1964,\textsuperscript{99} it has been held that the EPA should not be given a narrower reading.\textsuperscript{100}

Although the Court in \textit{Fitzpatrick} specifically dealt with only the interrelationship of the fourteenth and eleventh amendments, its rationale has been found to apply equally to the interaction of the fourteenth and tenth amendments.\textsuperscript{101} Several courts have cited \textit{Fitzpatrick} in holding that the Equal Pay Act should be excluded from any limitation on congressional power imposed by \textit{National League of Cities}.\textsuperscript{102}

\textsuperscript{93} \textit{Id.} at 852 n.17.
\textsuperscript{94} "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; . . . ." \textit{U.S. Const.} amend. XIV, § 1.
\textsuperscript{95} 100 U.S. 339 (1879).
\textsuperscript{96} \textit{Id.} at 346.
\textsuperscript{98} 427 U.S. 445 (1976).
In *Usery v. Allegheny County Institution District*, the Third Circuit held:

Expressly referring to *National League of Cities*, at 453, 96 S. Ct. at 2670 n.9, the Court made it perfectly clear (1) that Congress has § 5 Fourteenth Amendment power to prohibit sex discrimination in employment, and (2) that such power, despite the Tenth Amendment, extends to the state as an employer. Thus there is a clear constitutional justification for the Equal Pay Act.

The fact that the EPA was not passed pursuant to the fourteenth amendment does not bar the use of that amendment as justification for the application of the EPA to the states. As the Third Circuit stated in *Allegheny County*: “In exercising the power of judicial review, as distinguished from the duty of statutory interpretation, we are concerned with the actual power of the national government.” Adopting this rationale, courts have persistently found no merit in the argument that the constitutional basis for a federal law is limited to the powers enumerated in the “basis and purpose” section of the statute.

*Fitzpatrick* has provided adequate authority for holding the Equal Pay Act applicable to the states. In *Sheboygan*, the Seventh Circuit felt that it was unnecessary to consider the validity of predicating the EPA’s application to the City on fourteenth amendment grounds since it found that the Act was constitutionally applicable under the Commerce Clause. Had the court realized that the EPA suffered from the same constitutional infirmities as the Minimum Wage Law, and that it must grapple with the vague guidelines provided in *National League of Cities*, it might have decided *Sheboygan* on more definitive fourteenth amendment grounds.

**IX. Conclusion**

The Equal Pay Act, as applied to the states, is a constitutional exercise of congressional power under section five of the fourteenth amendment. No such assertion can be made, however, regarding the constitutionality of the EPA as an exercise of Congress’ commerce power.

In *Marshall v. City of Sheboygan*, the Seventh Circuit erroneously stated that the Equal Pay Act, as applied to the states, was not prohibited by the tenth amendment restriction on the Commerce Clause. The Seventh Circuit’s failure to recognize that the EPA could suffer from the same constitutional infirmities as
the Minimum Wage Law led to the court's failure to apply the test implicit in *National League of Cities v. Usery*. Had the court applied the standards of *National League of Cities*, it would have realized that the findings in the trial court below were insufficient to reach a conclusion on the constitutionality of the application of the EPA to the states as a Commerce Clause regulation.

The test provided by the Supreme Court in *National League of Cities* should be applied on a case-by-case basis in an effort to determine the constitutionality of any Commerce Clause regulation when such a regulation is to be applied to the states or their political subdivisions. A court, therefore, faced with a case involving a Commerce Clause regulation which is being applied to the states, must limit the holding to the particular facts in the case. Any broad holding, such as that handed down by the Seventh Circuit in *Marshall v. City of Sheboyan*, is clearly unwarranted.

Given the vague guidelines provided in *National League of Cities*, courts should decide issues involving the application of the Equal Pay Act to the states on the basis of section five of the fourteenth amendment. Such an approach would enable the courts to avoid both the time and confusion involved with the application of the standards in *National League of Cities*. Interpretation of the principles of *National League of Cities* should be left to cases within its purview. *Marshall v. City of Sheboyan* was not one of these cases.

*Frederick H. Kopko, Jr.*
Due Process—A Prisoner Who Has Successfully Appealed a First Conviction May Not Be Given a Harsher Sentence Upon Reconviction Without Valid Justification.

United States v. Tucker*

I. Introduction

In United States v. Tucker,¹ the Court of Appeals for the Seventh Circuit was presented with a significant question concerning the maximum penalty that can be levied against a criminal defendant who has successfully appealed a previous conviction for the same offense. The defendant asserted that his constitutional rights had been violated because his second sentence was actually more severe than the first. In response, the court concluded that Tucker's second sentence did not comply with minimal requirements of due process.

In North Carolina v. Pearce,² the Supreme Court held that a sentencing court may not impose a penalty which is more severe than one given before a successful appeal unless the reasons for the added punishment affirmatively appear on the record. These reasons, moreover, are to “be based upon objective information concerning identifiable conduct on the part of the defendant occurring after the time of the original sentencing proceeding.”³ The Seventh Circuit claimed that the justifications given for the added punishment in the instant case failed the Pearce test.

Although the Tucker result properly reflects current legal precedent, the case does raise three intriguing issues: (1) the definition of “sentence” in cases of this nature; (2) the “quality” of the penalty imposed; and (3) the possibility that harsher resentencing following a successful appeal should be proscribed altogether.

II. Statement of the Case

On February 19, 1976, Howard Tucker was convicted at a bench trial of a narcotics offense and received a sentence of probation for five years. The Seventh Circuit reversed the conviction, however, on the grounds that the district court had committed error by refusing to compel the government to disclose the identity of a confidential informant who had given information against the defendant.⁴ The action was remanded for retrial and Tucker was again convicted after a jury trial presided over by a different judge. The second sentence consisted of a five-year probation period, a special condition that Tucker spend ninety days at a correctional institution on a work release program, and a three-

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* 581 F.2d 602 (7th Cir. 1978).
1 581 F.2d 602 (7th Cir. 1978).
3 Id. at 726.
4 United States v. Tucker, 552 F.2d 202 (7th Cir. 1977).
year mandatory parole term to follow probation.

The second sentencing court gave the following reasons for the imposition of the more severe sentence: (1) the evidence at the second trial was more convincing than that at the first; (2) the second conviction was rendered by a jury, whereas the first trial had been before the court; (3) the Seventh Circuit questioned the sufficiency of the evidence when considering Tucker's first appeal; (4) Tucker had obtained a divorce since his first sentencing; and (5) the defendant had been unemployed for five months after his initial sentence proceeding.\(^5\)

Tucker's appeal from this second conviction set forth a single constitutionally premised argument which questioned the second trial court's authority to impose a more severe sentence upon reconviction.\(^6\) Tucker contended that the reasons offered as justification for the more severe second sentence were insufficient to satisfy the due process requirement of the fifth amendment. Normally due process is satisfied in these circumstances only if such a resentence is based on defendant misconduct which occurs after the original sentencing.\(^7\) The Tucker court held that the reasons articulated by the second judge constituted no more than a subjective assessment of Tucker's behavior and did not indicate reprehensible conduct sufficient to support the harsher sentence.\(^8\)

III. Application of the Pearce Standard

The Supreme Court addressed the propriety of imposing harsher sentences upon retrial in North Carolina v. Pearce, which consolidated two cases, both of which involved convicted defendants sentenced to prison. In each situation, the original conviction had been set aside and, after reconviction, each defendant had been given a sentence which exceeded the one originally imposed. No justification was given for the imposition of the longer sentence in either case.

In addressing these circumstances, the Pearce court explained that the due process clause of the fourteenth amendment requires that vindictiveness against a defendant who has successfully attacked his first conviction must play no part in the sentence imposed after retrial. Pearce evinced a conviction that a defendant must not be deterred from exercising his right to appeal by apprehension of potential retaliation in the form of an increased sentence from the second trial judge. Accordingly, to prevent such judicial abuse, Pearce required that the reasons for the added punishment be based upon the conduct of the defendant occurring after the initial sentencing. Furthermore, the Court held that "factual data upon which the increased sentence is based must be made part of the record, so that the constitutional legitimacy of the increased sentence may be fully reviewed on appeal."\(^9\)

The Seventh Circuit concluded that the justifications articulated by the second sentencing court in Tucker did not adequately support the harsher sentence.

\(^5\) 581 F.2d at 604.
\(^6\) Brief for Appellant at 1, United States v. Tucker, 581 F.2d 602 (7th Cir. 1978).
\(^7\) 395 U.S. at 726.
\(^8\) 581 F.2d at 607.
\(^9\) 395 U.S. at 726.
sentence. The first three reasons amounted to nothing more than subjective assessments by the court and thus failed to meet the requirement of *Pearce* that such reasons be based upon “objective information.” The fourth and fifth reasons—Tucker’s divorce and period of unemployment—were determined insufficient to indicate such “reprehensible conduct on the part of the defendant that [would call] for imposition of a harsher sentence in light of *Pearce*.”

IV. Definition of “Sentence”

Tucker was convicted at both trials of willful and knowing distribution of heroin in violation of 21 U.S.C. § 841(a)(1) (1970). Paragraph (b) of § 841, which provides for sentencing in such cases, states that a special parole term of at least three years must accompany any term of imprisonment imposed by the court. A subtle yet significant distinction existed between the two penalties imposed upon Tucker by the two courts. In the first trial the court never “sentenced” Tucker to a term of imprisonment. Thus, the § 841(b) requirement that a three-year term of probation follow such a penalty did not apply since no “sentence” of imprisonment was imposed. In the second situation, however, the court imposed a five-year prison term and then suspended its execution. Imposing a definite period of imprisonment and then suspending execution of the sentence is a “sentence” for the purpose of invoking a statutorily prescribed parole period. Under these circumstances, the mandatory parole period was deemed to apply even though the defendant was not required to spend time incarcerated.

The *Pearce* principle, as applied in *Tucker*, proscribed a harsher sentence upon reconviction. Significantly, the second trial court imposed the invalid penalty because it considered itself under a statutory mandate to reach such a result under its method of sentencing, namely, suspending execution of a prison sentence. *Pearce*, however, can proscribe not only the more severe penalty itself but also the manner in which it is imposed. A method of sentencing, although normally acceptable, is invalid to the extent that it results in an unconstitutionally severe punishment. Thus, sentencing options which are normally available to a trial judge might be removed if a more severe sentence results under conditions...

10 581 F.2d at 607.
11 Comprehensive Drug Abuse Prevention and Control Act of 1970 (Controlled Substances Act) § 704, 21 U.S.C. § 841(a) (1) (1970) [hereinafter cited as Controlled Substances Act] reads in relevant part: “It shall be unlawful for any person knowingly or intentionally (1) to manufacture, distribute, or dispense, or possess with intent to manufacture, distribute, or dispense, a controlled substance. . . .”
13 Controlled Substances Act, 21 U.S.C. § 841(b)(1)(A) (1970) provides in pertinent part: “Any sentence imposing a term of imprisonment under this paragraph shall, in the absence of such a prior conviction, impose a special parole term of at least 3 years in addition to such term of imprisonment. . . .”
14 The first sentencing judge suspended imposition of Tucker’s sentence in favor of imposing a five-year term of probation, 552 F.2d at 204 n.1. According to Zaroogian v. United States, 367 F.2d 959, 963 (1st Cir. 1966), suspending imposition of a sentence and placing the defendant on probation renders the sentence void.
15 Brief for Appellant at 21, United States v. Tucker, 581 F.2d 602 (7th Cir. 1978).
which violate the *Pearce* standard.\textsuperscript{17}

Cases considering the propriety of imposing a more severe sentence upon reconviction have always involved increased periods of incarceration.\textsuperscript{18} The sentences involved in *Tucker*, however, are unique because they bring into consideration the nature, purpose, and physical conditions of incarceration—the quality of the sentence—as well as the length or quantity of the sentence. The potential effects which the quality of a sentence might have upon a determination of severity merits further analysis.

V. Quality Versus Quantity of Sentence\textsuperscript{19}

In concluding that the second sentence imposed upon Tucker—five years probation with execution of all but ninety days suspended and a three-year mandatory parole to follow—was more severe than the first—five years probation—the court looked merely to the addition of the three-year parole term. This additional term did make the second sentence more severe in terms of restricting the defendant, but the court might also have addressed the nature and purpose of the sentence. For example, had the three-year parole term not been added to the second sentence, the court could still have declared the second sentence more severe because it required Tucker to spend ninety days of the five-year sentence on a work release program at a correction center. By the terms of the first sentence,\textsuperscript{20} the comparable ninety-day period would be spent on probation.\textsuperscript{21}

Many alternate sentences are available to a sentencing authority. Among the alternatives are imprisonment, assignment to a work release center, and probation. In evaluating the severity of a sentence, the quality of the penalty might be as significant as the quantity. For example, important differences regarding the treatment of convicts exist between prison and work release programs. Theoretically, rehabilitation is an important goal of incarceration. Nonetheless, the treatment potential of inmates is widely considered to be minimal. In fact, prisons have been described as "useless for any purpose other than locking away persons who are too dangerous to be allowed at large in free society."\textsuperscript{22}

Work release programs, conversely, are rehabilitative tools designed to bridge...
the gap between the isolated prison environment and the real world. They assist the convict in learning job skills, earning money, and preparing for life after release. In weighing the severity of sentences, it would be serious error for the court to compare imprisonment and work release on no basis other than duration because the quality of confinement in prison renders it more severe than confinement in a work release unit, due to the nature and purpose of the incarceration. Similarly, a work release sentence may be considered more severe than a sentence to probation of the same length because no confinement is required of a person on probation.

Presently, no defendant has challenged the severity of a resentence solely upon quality, although such a claim may be forthcoming: Pearce rests upon the assumption that fear of an increased sentence must not be allowed to deter a convict from the right to appeal. The quality of a sentence, however, may increase its severity without lengthening its duration. The courts, therefore, should be prepared to determine the effect of such an argument upon the Pearce principle.

VI. The Question of Harsher Resentencing

Prior to North Carolina v. Pearce, a controversy existed as to the constitutionality of harsher resentencing after a successful appeal. In Patton v. North Carolina, for example, the Fourth Circuit held that the practice was unconditionally invalid. By the time Tucker was litigated, however, Pearce had settled the issue by permitting a heavier penalty when the reasons for the added punishment affirmatively appear on the record. Pearce explicitly required that the factual basis for the higher sentence “be made part of the record.” The holding in Pearce, however, did not order the second sentencing judge to state his reasons on the record for imposing a higher sentence. The Tucker court, relying on subsequent judicial interpretation of the Pearce rule, required that the second sentencing judge must himself articulate the reasons for his conclusion that a harsher sentence is necessary. In this manner, Tucker extended the minimum protection afforded a defendant.

Tucker cannot be analyzed properly unless the Pearce standard is also reexamined. There are two important reasons for such an inquiry. First, the wisdom of Pearce must be reconsidered in its delineation of the minimal constitutional requirements for resentencing. Second, Tucker should have required added protection for defendants by prohibiting harsher resentencing entirely.

24 381 F.2d 636 (4th Cir. 1967).
25 See text accompanying note 3 supra.
26 395 U.S. at 726.
27 581 F.2d at 605.
28 See, e.g., Jackson v. Justices of Super. Ct. of Mass., 549 F.2d 215 (1st Cir. 1977); United States v. McDuffie, 542 F.2d 236 (5th Cir. 1976); Jones v. United States, 538 F.2d 1346 (8th Cir. 1976).
29 See text accompanying notes 39-53 infra for a discussion regarding the constitutional grounds. See, e.g., Mallory v. United States, 354 U.S. 449 (1957) and McNabb v. United States, 318 U.S. 332 (1943), which applied standards stricter than those mandated by the Constitution. There, as a matter of judicial policy, confessions were held inadmissible in federal courts if obtained while a suspect is being held in violation of the “speedy arraignment” provisions of Fed. R. Crim. P. 5(a).
The propriety of harsher resentencing has usually been defended on three grounds.30 First, it is asserted that a successful collateral attack upon the prior conviction "voids" both the previous sentence and conviction.31 Thus, no penalty exists with which the second sentence can be compared. This proposition has also been stated in terms of "waiver," a defendant who seeks a new trial waives any benefit he may have had from the prior sentence and conviction.32

Although this principle may have some merit in avoiding a plea of double jeopardy by a defendant who has successfully attacked a prior conviction and wishes not to be retried, it does not justify the imposition of harsher resentencing. Characterizing the entire trial proceeding as void unfairly benefits the prosecution even though the latter's error necessitated the new trial. A defendant who attacks his or her conviction does so on specific grounds, and the theory that such an appellant consciously chooses to waive any effect that the previous sentence may have had in setting a maximum limit on his penalty is pure fiction. If more severe resentences are to be permitted, the rationale should rest on a more realistic basis.

The second justification offered is that the possibility of a harsher second sentence is a deterrent to frivolous appeals.33 Prisoners might flood the courts with petitions for retrial if they are not restrained by the possibility of receiving more severe sentences.

Proponents of this position assume that the possibility of a harsher sentence will discourage only petitioners lacking meritorious claims from appealing and that innocent convicts will not be deterred. Yet the bulk of harsher resentences are likely given to petitioners with meritorious claims because those with frivolous appeals are subject to summary dismissal and thus are usually not retried. A policy allowing harsher resentencing, therefore, results in punishment for precisely that group which it does not wish to deter.34 Accordingly, the assumption that only
frivolous appeals are deterred hardly seems justified. Thus, the Pearce holding, emphasizing the fact that the fourteenth amendment forbids the deterrence of valid appeals by fear of higher penalties, eradicates this justification.

The third rationale concerns the freedom of a sentencing court to consider the defendant’s conduct subsequent to the first conviction in designing a punishment that suits the individualized needs of the offender. A ceiling on the sentencing authority, it is said, would interfere with the modern concept that a sentence should fit the offender and not merely the crime.

The validity of this argument is questionable, even if the underlying assumption is accurate, because the government already has adequate alternatives available to increase a defendant's punishment due to behavior occurring after the original sentencing. If the conduct is criminal, the convict can be retried for the new offense. If not, other penalties exist such as loss of good behavior time, adverse consideration of parole possibilities, or revocation of probation. Thus, the Pearce rule, which sanctions the imposition of more severe sentences in appropriate circumstances, gives the court far more discretion than is needed simply to fashion penalties appropriate to the defendant’s conduct subsequent to the original sentencing.

An analysis of the grounds commonly offered as justification for harsher resentencing indicates that none of these societal interests justify the intimidating effect harsher resentencing might have upon a convict’s right to appeal. The “waiver” concept is merely a legal fiction used to justify increased penalties and its demise would not compromise any public policy. The interest to society in deterring frivolous appeals may be attained by summarily disposing of such appeals. This procedure is less likely to intimidate valid claims for postconviction relief. Finally, the availability of numerous options for dealing with a defendant's behavior occurring after the original sentencing render the Pearce option unnecessary. Furthermore, although the Pearce rule, which, as adopted by the Seventh Circuit, places the burden on the sentencing judge to prove lack of vindictiveness by stating affirmatively his reasons for increasing a sentence, the opportunity for unfairness still exists.

Thus, no need for the Pearce option exists in dealing with retried defendants, and, in addition, a defendant might be treated unfairly because of the rule. As a result, the Seventh Circuit would stand on solid ground if, for policy or constitutional reasons, it decided to prohibit harsher resentencing within its jurisdiction. Tucker did not provide an appropriate opportunity for such a radical step, since

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Your Honor, I don’t want a new trile [sic] I am afraid of more time***.
Your Honor, I know you have tried to help me and God knows I appreacate [sic] this but please sir don’t let the state re-try me if there is any way you can prevent it.

Very truly yours

381 F.2d at 639 n.7.
35 395 U.S. at 725.
37 Pearce and Tucker only allow for harsher resentencing based upon conduct occurring after the time of the original sentencing. For this reason, possible abuses that might arise if harsher resentencing was allowed based upon behavior occurring before the original sentencing will not be discussed in this comment.
the case was readily decided within current precedent. Yet, when the proper case arises, the Seventh Circuit should be prepared for an assault on Pearce.

B. A New Argument to Displace Pearce

In Patton v. North Carolina,\(^3\) the Fourth Circuit held that an increase of a defendant's punishment after the reversal of his initial conviction constituted a violation of the fourteenth amendment "in that it exacted an unconstitutional condition to the exercise of his rights to a fair trial, arbitrarily denied him the equal protection of the law, and placed him twice in jeopardy of punishment for the same offense."\(^4\) The Supreme Court's holding in North Carolina v. Pearce, however, modified Patton to the extent that such increased sentences were held to be valid under the equal protection or double jeopardy provisions of the Constitution and, in some instances, the due process clause.\(^4\)

Pearce, however, did not consider a fourth constitutional theory which, if accepted, would have led to a contrary result. The doctrine of unconstitutional conditions states that the receipt of governmental benefits cannot be conditioned upon the surrender or limitation of constitutional rights absent some recognized public interest.\(^2\) Under this concept, the individual may not be required to waive a constitutional right in exchange for the retention of some unconstitutional privilege.\(^4\)

The doctrine of unconstitutional conditions was first expounded\(^4\) in Frost & Frost Trucking Co. v. Railroad Commission,\(^4\) which involved a state statute requiring private carriers to obtain a certificate of public necessity and convenience before operating on the state highways between fixed termini. The purpose of this provision was to subject private carriers to the stricter regulations appropriate to common carriers.\(^4\) In order to prevent the potential erosion of fundamental liberties, the Supreme Court held that the state of California could not constitutionally condition the privilege to use its highways upon the surrender of the constitutional right to due process of law by affixing to the privilege an unconstitutional condition precedent that the carrier assume the burdens and duties of a common carrier against his will.

This doctrine was further developed in Speiser v. Randall\(^4\) and Griffin v. California.\(^4\) The Supreme Court in Speiser held that the receipt of a tax exemption for veterans could not be conditioned upon the surrender of the right to refrain from unconstitutional oaths pursuant to the first amendment.\(^4\) In

\(^3\) 381 F.2d 636 (4th Cir. 1967).
\(^4\) Id. at 646.
\(^4\) The doctrine of "unconstitutional conditions" was first explained in Note, Unconstitutional Conditions, 73 Harv. L. Rev. 1595 (1960). This note was cited regarding the unconstitutional conditions doctrine by the Fourth Circuit in Patton v. North Carolina, 381 F.2d at 640 n. 11, and by Van Alstyne, supra note 30, at 614.
\(^3\) Van Alstyne, supra note 30, at 616.
\(^4\) See text accompanying note 3 supra regarding due process requirements.
\(^4\) The private carriers in this case were automobiles for hire.
\(^3\) 357 U.S. 533 (1958).
\(^4\) 380 U.S. 609 (1965).
\(^4\) 357 U.S. at 529.
Griffin, the Court stated that the privilege not to have the prosecutor comment upon a defendant's refusal to testify could not be based upon the waiver of the constitutional right against self-incrimination.

Before Patton, harsher resentencing of the type in Tucker had never been explicitly held invalid under the unconstitutional conditions doctrine. In an analogous situation, however, the Supreme Court in Green v. United States declared that to make a defendant exchange his constitutional protection against a second prosecution for an offense punishable by death as the price of a successful appeal from an erroneous conviction was a violation of double jeopardy. The defendant in Green had originally been convicted of second degree murder. On appeal, Green's conviction was reversed and the case was remanded for a new trial. On remand, the defendant was tried for first degree murder under the original indictment, convicted and sentenced to death. Relying in part on the Supreme Court's reversal in Green, the Patton court challenged a more severe second sentence in terms of the doctrine of unconstitutional conditions.

The doctrine of unconstitutional conditions is applicable to the rights of defendants convicted in violation of constitutional safeguards, in the following way: (1) a defendant enjoys protection against a more severe resentence so long as he passively accepts his situation; (2) the due process clause of the fifth amendment gives a defendant a constitutional right to a fair trial but to obtain this right, the defendant has to appeal; (3) under Pearce a defendant forfeits his protection against a higher resentence the moment he appeals; (4) thus, to obtain the unconstitutional privilege against a higher resentence, a defendant has to waive his fifth amendment right to due process. The societal interests at issue clearly do not justify placing a defendant in such a dilemma.

In considering the validity of harsher resentencing, the Pearce court did not consider the Patton conclusion concerning the unconstitutional conditions doctrine. The fear of a greater sentence on retrial may prevent defendants from seeking a constitutionally proper retrial through the appellate process. Therefore, in order to protect the right to a fair trial, the Seventh Circuit, using an unconstitutional conditions justification, might have held that the original sentence must operate as a ceiling for any sentence subsequently imposed following the successful appeal and retrial of the accused for the same offense. Such a ruling would have set the stage for a decisive Supreme Court ruling on the question of whether harsher resentencing should ever be allowed.

VII. Conclusion

The right to a fundamentally fair trial is at the very core of civil liberties. In Tucker, the Seventh Circuit upheld this freedom within the parameters of existing precedent. A review of the Pearce rule, however, reveals that harsher resentencing cannot be justified under any circumstances. For this reason, the

50 Van Alstyne, supra note 30, at 617.
51 355 U.S. 184 (1957).
52 See text accompanying notes 30-38 supra, for a discussion of the societal interests involved.
53 See note 4 supra.
Seventh Circuit should in the future transcend the narrow holding of Tucker and, when the appropriate case arises, proscribe harsher resentencing within its jurisdiction. This action may be taken either on the basis of the court's right to establish federal safeguards beyond minimal constitutional requirements or by adopting the "unconstitutional conditions" doctrine.

Furthermore, a close reading of Tucker reveals two other potential issues which did not require adjudication in Tucker but are likely to generate litigation in the future. First, since the Tucker opinion did not discuss the definition of "sentence" pursuant to the Tucker facts, the Seventh Circuit did not fully clarify the fact that Pearce forbids not only certain penalties, but also certain methods of imposition of sentences. Even more significant, Tucker continues the judicial trend of viewing the severity of penalties solely in terms of quantity. With the increasing use of rehabilitative sentences such as work release programs, it is likely that a defendant will eventually raise the issue of quality of the resentence. This, however, must await future litigation.

In Tucker, the Seventh Circuit reached a result which properly reflects current legal precedent. To this extent, the decision is laudable. Yet the seeds of future controversies are apparent in the instant case. Within the foreseeable future, the Seventh Circuit may be directly confronted with the questions left unanswered by Tucker and the court should be prepared to respond in a manner which would genuinely protect the interests of the retried defendant.

Deborah L. Thomas

United States v. Board of School Commissioners*

I. Introduction

United States v. Board of School Commissioners represents the culmination of ten years of litigation involving school desegregation in Indianapolis, Indiana. Although eight years ago the district court held that the Board of School Commissioners had committed an equal protection violation which could be the basis of an intradistrict school desegregation remedy, litigation continued in search of an equal protection violation which could be the basis of an interdistrict school desegregation remedy. In 1977 the Supreme Court extended this search by remanding the case to the Seventh Circuit for further consideration in light of the Supreme Court's recent holding that proof of discriminatory intent is required to establish an equal protection violation.

II. The Indianapolis Litigation

In 1968 the United States Attorney General filed a complaint charging the Board of School Commissioners of the City of Indianapolis, Indiana, and others with racial discrimination in the assignment of students to schools within the Indianapolis Public School District (IPS).

In 1969, while this litigation was pending in the district court, the Indiana

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* 573 F.2d 400 (7th Cir. 1978).
2 332 F. Supp. at 677-78.
3 429 U.S. 1068.
5 The five district court opinions issued in United States v. Board of School Comm'rs between 1971 and 1978 are denoted Indianapolis I through V. The Seventh Circuit decision which is the subject of this comment is denoted Board of School Commissioners.
6 This action was initiated pursuant to 42 U.S.C. § 2000(c)-6(a), 6(b) (1970) (amended 1972). 332 F. Supp. at 656.

The complaint also charged the defendants with racial discrimination in the assignment of teachers. In 1968 the federal district court found racial discrimination in the assignment of teachers and ordered corrective reassignment of teachers. United States v. Board of School Comm'rs, No. IP 68-C-225 (S.D. Ind., filed Aug. 5, 1968). In 1969 three teachers instituted a class action in the circuit court of Marion County, Ind., to enjoin the involuntary reassignment of teachers. The court entered a temporary restraining order prohibiting the reassignment. The defendants removed the action to the federal district court which dissolved the temporary restraining order. Burns v. Board of School Comm'r's, 302 F. Supp. 309 (S.D. Ind. 1969), aff'd per curiam, 437 F.2d 1143 (7th Cir. 1971).
General Assembly repealed a provision of a 1961 Act which had authorized the automatic extension of the boundaries of IPS with an extension of the boundaries of the City of Indianapolis. As a result of this repeal, the boundaries of IPS no longer automatically coincided with the boundaries of the City of Indianapolis.

Sixteen days after this repeal, the General Assembly adopted the Consolidated First-Class Cities and Counties Act (Uni-Gov Act) which consolidated the governments of the "old" City of Indianapolis and surrounding Marion County (with certain exceptions) into a metropolitan city government which continues to be called the City of Indianapolis. The Uni-Gov Act expressly provided that IPS would not be affected by the expansion of the City of Indianapolis. As a result of the Uni-Gov Act and its companion legislation, IPS was confined to the area of the "old" City of Indianapolis in which approximately 98.5% of the blacks in Marion County resided in 1969.

In 1971, in Indianapolis I, the district court found racial discrimination evidenced by the gerrymandering of school attendance zones, the segregation of faculty, the use of optional attendance zones among the schools, and the pattern of school locations and construction. The court concluded that: (1) the Board of School Commissioners had practiced de jure segregation of IPS students on May 17, 1954 (the date of Brown v. Board of Education); and (2) the Board of School Commissioners had not eliminated de jure segregation of IPS students on or before May 31, 1968 (the date of the Attorney General’s complaint). The court ultimately held that the Board of School Commissioners had breached its affirmative duty to desegregate the schools within IPS, a duty imposed by Brown v. Board of Education (Brown II), and thus had denied black students in IPS the right to equal protection of the laws as guaranteed by the fourteenth amendment.

In determining the scope of a remedy for this constitutional violation, the district court considered the phenomenon of "white flight," the flight of white students from a school which accelerates as the percentage of black students in the school approaches a critical percentage known as the "tipping point."
Experts testified that the tipping point was approximately 40\%, and the court noted that the percentage of black students in IPS was already approaching that critical percentage. Statistically, a reassignment of students among the schools within IPS to desegregate the predominantly white and black schools would force each school to the tipping point and would accelerate “white flight” from IPS into the surrounding City of Indianapolis. Thus, a desegregation remedy encompassing only the schools within IPS (an intradistrict remedy) could not “[promise] realistically to work now.”

The district court observed, however, that “white flight” would be minimal if the boundaries of IPS coincided with the boundaries of the City of Indianapolis. IPS, which during the 1970-71 academic year had 100,145 enrolled students—of whom 36.5\% were black, is surrounded by ten outside school corporations within Marion County, which during the 1969-70 academic year had 73,205 enrolled students—of whom 2.62\% were black. Statistically, a transfer of students between the schools within IPS and the ten outside school corporations to desegregate the predominantly white and black schools within IPS would not force any school to the tipping point. Thus, a desegregation remedy encompassing the schools within IPS and the ten outside school corporations (an interdistrict remedy) would “[promise] realistically to work now.”

Concluding that an interdistrict remedy raised questions which should not be answered without the addition of other parties, the court retained jurisdiction for further consideration of an interdistrict remedy when other interested parties could be joined to the action.

Later in 1971, the Buckley plaintiffs (two black students) intervened in their own right and as representatives of a class consisting of all black students in IPS. The intervening plaintiffs joined as defendants additional state officials and nineteen outside school corporations (including the ten outside school corporations within Marion County). In an amended complaint, the intervening plaintiffs claimed that: (1) the Uni-Gov Act and its companion legislation (which excluded IPS from the “new” City of Indianapolis) were unconstitutional as racially discriminatory; and (2) the state and local school authorities had practiced racial discrimination in the schools within IPS and the surrounding school districts.

Two weeks after the plaintiffs’ intervention, the Board of School Commissioners joined as defendants the Metropolitan Development Commission of

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17 *Id.* at 676. In *Indianapolis II*, the district court considered additional evidence on the tipping point and concluded that the tipping point was approximately 25 to 30\%. 368 F. Supp. at 1197.

18 332 F. Supp. at 657.


20 332 F. Supp. at 678 (quoting Green v. County School Bd., 391 U.S. 430, 439 (1968)).

21 The total student enrollment and percentage of black student enrollment were calculated from figures in the court’s opinion. 332 F. Supp. at 657.

22 Only these roughly comparative statistics were given in the court’s opinion. *Id.* at 676.

23 *See* note 20 *supra*.


25 368 F. Supp. at 1195.

26 *Id.* at 1195-96.

27 503 F.2d at 73.
Marion County (Commission) and the Housing Authority of the City of Indianapolis (HACI). In a cross-complaint, the Board of School Commissioners charged the Commission and HACI with contributing to school segregation in IPS by constructing public housing projects only within IPS territory.

In 1973, while further consideration of an interdistrict remedy was pending in the district court, the Board of School Commissioners appealed *Indianapolis I*, contending that the segregation existing in the schools within IPS was *de facto* and not *de jure*. The Seventh Circuit affirmed the district court judgment, holding that the district court had properly inferred the discriminatory intent required for a finding of *de jure* segregation from the pattern of practices of the Board of School Commissioners.

Later in 1973, in *Indianapolis II*, the district court concluded that: (1) a desegregation remedy encompassing only the schools within IPS (an *intradistrict* remedy) was unworkable; (2) the practices of *de jure* segregation by the Board of School Commissioners were acts of the state; (3) the added defendant state officials had practiced *de jure* segregation within IPS by commission (racial discrimination in approving school locations) and by omission (breach of their affirmative duty to desegregate the schools within IPS, a duty imposed by *Brown II*); and (4) none of the added defendant school corporations had practiced *de jure* segregation within their respective districts.

The district court ultimately held that: (1) the state through its General Assembly has the affirmative duty to desegregate the schools within IPS and thus has the duty to devise a remedy encompassing the schools within IPS and the outside school corporations (an *interdistrict* remedy); and (2) if the General Assembly fails to fulfill its duty within a reasonable time, the district court has the duty to devise a remedy encompassing the schools within IPS and the outside school corporations (an *interdistrict* remedy). In view of these holdings, the court stated that consideration of the constitutionality of the Uni-Gov Act and its companion legislation was unnecessary. The charges brought by the Board of School Commissioners against the Commission and HACI were not taken up at this trial.

Subsequently, in 1973, in *Indianapolis III*, the district court issued a supplemental opinion consisting primarily of guidelines to be followed by the General Assembly in implementing *Indianapolis II*.

In 1974, less than a year after the district court had ordered an *interdistrict* remedy, the Supreme Court in *Milliken v. Bradley* (Milliken I) held that before a federal court can order an *interdistrict* school desegregation remedy, "it must

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28 419 F. Supp. at 182.
29 Id.
30 474 F.2d at 84.
31 Id. at 84, 89. In holding that discriminatory intent is required to establish *de jure* segregation, the Seventh Circuit correctly anticipated *Keyes v. School Dist. No. 1, Denver, Colo.*, 413 U.S. 189, 208 (1973). *See* text accompanying note 54 infra.
32 368 F. Supp. 1191.
33 Id. at 1205.
34 Id. at 1208.
35 Id. at 1223.
first be shown that there has been a constitutional violation within one district that produces a significant segregative effect in another district.37

Later in 1974, in the appeal of Indianapolis II, the Seventh Circuit reversed the district court order pertaining to a remedy encompassing schools outside the boundaries of the City of Indianapolis, vacated the order pertaining to a remedy encompassing schools within the boundaries of the City of Indianapolis, and remanded the case for further consideration in light of Milliken I.38

In 1975, in Indianapolis IV,9 the district court announced that the earlier findings that the state had practiced de jure segregation in IPS were now the law of the case.40 Amplifying these earlier findings, the court found that: (1) the Commission and HACI have had the authority to construct public housing projects within and outside IPS territory; (2) suburban Marion County has resisted the construction of public housing projects outside IPS territory; (3) HACI with the Commission's approval has constructed every public housing project within IPS territory; and (4) 98% of the public housing tenants were black and their children attended schools within IPS.41

The district court ultimately held that: (1) the General Assembly's passage of the Uni-Gov Act and its companion legislation (which excluded IPS from the "new" City of Indianapolis) breached the state's affirmative duty to eliminate de jure segregation in the schools within IPS and thus established an equal protection violation which could be the basis of a remedy encompassing the schools within IPS and the surrounding City of Indianapolis (an interdistrict remedy); and (2) the Commission's approval and HACI's construction of all public housing projects within IPS territory produced segregative effects, namely, the effects of increasing the racial disparity in residential and school populations between IPS territory and the surrounding City of Indianapolis, and thus established an equal protection violation warranting an injunction from locating additional public housing projects within IPS territory.42

In 1976, in the appeal of Indianapolis IV, the Seventh Circuit affirmed the district court order, emphasizing that the General Assembly's passage of the Uni-Gov Act and its companion legislation produced segregative interdistrict effects (the Milliken I prerequisite for an interdistrict remedy), namely, the effects of inhibiting the power of the Board of School Commissioners to desegregate the schools within IPS, and thus could be the basis of an interdistrict remedy.43

In 1977 the Supreme Court vacated the judgment of the Seventh Circuit and remanded the case to the Seventh Circuit for further consideration in light of Washington v. Davis45 and Village of Arlington Heights v. Metropolitan Housing Development Corp.46

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37 Id. at 745.
38 503 F.2d at 86.
40 Id. at 183.
41 Id. at 182.
42 Id. at 183, 186.
43 541 F.2d at 1218-21, 1224.
44 429 U.S. 1068.
45 426 U.S. 229.
46 429 U.S. 252.
III. Requiring Discriminatory Intent for Equal Protection Violations—

Davis and Arlington Heights

In Washington v. Davis, the Supreme Court announced that proof of discriminatory purpose is required to establish an equal protection violation.47 In Davis, two black men, who had been denied positions as police officers in the District of Columbia Metropolitan Police Department because they had failed a qualifying test, contended that the Department’s use of the qualifying test violated their rights under the due process clause of the fifth amendment.48 The rejected applicants based their contention on the fact that a disproportionate number of blacks failed the test.49

The District of Columbia Court of Appeals, applying Title VII60 standards to resolve this constitutional issue, held that the racially disproportionate impact, absent proof that the test adequately measured job performance, established an equal protection violation.51 The Supreme Court reversed, holding that proof of discriminatory purpose is required to establish an equal protection violation and declining to hold that the constitutional standard for adjudicating claims of invidious racial discrimination is identical to the Title VII standards.52

The Supreme Court emphasized “the basic equal protection principle that the invidious quality of a law claimed to be racially discriminatory must ultimately be traced to a racially discriminatory purpose.”53 The Court noted, for example, that in school desegregation cases, de jure segregation is distinguished from de facto segregation by “purpose or intent to segregate.”54 Thus, the disproportionate impact alone of predominately white or black schools does not establish an equal protection violation without proof of discriminatory purpose.

Attempting to clarify the relationship between discriminatory purpose and disproportionate impact, the Supreme Court made two observations. First, the racially discriminatory purpose need not be express or appear on the face of a statute.55 A statute, otherwise neutral on its face, can invidiously discriminate on the basis of race through its application.56 Second, the racially disproportionate impact of a law is not irrelevant.57 A racially discriminatory purpose can be

47 Prior to Davis, various circuits had held that proof of a racially disproportionate impact, absent some justification, established an equal protection violation. 426 U.S. at 244-45.
48 Id. at 232-33. The Davis Court noted that the due process clause of the fifth amendment contains an equal protection component. Id. at 239.
49 Id. at 233.
51 426 U.S. at 236-37.
52 Id. at 240.
53 Id. at 240 (quoting Keyes v. School Dist. No. 1, Denver, Colo., 413 U.S. at 208).
54 Id. at 241.
55 Id.
56 Id.
57 Id.
inferred if the law bears more heavily on one race than another or if the discrimination is difficult to explain on nonracial grounds.58

Less than a year after Davis, in Village of Arlington Heights v. Metropolitan Housing Development Corp.,59 the Supreme Court reaffirmed the Davis holding that proof of discriminatory purpose or intent is required to establish an equal protection violation. In Arlington Heights, Metropolitan Housing Development Corporation (MHDC) had applied to the Village for a rezoning of land from single-family to multiple-family classification in order to construct a racially integrated, low- and moderate-income housing project.60 Upon denial of the application, MHDC and three black residents claimed that the Village's rezoning denial was racially discriminatory and violated, among other things, the fourteenth amendment and the Fair Housing Act.61

The district court, ruling in favor of the Village, concluded that the rezoning denial was motivated not by racial discrimination but by a desire to protect property values and to maintain the Village's zoning plan.62 The Seventh Circuit affirmed these conclusions, but reversed the judgment, holding that the "ultimate effect" of the rezoning denial was racially discriminatory.63 The Supreme Court reversed the Seventh Circuit judgment, holding that proof of discriminatory intent or purpose is required to establish an equal protection violation, and remanded the case for further consideration of the alleged Fair Housing Act violation.64

Attempting to clarify the Davis holding, the Supreme Court maintained that the racially discriminatory purpose need not be the "dominant" or "primary" purpose but only a "motivating factor" behind the governmental decision alleged to constitute an equal protection violation.65 The determination whether a discriminatory purpose was a "motivating factor" behind a governmental decision requires an examination of a number of factors, including the impact of the decision.66 As mentioned in Davis, if the decision bears more heavily on one race than another or if a clear pattern unexplainable on nonracial grounds emerges from the impact of the decision, then discriminatory intent can be inferred from the impact.67 The Court asserted, however, that such cases are rare.68

In addition to impact, the Court identified five other, though not exclusive, factors to examine:

1. [t]he historical background of the decision . . . particularly if it reveals a series of official actions taken for invidious purposes;
2. [t]he specific sequence of events leading up to the challenged decision;

58 Id. at 242.
59 429 U.S. 252.
60 Id. at 254.
61 Id.
62 Id. at 259.
63 Id. at 254, 259-60.
64 Id. at 270-71. For the Seventh Circuit decision on the remand of Arlington Heights, see text accompanying note 110 infra.
65 429 U.S. at 265-66.
66 Id. at 266.
67 Id.
68 Id.
[3] departures from the normal procedural sequence;
[4] substantive departures . . . particularly if the factors usually considered important by the decisionmaker strongly favor a decision contrary to the one reached;
[5] the legislative or administrative history . . . especially where there are contemporary statements by members of the decisionmaking body, minutes of its meetings, or reports. 69

If an examination of these factors reveals proof that a governmental decision was motivated in part by a discriminatory purpose, then the plaintiff has satisfied the "threshold showing" for establishing an equal protection violation. 70 The burden then shifts to the defendant to prove "that the same decision would have resulted even had the impermissible purpose not been considered." 71 Thus, the establishment of an equal protection violation requires two steps: (1) a "threshold showing" and (2) the "same decision test."

IV. Circumventing the Discriminatory Intent Requirement—The Intent Standard in Board of School Commissioners

During 1976 and 1977 the Supreme Court remanded several school desegregation cases including Board of School Commissioners for further consideration in light of Davis and Arlington Heights. 72 On the remand of Board of School Commissioners, the Seventh Circuit in dicta equated the discriminatory intent requirement with a disproportionate impact requirement, a circumvention of the discriminatory intent requirement announced in Davis and partially clarified in Arlington Heights.

The Seventh Circuit maintained that Davis and Arlington Heights had not explained the type of discriminatory intent that a plaintiff must prove to constitute a prima facie case of an equal protection violation and offered two suggestions for determining discriminatory intent. 73

First, discriminatory intent is to be gleaned from government institutions and not from individual officials. 74 This suggestion is inconsistent with the Arlington Heights factors identified as probative of discriminatory intent, particularly "[t]he legislative or administrative history . . . especially where there are contemporary statements by members of the decisionmaking body, minutes of its meetings, or reports. 75

Second, discriminatory intent is to be determined by the following standard:

A presumption of segregative purpose arises when plaintiffs establish that the natural, probable, and foreseeable result of public officials' action or inaction [is] an increase or perpetuation of public school segregation. The presumption becomes proof unless defendants affirmatively [establish] that

69 Id. at 267-68.
70 Id. at 270 n.21.
71 Id.
73 573 F.2d at 412.
74 Id. at 413.
75 429 U.S. at 268.
their action or inaction [is] a consistent and resolute application of racially neutral policies.\textsuperscript{76}

This standard, however, is probative of disproportionate impact and not discriminatory intent. The inconsistency between the Board of School Commissioners standard and Arlington Heights is illustrated by the following hypothetical fact pattern.

First, assume that a school board adopts a neighborhood school policy, a policy of assigning students to the schools nearest their residence in a school district in which the white and black residential areas are segregated. Second, assume that after the school policy becomes effective, the schools in the white residential areas become predominantly white and the schools in the black residential areas become predominantly black. Third, note that a neighborhood school policy can have two plausible purposes: (1) nonracial purposes such as safety and economy in reduced transportation costs, ease in student assignment and administration, and better home-school communication; and (2) racial purposes such as segregation of white students from black students.

The first step in applying the Board of School Commissioners standard to this hypothetical is to determine whether the increase or perpetuation of school segregation was a natural, probable, and foreseeable result of this school policy. In effect, this inquiry is equivalent to asking whether the school policy produced a racially disproportionate impact. Even if the segregative effects of the school board action were not foreseeable when the school policy was adopted, the continuation of these segregative effects is a foreseeable result of school board inaction. Thus, a presumption of discriminatory intent will always arise if a racially disproportionate impact exists.

The second step in applying the Board of School Commissioners standard to this hypothetical is to determine whether the school board can affirmatively establish that its action or inaction was a consistent and resolute application of racially neutral policies. The response to this inquiry depends on whether the school board must prove that its action or inaction was: (1) not taken for racial purposes or (2) taken for nonracial purposes.

If the school board must prove that its action or inaction was not taken for racial purposes, then the school board is forced to prove a negative. “Given the extraordinary difficulty of establishing the absence of racial motivation, the presumption of segregative design is, for practical purposes, the equivalent of a conclusive presumption.”\textsuperscript{77} Thus, a presumption of discriminatory intent is equivalent to proof of discriminatory intent.

Implicit in the first interpretation of the Board of School Commissioners standard is the following reasoning: (1) a racially disproportionate impact is equivalent to a presumption of discriminatory intent; (2) a presumption of discriminatory intent is equivalent to proof of discriminatory intent; (3) therefore, a racially disproportionate impact is equivalent to proof of discriminatory intent.

\textsuperscript{76} 573 F.2d at 413 (quoting NAACP v. Lansing Bd. of Educ., 559 F.2d 1042, 1046-47 (6th Cir.), cert. denied, 434 U.S. 997 (1977), which quoted Oliver v. Michigan State Bd. of Educ., 508 F.2d 178, 182 (6th Cir. 1974)).

Thus, this first interpretation of the *Board of School Commissioners* standard disaffirms the *Arlington Heights* holding, which mandates inferring discriminatory intent from a racially disproportionate impact alone only in rare cases.78

If the school board must prove that its action or inaction was taken for non-racial purposes, then the second step in *Arlington Heights* for establishing an equal protection violation, the "same decision test," becomes redundant. In effect, proving that its action or inaction was taken for nonracial purposes is equivalent to proving that the "same decision would have resulted even had the impermissible purpose not been considered."79 Thus, proof of discriminatory intent is equivalent to proof of an equal protection violation.

Implicit in the second interpretation of the *Board of School Commissioners* standard is the following reasoning: (1) a racially disproportionate impact is equivalent to a presumption of discriminatory intent; (2) a presumption of discriminatory intent shifts the burden of the "same decision test" to the defendant; (3) therefore, a racially disproportionate impact shifts the burden of the "same decision test" to the defendant. Thus, this second interpretation of the *Board of School Commissioners* standard disaffirms the *Arlington Heights* holding, which mandates shifting the burden of the "same decision test" to the defendant only after the plaintiff has proven discriminatory intent.

Under both interpretations of the *Board of School Commissioners* standard, proof of a racially disproportionate impact shifts the burden of the "same decision test" to the defendant.80 *Arlington Heights*, however, mandates that the burden of the "same decision test" not shift to the defendant upon mere proof of a racially disproportionate impact. Instead, the plaintiff must satisfy a higher "threshold showing," proof of a racially discriminatory intent, which is to be inferred from a racially disproportionate impact alone only in rare cases.

The Seventh Circuit, however, is not alone among the circuits in proposing a standard for inferring discriminatory intent from a racially disproportionate impact alone.81 These circuits have observed that determining the "motivating factors" behind a governmental decision is an impossible burden, "for in an age when it is unfashionable for state officials to openly express racial hostility, direct evidence of overt bigotry will be impossible to find."82 To accept this statement, however, is to argue for the collapse of the distinction between *de jure* and *de facto* segregation and to invite a deluge of school desegregation litigation.

Whether the Supreme Court will allow the circuits to continue circumventing the discriminatory intent requirement in establishing equal protection viola-

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78 429 U.S. at 266.
79 Id. at 270 n.21.
80 Under the first interpretation of the *Board of School Comm'rs* standard, the burden of the "same decision test" shifts to the defendant upon application of the second step in *Arlington Heights*. Under the second interpretation of the *Board of School Comm'rs* standard, the burden of the "same decision test" shifts to the defendant upon application of the second step in the *Board of School Comm'rs* standard, making application of the second step in *Arlington Heights* redundant.
81 See, e.g., United States v. Texas Educ. Agency, 564 F.2d 162 (5th Cir. 1977), petition for rehearing denied and petition for rehearing en banc denied, 579 F.2d 910 (5th Cir. 1978); Arthur v. Nyquist, 573 F.2d 134 (2d Cir. 1978); School Dist. of Omaha v. United States, 565 F.2d 127 (8th Cir. 1977) (per curiam), cert denied, 434 U.S. 1064 (1978); 559 F.2d 1042.
82 573 F.2d at 412.
tions in school desegregation cases remains an unsettled issue. The Court's recent remand of several desegregation cases reflects a desire for further development of the discriminatory intent requirement in the lower courts before settling the issue.

V. Circumventing the Discriminatory Intent Requirement—The Implicit Holding in Board of School Commissioners

In Board of School Commissioners, the Seventh Circuit, prompted by the Supreme Court's recent holding that proof of discriminatory intent is required to establish an equal protection violation, devised a means to obtain a school desegregation remedy without proving that school authorities acted with discriminatory intent. Recognizing that residential patterns are reflected in the racial composition of an area's schools, the Seventh Circuit held that if state segregative housing practices have caused residential segregation and if the residential segregation, in turn, has caused school segregation, then the state segregative housing practices can be the basis of a school desegregation remedy. This holding implies that a school desegregation remedy can be based not only on equal protection violations by a housing authority, in which proof of discriminatory intent is required, but also on Fair Housing Act violations by a housing authority, in which proof of discriminatory intent is not required. In effect, the implicit holding in Board of School Commissioners is a circumvention of the discriminatory intent requirement announced in Davis and partially clarified in Arlington Heights.

A. Recognizing the Relationship Between School Segregation and Residential Segregation—Milliken I

Although the Supreme Court has never confronted the question whether state segregative housing practices can be the basis of a school desegregation

83 In School Dist. of Omaha, a dissent argued that the Court of Appeals which had adopted a standard for determining discriminatory intent similar to the first interpretation of the Board of School Comm'rs standard had correctly anticipated Arlington Heights. 433 U.S. at 669-71 (Brennan, J., Marshall, J., dissenting). On remand, the court of appeals reaffirmed the adoption of its earlier standard. 565 F.2d at 128. Subsequently, the Supreme Court denied certiorari. 434 U.S. 1064.

84 The Seventh Circuit remanded Board of School Comm'rs to the district court to determine whether the General Assembly, the Commission, and HACI had acted with racially discriminatory intent. 573 F.2d at 414. On remand, the district court found that the General Assembly had acted with the racially discriminatory intent and purpose of confining black students to IPS. This finding was based on an application of the factors enunciated in Arlington Heights without use of the Board of School Comm'rs standard. The district court also found that the Commission and HACI were racially motivated by the invidious purpose of keeping blacks within IPS territory. This finding was based on an application of the Board of School Comm'rs standard. United States v. Board of School Comm'rs, No. IP 68-C-225 (S.D. Ind., filed July 11, 1978).

85 573 F.2d at 409.


87 See text accompanying note 110 infra.
remedy, the Court has recognized the relationship between school segregation and residential segregation in several school desegregation cases. In *Milliken I*, the Sixth Circuit affirmed the district court's conclusions that: (1) the Detroit Board of Education and the state of Michigan had practiced *de jure* segregation in the schools within the Detroit Public School System, and (2) an *interdistrict* school desegregation remedy encompassing the schools within the City of Detroit and the surrounding metropolitan area was necessary to lessen the racial identifiability of the schools within the City of

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88 In Evans v. Buchanan, 393 F. Supp. 428 (D. Del.), aff'd, 423 U.S. 963 (1975), the Supreme Court, however, did summarily affirm a district court decision basing an *interdistrict* school desegregation remedy on eight separate interdistrict constitutional violations including four housing violations.

89 In Swann v. Charlotte-Mecklenburg Bd. of Educ., 402 U.S. 1 (1971), the Court recognized this relationship between school segregation and residential segregation. "People gravitate toward school facilities, just as schools are located in response to the needs of people. The location of schools may thus influence the patterns of residential development of a metropolitan area and have important impact on composition of inner-city neighborhoods." 402 U.S. at 20-21. The Court stated that a district court may consider residential patterns in fashioning a school desegregation remedy. 402 U.S. at 21.

The Court, however, cautioned against using school desegregation cases to "embrace all the problems of racial prejudice, even when those problems contribute to disproportionate racial concentrations in some schools." 402 U.S. at 23. "One vehicle can carry only a limited amount of baggage." 402 U.S. at 22.

(For a school desegregation case in which a circuit court heeded the warning in *Swann*, see Hart v. Community School Bd., 383 F. Supp. 699 (E.D.N.Y. 1974), aff'd, 512 F.2d 37 (2d Cir. 1975). In *Hart*, the school board impleaded city, state, and federal housing and urban development bodies and officials, charging these third-party defendants with fostering residential segregation which resulted in school segregation. After finding the school board liable, the district court "mooted" the third-party complaint but retained jurisdiction over the third-party defendants for purposes of ordering a comprehensive remedy. 383 F. Supp. at 754. The circuit court, however, recommended to the district court that it withdraw its decision to "moot" the third-party action and dismiss it. 512 F.2d at 56.)

In *Keys*, the Court again observed that school policies "may have a profound reciprocal effect on the racial composition of residential neighborhoods within a metropolitan area. . . ." 413 U.S. at 202. "[T]he familiar root cause of segregated schools in all the biracial metropolitan areas of our country is essentially the same: one of segregated residential and migratory patterns the impact of which on the racial composition of the schools was often perpetuated and rarely ameliorated by action of public school authorities."

413 U.S. at 22-23 (Powell, J., concurring in part and dissenting in part).

In *Austin Independent School Dist.*, the concurring opinion observed:

"[T]he principal cause of racial and ethnic imbalance in urban public schools across the country—North and South—is the imbalance in residential patterns. Such residential patterns are typically beyond the control of school authorities. For example, discrimination in housing—whether public or private—cannot be attributed to school authorities. Economic pressures and voluntary preferences are the primary determinants of residential patterns."


The Supreme Court reversed and remanded, holding that a federal court cannot impose an interdistrict school desegregation remedy for single-district de jure segregation violations absent significant segregative effects in the other districts. Specifically, an interdistrict school desegregation remedy is appropriate "where the racially discriminatory acts of one or more school districts caused racial segregation in an adjacent district, or where district lines have been deliberately drawn on the basis of race."

Although the district court also found that federal, state, and local governmental actions and private actions had produced the pattern of residential segregation throughout the Detroit metropolitan area, the Sixth Circuit did not rely on housing violations in affirming the district court judgment. Accordingly, Chief Justice Burger, writing for the Court, concluded that the case in its present posture did not present any question concerning possible housing violations.

Justice Stewart concurred in the majority opinion but noted that if "state officials had contributed to the separation of the races . . . by purposeful, racially discriminatory use of state housing or zoning laws, then a decree calling for transfer of pupils across district lines or for restructuring of district lines might well be appropriate." Justice Stewart concluded, however, that the facts did not show that the racial composition of the schools or that residential patterns "were in any significant measure caused by governmental activity."

Milliken I suggests that if the plaintiffs had shown that the state was "in any significant measure" responsible for the residential segregation in the Detroit metropolitan area, Justice Stewart would have voted to affirm an interdistrict school desegregation remedy based on state segregative housing practices.

B. Basing a School Desegregation Remedy on State Segregative Housing Practices—Milliken I and Milliken II

The possibility of basing a school desegregation remedy on state segregative housing practices which have caused segregation in the schools is supported by the Supreme Court's interpretation in Milliken I and Milliken v. Bradley (Milliken II) of the following remedial principle: "Once a right and a violation have been shown, the scope of a district court's equitable powers to remedy past wrongs is broad, for breadth and flexibility are inherent in equitable remedies."

Milliken II enunciated three factors for federal courts to consider in ordering a school desegregation remedy. First, "the interests of state and local authorities in managing their own affairs, consistent with the Constitution," must be considered. Second, the remedy must be related to "the condition alleged to
offend the Constitution. . . ." 103 Third, the remedy must be designed "to restore the victims of discriminatory conduct to the position they would have occupied in the absence of such conduct." 104

In ordering a school desegregation remedy based on state segregative housing practices, a federal court will encounter no theoretical difficulty with the first and second factors, but will encounter practical difficulty with the third factor.

First, such an order will not impermissibly interfere with school districts in managing their own affairs. The Milliken I holding that an interdistrict school desegregation remedy is appropriate (a permissible interference) when the acts of one school district (an instrumentality of the state) produce significant segregative effects in surrounding school districts (instrumentalities of the state) indicates that a school desegregation remedy might also be appropriate (a permissible interference) when the acts of a housing authority (an instrumentality of the state) produce significant segregative effects in surrounding school districts (instrumentalities of the state). 105 In each case the surrounding school districts are ordered to participate in a remedy of the constitutional violations of either another school district or a housing authority. The identity of the instrumentalities of the state that committed the constitutional violations will not alter the permissible interference of the order on the school districts in managing their own affairs.

Second, the order is related to a condition which offends the Constitution, for school segregation caused by an instrumentality of the state (a school district or a housing authority) is a condition which offends the Constitution. 106

Third, whether the order can be limited to remedying the incremental segregative effect of housing violations on the racial composition of the schools in the presence of the violations, compared to the racial composition of the schools in the absence of the violations, depends on the quality of the available evidence. 107 The court must not only determine the number of persons affected by the housing violations but also estimate the number of students among those persons affected by the housing violations. A court might find itself incapable or unwilling to formulate such an estimate.

Thus, Milliken I and Milliken II suggest that a school desegregation remedy based on state segregative housing practices is a theoretical possibility but not a practical possibility.

103 Id. at 280 (quoting Milliken I, 418 U.S. at 738).
104 Id. at 280 (quoting Milliken I, 418 U.S. at 746).
105 For clarification of a permissible interference, see Hills v. Gautreaux, 425 U.S. 284 (1976). In Hills, the Court distinguished Milliken I, affirming the Seventh Circuit's authorization of a metropolitan area remedy for racial discrimination in housing practices within the City of Chicago without a showing of significant segregative effects in the suburbs. Justice Stewart, speaking for the Court, maintained that ordering the Department of Housing and Urban Development to create housing alternatives in the suburbs would be commensurate with the nature and extent of the constitutional violation and would not impermissibly interfere with local governments and suburban housing authorities.
106 347 U.S. 483.
C. Defining State Segregative Housing Practices—Board of School Commissioners

In *Board of School Commissioners*, the Seventh Circuit held that state segregative housing practices can be the basis of a school desegregation remedy, but the court did not explicitly define the violations established by “state segregative housing practices.” Implicit in this holding is the potential for obtaining a school desegregation remedy without proving that either school or housing authorities acted with discriminatory intent.

Clearly, “state segregative housing practices” can establish equal protection violations, for that was the issue in *Board of School Commissioners*.

The Seventh Circuit, however, intended “state segregative housing practices” to establish other housing violations:

> *It does not matter whether HACI itself had a discriminatory intent* in limiting public housing to IPS or whether the suburbs with discriminatory intent refused to cooperate, thus preventing HACI from expanding public housing projects beyond the IPS boundary. The result was the same and HACI, as a public agency, should not be free from an injunctive order merely because its conduct was forced from the outside.\(^{108}\)

The court is not referring to an equal protection violation, for proof of discriminatory intent is required to establish an equal protection violation. The court, however, might be referring to a Fair Housing Act\(^ {109}\) violation.

On the remand of *Arlington Heights*, the Seventh Circuit held that a Fair Housing Act violation can be established by a showing of discriminatory effect without a showing of discriminatory intent.\(^ {110}\) A Fair Housing Act violation can produce significant segregative effects in a school district identical to those resulting from an equal protection violation. The Fair Housing Act violation can be the basis of a housing remedy, but can it also be the basis of a school remedy? The answer depends on whether the constitutional and statutory standards applicable in cases of racial discrimination can coexist, namely, whether proof of discriminatory intent is required for constitutional adjudications but not for statutory adjudications of racial discrimination.

VI. Conclusion

In *Board of School Commissioners*, the Seventh Circuit, searching for an equal protection violation which could be the basis of an interdistrict school desegregation remedy, circumvented the Supreme Court’s recent holding that proof of discriminatory intent is required to establish an equal protection violation.

First, the *Board of School Commissioners* standard for determining discriminatory intent equated the discriminatory intent requirement with a disproportionate impact requirement.

\(^{108}\) 573 F.2d at 414 n.34 (emphasis added).


Second, the Seventh Circuit held that state segregative housing practices can be the basis of a school desegregation remedy. If the practices are intended to establish equal protection violations, the plaintiff must prove discriminatory intent on the part of housing authorities; however, if the practices are intended to establish Fair Housing Act violations, the plaintiff need not prove discriminatory intent on the part of any instrumentality of the state.

Thus, this twofold circumvention of the discriminatory intent requirement reflects the Seventh Circuit’s determination to remedy the racially discriminatory effects of governmental action or inaction—whether or not ultimately traced to a racially discriminatory intent.

*Diane L. Wolf*
First Amendment—Freedom of Speech—Request for Injunction to Prohibit Nazi March in Jewish Community Denied.

Frank Collin and the National Socialist Party of America v. Albert Smith and the Village of Skokie, Illinois*

I. Introduction

In Collin v. Smith the Seventh Circuit undertook to decide whether municipal ordinances adopted by the Village of Skokie, Illinois, were constitutionally acceptable restrictions upon the right of the pro-Nazi National Socialist Party of America to demonstrate upon the public sidewalk in Skokie. This determination required the court to consider the status of the right of free speech when it clashes with other rights or values.

Protection of individual liberties was a founding principle in America’s constitutional system of government, and continues to be a highly respected value.1 The concept of individual liberty is itself rather intangible. Historically, this concept reflects a desire to protect the rights of individual citizens to live peacefully and worship freely without government encroachment.2 In order to preserve this freedom, the right to participate in certain activities is guaranteed to the people in the first amendment of the Bill of Rights. These rights, among them the right to speak freely, to assemble, and to petition the government for redress of grievances, guarantee a voice to the people to protect their freedom and liberty from oppressive government interference.

The climate in which the Seventh Circuit decided Collin merits special consideration. The nature of the Nazi/Jewish confrontation brought immediate national attention to the planned demonstration and the efforts of the Jewish community to prevent it. This publicity not only emphasized the emotional nature of the conflict, but compounded the impact of the march upon the residents of Skokie. In addition, the national attention which focused upon the eminent decision of the Seventh Circuit escalated the natural pressures already inherent in the resolution of the first amendment issue.

In the final analysis, the Seventh Circuit found the Village ordinances to constitute an undue and thus unconstitutional burden upon protected speech. Well-established principles of law, born of landmark cases in the area of free speech, were cited to justify and buttress the court’s conclusion. The impact of this decision is a solid reaffirmation of traditional principles of free speech. These principles proclaim that “freedom to think as you will and speak as you think are means indistinguishable to the discovery and spread of political truth; that with-

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* 578 F.2d 1197 (7th Cir.), cert. denied, 47 U.S.L.W. 3264 (Oct. 16, 1978).
1 An initial understanding of the purpose of first amendment guarantees is essential before analyzing the NSPA’s status. If the purpose of protecting free speech is forgotten, the focus of protection shifts to the action of speaking, and the principles that free speech is meant to preserve are abandoned. In short, it is not speech itself which is sacred, but the underlying values which freedom of speech exists to protect.
out free speech and assembly discussion would be futile; that with them discussion affords ordinarily adequate protection against the dissemination of noxious doctrine. A close examination of Collin reveals, however, that dissemination of such noxious doctrine may raise some additional constitutional problems that are worthy of discussion. These questions focus upon the interrelationship of free speech, the rights of those who are targets of that speech, and the rights of a government to protect those rights on behalf of its citizens.

II. Development of the Issue: the Factual Setting

On March 20, 1977, the president of the National Socialist Party of America (NSPA), Frank Collin, announced that the Nazi-based organization planned to demonstrate on May 1 in front of the City Hall of Skokie, Illinois. Skokie is a predominantly Jewish suburb of Chicago. The NSPA planned to wear full military uniforms with swastika armbands and flags and to carry placards with prowhite slogans. The demonstration was planned as a peaceful exercise of 30-50 demonstrators and no speeches were to be made.

The news that the Nazi group planned to march in downtown Skokie evoked immediate response from Village residents. Many residents had themselves been prisoners of war during the height of the Nazi regime or had lost personal family members in the holocaust. Thus, the presence of proclaimed Nazis and display of the swastika, the symbol of Nazi principles, were particularly offensive, if not threatening to them. To add to the general furor, some Jewish members of the community began to receive harassing or threatening phone calls, and handbills announcing the proposed march began to circulate throughout the Village.

On April 28, 1977, the Village of Skokie filed a complaint in the Circuit Court of Cook County asking that an injunction be issued to prevent the NSPA from marching in Skokie on May 1. The injunction was initially granted, thus delaying the demonstration, but was later removed in full.

Appeal to the Illinois Supreme Court also resulted in denial of the stay. The NSPA appealed directly to the Supreme Court Justice for the Seventh Circuit, Justice John Paul Stevens. Justice Stevens treated the appeal as a petition for certiorari and recommended it to the full Supreme Court for review.

On June 14, 1977, the Supreme Court reversed the Illinois Supreme Court denial of the stay and remanded the case to the Illinois state courts for granting of a stay or immediate appellate review. National Socialist Party of America v. Village of Skokie, 432 U.S. 43 (1977). The Illinois Supreme Court ordered the Illinois Appellate Court to commence expedited appellate review, or in the alternative, to grant a stay of the injunction. The Appellate Court set the case for immediate review, and on July 12 removed the injunction in part, and affirmed that part of the injunction which prohibited the display of the swastika. Village of Skokie v. National Socialist Party of America, 51 Ill. App.3d 279, 366 N.E.2d 347 (1977). Mr. Justice Stevens denied a stay of this modified injunction. 434 U.S. 1327 (1977). The affirmed portion of the decision of the Appellate Court was subsequently appealed to the Illinois Supreme Court, which found the prohibition of the swastika to be unjustified. The injunction was removed in full on January 27, 1978. Village of Skokie v. National Socialist Party of America, 69 Ill.2d 605, 373 N.E.2d 21 (1978).
While the NSPA was appealing the initial grant of the injunction, the Village of Skokie enacted three ordinances designed to regulate public parades and assemblies within the Village. The first of these regulations, Ordinance No. 775-N-994 (994) required that a permit be obtained from Village officials for all parades or public gatherings in which fifty or more people or vehicles would be involved. Issuance of the permit was subject to several requirements, including proof of insurance coverage and submission of the permit application at least 30 days prior to the planned activity. The permit could be denied if appropriate Village officials found that the assembly would "portray criminality, depravity or lack of virtue in, or incite violence, hatred, abuse or hostility toward a group of persons by reason of reference to religious, racial, ethnic, national or regional affiliation," or if the activity promoted an unlawful purpose. Failure to obtain a permit before the assembly was punishable by a fine ranging from $5 to $500.

The other two ordinances were criminal in nature. Ordinance No. 775-N-995 (995) prohibited dissemination of any printed materials which would promote hatred against others based on race, religion or national origin. Ordinance No. 775-N-996 (996) made it illegal for members of political parties to wear military-style uniforms while demonstrating within Skokie. The maximum penalty for violation of either 995 or 996 was 6 months of imprisonment and a $500 fine.

After the Village had enacted these ordinances the NSPA rescheduled their demonstration for July 4, 1977, and applied for the requisite permit. The plans submitted on the application form were essentially the same as those of the formerly proposed May 1, 1977, march.

The Village officials refused to issue the permit. They considered that the activity had an "unlawful purpose" under 994 because the NSPA intended to

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7 The power of a state to regulate can be exercised by a lesser governmental body pursuant to state grant of authority. Under the "home rule" provision of the Illinois Constitution, Skokie has plenary legislative authority to enact ordinances for the protection of the public welfare. ILL. CONST. ART. 7, § 6(a).

8 Skokie, Ill. Village Ordinance 994 27-54, provides:
   No permit shall be issued to any applicant until such applicant procures Public Liability Insurance in an amount of not less than Three Hundred Thousand Dollars ($300,000.00) and Property Damage Insurance of not less than Fifty Thousand Dollars ($50,000.00). Prior to the issuance of the permit, certificates of such insurance must be submitted to the Village Manager for verification that the company issuing such insurance is authorized to do business and write policies of insurance in the State of Illinois.

9 This requirement, contained in § 27-52 of 994, was not challenged in Collin.

10 § 27-56(c) of 994.

11 § 27-56(1) of 994.

12 The pertinent part of 995, § 28-43.1, provides: "The dissemination of any materials within the Village of Skokie which promotes and incites hatred against persons by reason of their race, national origin, or religion, and is intended to do so, is hereby prohibited."

"Dissemination of materials" is defined by § 28-43.2 to include: "publication or display or distribution of posters, signs, handbills, or writings and public display of markings and clothing of symbolic significance."

13 Section 28-42.1 of Ordinance 996 provides that: "No person shall engage in any march, walk or public demonstration as a member or on behalf of any political party while wearing a military-style uniform." A political party is defined to include any organization existing primarily to influence government or politics. § 28-42.2.
wear military uniforms in violation of 996.14

Upon denial of the permit the NSPA filed an action in the Federal District Court for the Northern District of Illinois, protesting that through the enforcement of the Skokie ordinances the members of the NSPA had been deprived of their constitutional right of free speech. The district court found that the proposed actions of the NSPA were entitled to first amendment protection and that the three ordinances were unconstitutional restrictions on the exercise of free speech.15 The Village of Skokie brought this appeal to the Seventh Circuit, arguing that the actions of the NSPA were not entitled to free speech protection and that the regulations imposed upon the demonstrators were justified by the recognized ability of a government to regulate under the police power.

III. The Collin Decision Under Existing Legal Standards

"Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the government for a redress of grievances."16 The specific language of the first amendment reflects the importance with which the enumerated rights, including the right to free speech, are regarded. These first amendment guarantees are generally recognized as fundamental rights which underlie the guarantee of liberty under the Constitution.17

When faced with a situation such as Collin that involves both legal and emotional issues, courts generally tend to strip away the emotional overtones and reduce the legal question to traditional principles. This is, in effect, what the Seventh Circuit did in Collin, breaking down the complex questions involved into several components of traditional constitutional analysis:

a) Did the actions of the NSPA constitute speech under the first amendment?

b) If the actions constitute speech, was this speech within the protection of the first amendment?

c) If the speech is within the protection of the first amendment, were the restrictions placed on the actions of the NSPA unconstitutional obstacles to exercise of this protected speech?

A. Did the actions constitute speech?

The determination by the Seventh Circuit that the activities of the NSPA were within the constitutional scope of speech rested first upon the recognition that action which has expressive value is a form of speech under the first amend-

14 The court noted that intent to violate 995 or 996 would constitute an "unlawful purpose" under 994. Refusal of the permit here, however, was based only on the intended violation of 996.


16 U.S. CONST. amend I. Although this amendment is expressly applicable to Congress, it has been held applicable to the states as well under the 14th amendment. Gitlow v. New York, 268 U.S. 652 (1925).

ment. Accepting this premise, the court scrutinized the specific actions of the NSPA and found that such expressive value existed.

In support of its decision the court relied on several Supreme Court cases in which essentially the same type of conduct as that in Collin was found to constitute speech under the first amendment. In Tinker v. Des Moines Independent Community School District the Supreme Court found that wearing a black armband to protest the Vietnam War was closely akin to pure speech and therefore worthy of first amendment protection. Similarly, cases which held display of a party flag, carrying of protest signs and marching or demonstrating to constitute speech were cited by the Collin court to support its finding that the proposed actions were indeed forms of symbolic speech.

B. Was this speech within the protection of the first amendment?

Historically, courts have not found all speech worthy of first amendment protection. Thus, some types of speech are "no essential part of any exposition of ideas and are of such slight social value as a step to truth that any benefit that may be derived from them is clearly outweighed by the social interest in order and morality." Accordingly, speech has been divided into categories of protected and nonprotected, the general rule being that all speech is protected unless it meets a specific exception. These exceptions, established through case law, include insulting or fighting words, words which incite riot, words which are offensive because of their erotic nature or obscene message, and words which constitute libel or slander of another person. Refusal of protection to these four types of speech is justified by the rationale that their use would tend to promote breach of the peace, or that they are so objectionable to the general public that their benefit is clearly outweighed by the social interests involved.

In order to reach its decision that the proposed actions of the NSPA did qualify as protected speech, the Seventh Circuit systematically found each of the four recognized exceptions inapplicable to the factual situation in Collin. The first of these, and possibly the easiest to eliminate, was obscenity. Although the court recognized that the presence of persons advocating Nazi principles and the display of Nazi uniforms and swastikas may be very offensive to the general populace of Skokie, it noted that obscenity was limited to material of an erotic or sexual nature. Since the actions of the NSPA were not subject to this type of connotation, no restriction could be allowed on this basis.

24 Id. at 571-72.
25 Id.
Both the "fighting words" exception and the "incitement to riot" exception were eliminated by the Seventh Circuit because the Village of Skokie did not express any fear of breach of the peace if the NSPA were allowed to march.\(^3\) Nonassertion of any likelihood of violence by the Village was accepted by the court as a concession that there was no imminent danger of disturbance.\(^2\) Since tendency to cause a breach of the peace is an element of both exceptions, this concession prevented the court from finding either exception applicable to the Collin situation.

The final exception eliminated by the Seventh Circuit in supporting its finding of protected speech involved libel and slander. Libel or slander of a group has not met uniform acceptance in U.S. law, but was recognized by the Supreme Court in Beauharnais v. Illinois\(^3\) in essentially the same circumstances as Collin. In Beauharnais, the Supreme Court upheld a conviction under an Illinois statute after the defendant distributed leaflets that called for the protection of white neighborhoods from negro encroachment.\(^4\)

Although Beauharnais has not been specifically overruled by the Supreme Court, the Seventh Circuit noted that the Beauharnais doctrine has been modified extensively by subsequent court decisions and thus found it inapplicable in this case.\(^5\)

C. Were the restrictions placed upon the actions of the NSPA unconstitutional obstacles to exercise of protected speech?

First amendment rights are not absolute. They are limited by coexisting rights that also deserve and demand protection.\(^6\) One of these coexisting rights is that of a government to regulate for the protection and welfare of its citizens. This right, known as police power, is rooted in the reserve powers of a state under the tenth amendment and empowers a government to preserve the public peace.\(^7\) The nature of this right is such that its exercise will often conflict with the exercise of free speech because open discussion in the public forum will inevitably cause some disruption of the public order. In reconciling these conflicting rights the courts have balanced the interests involved, weighing the social value pro-

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31 578 F.2d at 1203.
32 578 F.2d at 1204. In the dissenting opinion which accompanied the denial of certiorari in Collin, Justice Blackmun analogizes the actions of the NSPA to be in the same category as the "right" to cry "fire" in a crowded theater, 47 U.S.L.W. 3264 (Oct. 16, 1978). This statement thus seems to question the finality of such a concession.
33 343 U.S. 250 (1952).
34 The statute involved in Beauharnais was very similar to that in Collin, prohibiting portrayal of "depravity, criminality, unchastity, or lack of virtue of a class of citizens, of any race, color, creed or religion . . . which exposes the citizens . . . to contempt, derision or obloquy or which is productive of breach of the peace or riots . . . " 35 The Beauharnais decision recognized the right of a state to punish utterances directed at defined groups under criminal libel laws. Since Beauharnais was decided, however, several important libel cases have been decided which assess the constitutional status of libel. See Gertz v. Robert Welsh, Inc., 418 U.S. 323 (1974); New York Times Co. v. Sullivan, 376 U.S. 254 (1964); Garrison v. Louisiana, 379 U.S. 64 (1964). As a result, the current validity of Beauharnais may be in doubt. See Tollet v. United States, 485 F.2d 1087 (8th Cir. 1973). For general discussion, see Nowak, supra note 1, at 781.
36 Cushman, supra note 29, at 491.
37 U.S. Const. amend. X. See also Tenneco v. Lafourche, 427 F.2d 1061, cert. denied, 400 U.S. 904 (1970), as to use of police power to restrict some private rights.
tected by the government restriction against the seriousness of the threat to protected speech.

After finding that the proposed actions of the NSPA did constitute protected speech, the Collin court examined the Village ordinances one by one to see if an undue burden had been placed upon exercise of that speech. The unconstitutionality of two of the ordinance provisions, the insurance requirement of §§ 27-54 and 27-56(j) of 994 and the military uniform prohibition of 996 was conceded by the Village of Skokie. The Seventh Circuit summarily affirmed the unconstitutionality of 996, and likewise accepted the district court’s finding of unconstitutionality of the insurance requirement based on its discretionary waiver provision. The court noted that the insurance requirement itself seemed tied to control of the content of the proposed speech, in that the nature of the activity would affect the availability of the required insurance.

Restrictions which control content of protected speech have met with heavy judicial disfavor. The Supreme Court in Cohen v. California explicitly stated that protected speech could not be regulated on the basis of its message, ideas or content. This disfavor of content control is based on the realization that the purpose of the right to free speech is to ensure open and uninhibited debate on public issues and that control of the substance of discussion would effectively defeat that purpose.

Regulation of free speech has generally been allowed when limited to restrictions on “manner.” This has routinely included regulation of time, place and duration of demonstrations or parades where the city has a significant government interest in rerouting traffic or providing additional police staff. Such regulation can be accomplished by requiring that a permit be obtained prior to the activity, stating the time, location and type of the proposed demonstration, as well as number of people to be involved. The requirement of a permit fee has been upheld as a reasonable restriction designed to cover administrative expenses; however, courts are careful to ensure that the burden of acquiring the permit is not an inhibiting obstacle to the activity.

38 578 F.2d at 1207-08. See also 578 F.2d at 1208 n. 19. There was some disagreement among the Collin judges as to whether the concession was an irrevocable waiver of defense under its recent decision of Mitchell v. Archibald & Kendall, Inc. 573 F.2d 429 (7th Cir. 1978) (alternate holding). Judge Sprecher in his dissent felt that the court should consider these defenses, particularly because parties could otherwise use concession to prevent a court from addressing an important constitutional question. The majority opinion, however, finds Mitchell inapplicable and accepts the concessions.

39 Permit systems which allow exemption of certain organizations or discretionary application of the requirements of government officials are particularly vulnerable to first amendment challenges. See Shuttlesworth v. City of Birmingham, 394 U.S. 147 (1969); Hague v. C.I.O., 307 U.S. 496 (1939).

40 The court relied both on common sense and expert testimony heard in the district court in reaching its decision. 578 F.2d at 1208. The district court, in considering Collin, referred to testimony by a licensed insurance broker in Collin v. O'Malley, 452 F. Supp. 577 (1978), in which the NSPA was required to obtain $350,000 insurance coverage before a permit to march in a Chicago city park would be issued. The witness testified that a four-month search for such insurance was unsuccessful, and estimated that when and if the policy could be secured, the premium would be as much as $1,000 for each event.


allowed the permit requirement to stand once stripped of unconstitutional pre-requisites.

Consistent with this general disapproval of burdens upon speech, the Seventh Circuit found Ordinance 995, regulating dissemination of materials, unconstitutional due to overbreadth. The doctrine of overbreadth was succinctly described by Justice Harlan, who stated that “a governmental purpose to control or prevent activities subject [to] regulation may not be achieved by means which sweep unnecessarily broadly and thereby invade the area of protected freedoms.” Since the Collin court found the wording of 995 susceptible to an interpretation that would outlaw protected speech, it declared the ordinance unconstitutional.

Once ordinances 995 and 996 were declared unconstitutional, the Village could not assert intent to violate them as “portraying criminality” under § 27-56(c) of 994 or as constituting an “unlawful purpose” under § 27-56(i) of that ordinance. Since the Village’s refusal to issue a permit had been based upon intention to violate 996, this finding of unconstitutionality destroyed the justification for the permit denial. Absent this justification, the Seventh Circuit found the permit denial to constitute an undue burden upon free speech. The court therefore affirmed the district court decision enjoining the Village from either enforcing the unconstitutional ordinances against the NSPA or denying a permit based on violations thereof.

IV. Interrelationship of Coexisting Rights

Despite the court’s insistence that the decision reached was necessary to retain the meaning of civil rights, an air of something left unsaid seems to lurk behind the strong words of the court’s opinion. Although the court adamantly upheld the right to express unpopular viewpoints or to advocate beliefs and goals repugnant to the core of generally held values as being essential to realization of the high purposes of the first amendment, an underlying thread of discontent with the practical effect of its decision can be discerned. In Collin, the court stated that it “regrets the use appellees plan to make of their rights.” Certainly this statement cannot be interpreted as a desire that that expression of unpopular viewpoints should not have first amendment protection, for the court repeatedly stressed the value of such free and open exchange of ideas as a fundamental principle upon which our liberty is grounded.

The underlying discontent the court revealed focuses on the dilemma the factual reality of this case presents and highlights the problem that courts face in balancing first amendment rights against other conflicting concerns. An examination of the facts of Collin reveals the facet of the case that seems to tug on the court’s conscience. Although the actions of the NSPA could appear to be

45 For further explanation of overbreadth, see Note, The First Amendment Overbreadth Doctrine, 83 Harv. L. Rev. 844.
47 578 F.2d at 1207.
48 578 F.2d at 1210 (emphasis added).
49 See 578 F.2d at 1201, 1210.
a legitimate expression of belief, the court seemed to feel that the underlying purpose of the proposed activities was not to "communicate" in the sense of an open exchange of ideas. Rather, the planned march seemed designed to disturb the Jewish residents of Skokie and to use the Jewish character of the community as an incendiary source of national attention for the NSPA.

Use of the cloak of first amendment protection to justify actions intended to exploit the known weakness of an individual or group offends a natural sense of justice. This justice dictates that while rights can and should be used, they should not be abused, especially at the expense of other members of society. Some difficulty arises, however, in trying to determine when use becomes abuse and when abuse should result in limitation or restriction of an activity. It would logically seem that such a determination would depend on such factors as the exact nature of the activity and the extent of its effect on those who are exposed to it.

Although the court did express dissatisfaction with the use the NSPA planned to make of their right to free speech, in its final analysis the court did not consider possible abuse of speech as a factor in its decision. Instead, after finding the proposed activity to be within the aegis of protected speech, the court looked simply at whether the Village ordinances were time, place and manner restrictions and whether they were narrow enough to avoid overbreadth. It thus appears that the Seventh Circuit, while following current standards of first amendment law, was not required to consider whether speech which is intended to disturb the mental and emotional peacefulness of a group deserves full first amendment protection.

The court's nonconsideration of this possible effect of the actions of the NSPA has interesting implications. The potential for emotional distress of the Jewish residents of Skokie was apparent upon the face of the situation. Yet the court not only did not look at the reasonableness or extent of such disturbance, but also did not find the question of its existence to be significant. The regret the court expresses as to the effect of its decision suggests that the court did feel there was an interest being compromised, but that the interest had to be sacrificed in favor of the rights of free speech.

The Collin situation thus presents an excellent opportunity to examine whether, under these circumstances, or in any circumstances in which one group of citizens is victimized by the exercise of free speech by another, the right of free speech can be limited to prevent this effect. A thorough exploration of this question requires that several issues be addressed:

a) Has a right to remain free of mental or emotional abuse from the words or actions of another been judicially recognized?

b) What is the status of such a right when it comes into conflict with the exercise of free speech?

c) How can such a right be protected without undue infringement upon free speech?
A. Past Recognition of the Right

The idea that there is a right of protection from the abusive exercise of speech by another is not a concept which is new to our society. The fundamental principles of freedom and liberty seem to inherently recognize the right of individuals to peaceful coexistence free from physical or mental harassment. Yet it appears the Collin court did not give this right official recognition, or at least consider it a relevant factor in deciding whether regulation of the NSPA activities was warranted. This omission calls into question the legal existence or status of such a right.

There has been some recognition of a right to remain free from abusive speech. When the effect of such speech is physically abusive the law of nuisance has been extended to regulate its exercise. This includes situations where the form of the speech is abusive to the listener, as, for example, when a loudspeaker system is used to communicate in a residential neighborhood for an extended time disturbing the peacefulness and serenity of the residential area.50

When the effect of speech is such that a physical response results, the law has also allowed restriction of speech. Perhaps the most classic example of the courts' willingness to regulate free speech which has physical consequences is their denial of first amendment protection to speech which has the tendency to incite violence.51 This tendency is generally cited as justification for government regulation of speech as necessary to preserve order, which ultimately seems to be protection of citizens from the consequences of the exercise of free speech by another.

The history of judicial recognition of a right to protection from speech which causes mental or emotional anguish is less concrete than that dealing with physical effect. Harassment of individuals, either through verbal threats or menacing actions, has been subject to regulation, either through criminal prohibitions or injunction.52 Although this might technically involve some danger of physical violence, there appears to be some inherent recognition of the right of an individual to remain free of mentally abusive words or actions.

The most definite recognition of the right of an individual to remain free from abusive speech has been in the growth of the tort of intentional infliction of mental or emotional distress. Although the law had been slow to grant "peace of mind" independent legal protection, in recent years an increasing number of states, including Illinois,53 have recognized this right.54 This tort is necessarily found to exist only after the disturbing speech or action has taken place.

Post facto determination does not have the chilling effect upon first amendment rights that the Collin prior restraint context does, and thus is more acceptable to the courts.55 Most importantly, however, the fact that this tort is

55 Prior restraint upon speech has historically been viewed more critically by the courts than has subsequent punishment. This is generally based on the belief that prior restraint has a more serious effect as an infringement upon speech. See Organization for a Better Austin v. Keefe, 402 U.S. 415, 419 (1971).
recognized stands as a statement by the courts that there is a protectable interest in peace of mind and that those who intentionally invade the peace of another may be subject to judicial censure.

B. The Practical Difficulties Involved

As Collin illustrates, when a question involving validity of regulation or restriction upon free speech arises, courts have been reluctant to consider the possibility that the targeted listeners may have a right not to hear the speech. The Collin situation demonstrates the practical difficulty that protecting such a right would present. Considering the difficulty in judging the offensiveness of the proposed activities, and the judicial preference for first amendment rights, it is not surprising that some benefit of the doubt is extended in favor of speech.

It appears that the court in Collin felt that enforcement of fine-line distinctions between speech which was abusive and that which merely expressed unpopular ideas was likely to result in a chill of first amendment rights. The court's sensitivity to the proximity of first amendment rights is revealed by its statement that such situations “are indistinguishable in principle from speech that ‘invites dispute . . . induces a condition of unrest, creates dissatisfaction with conditions as they are, or even stirs people to anger,’” all of which the court recognizes as within the protection of the first amendment. Thus the court chose to sacrifice any possible protection of the Skokie citizens from mental abuse in favor of full protection of speech.

The explanation for this disregard of the residents' emotions can probably be placed at least in part upon practical considerations. The distinction between activities which are designed to intentionally harass and those which are not would require the court to make a subjective determination of motive. In addition, deciding whether such activity is indeed abusive to its hearers rather than merely annoying requires abstract consideration of the background of the target and the actor's knowledge of this background in exploiting weaknesses.

Although the line dividing mental harassment from simple disturbance is difficult to draw, such a distinction has been made in other contexts. The clearest example of this is again the tort of intentional infliction of mental distress. Because of the close proximity of free speech, courts have strictly construed “mental distress” to require more than insults or indignities. Recovery has generally required a showing of both intent and extremely outrageous conduct such that an ordinary man in the plaintiff's position would be mentally distressed. Thus while such a distinction may not be simple to make, it is possible, at least in a post facto context.

A second reason for the court's reluctance to allow regulation in Collin is a fear of the consequences of enunciating a new exception to protected speech. This concern is best expressed in the concurring opinion of Judge Wood:

56 578 F.2d at 1206 (quoting Terminiello v. Chicago, 337 U.S. 1, 4 (1949)).
57 E.g., Slocum v. Food Fair Stores of Florida, 100 S.2d 396 (Fla. 1958).
58 See W. Prosser, supra note 54, at 59. See also Nickerson v. Hodges, 146 La. 735, 84 So. 37 (1920).
It may also be well to remember that often "words die away, and flow off like water—leaving no taste, no color, no smell, not a trace." Any exception, however, to the First Amendment which we might be tempted to fashion for these particular persuasive circumstances would not "die away." It would remain a dangerous and unmanageable precedent in our free and open society.59

Future impact of a decision is always a relevant consideration, as Judge Wood recognizes. However, the hesitation to create a new exception to protected speech must be weighed against the need for protection of the recipients of that speech.

Despite refusal to expressly consider the potential mental disturbance of targeted listeners as a factor in determining whether speech can be restricted, it appears that some courts have implicitly granted protection of this right. This protection has generally been accomplished by construing the facts so broadly as to fit the contested activity within one of the existing exceptions to protected speech. An example of this approach is the decision in *Jewish War Veterans of the U.S. v. American Nazi Party.*60

In *Jewish War Veterans* the District Court of the Northern District of Illinois enjoined a demonstration upon the public streets based on its likelihood to cause a public disturbance. An examination of the case reveals a situation markedly similar to that presented in *Collin.* Members of the Nazi party announced that on the Jewish High Holy Days they would march through Jewish neighborhoods wearing "storm-trooper" uniforms and carrying placards inscribed with anti-Jewish slogans. The plaintiff group asked for an injunction to prevent the march, claiming that the actions of the Nazis infringed upon their right to worship peacefully and without insult, that it abridged their privileges and immunities, and that it would tend to incite riot and create public disturbances.

In issuing the requested injunction, the court recognized that the nature of the proposed action was such that it invited some type of response. The court was thus able to justify its restriction of speech under the traditional "tendency to incite violence" exception to protected speech, though no concrete threat of actual violence was shown.

The root of the court's decision seems to be a feeling that inherent injustice would be done if the Nazis were allowed to harass the Jewish citizens as an exercise of first amendment rights. A comment in the majority opinion best capsulizes this feeling:

Defendants do not march, or seek permission to march, for the purpose of obtaining lawful rights for themselves. There is nothing constructive in their activities. By their scurrilous attacks they seek only to destroy—to take from others rights to which they are entitled as human beings as well as under the Constitution.61

The court in *Jewish War Veterans* was thus presented with much the same problem as the Seventh Circuit in *Collin*. In *Jewish War Veterans*, however, the court had a nail upon which to hang its justification for restriction of speech, namely the alleged threat of violence. While a court often may be able to prevent abusive use of speech by relying on the tendency of such speech to result in violence, this cannot cover every situation where speech is abusive.

The most obvious exception is the situation presented in *Collin*, in which the Village conceded that despite the objectionable nature of the NSPA activities, no responsive violence was anticipated. If the court relies on the "tendency to incite violence" exception as providing adequate protection against abusive speech, the result is disproportionate. Those who threaten responsive disturbance would have their peace protected, while those who passively accept abuse without fighting back would not.

C. Protection Without Infringement Upon Speech

Summarizing the present status of first amendment rights vis-à-vis the right of targeted listeners to be free of mental distress intentionally inflicted, it is apparent that courts presented with such conflicts have either found alternate justification for restriction of the speech, as in *Jewish War Veterans*, or have opted for protection of speech without regard to its effect upon its audience, as in *Collin*.

The failure to openly recognize such a countervailing right does not appear to be based upon judicial denial of the existence of such an interest, since the same value has been granted independent legal protection in the tort context. Rather, the reluctance to recognize such a right seems to be a function of judicial hesitation to step outside established standards, especially since the full implications of such a step would be difficult to project. As a result, the Seventh Circuit missed an opportunity to openly recognize the existence of such a right and to examine the scope of its protection.

Had the Seventh Circuit decided to recognize expressly a right of targeted listeners to be protected from mentally abusive speech, it would not necessarily have produced a different result in *Collin*. This right would become part of the balancing process, and the court would then need to consider the extent of the effects of the speech upon the audience in deciding whether the speech was abusive enough to justify restriction upon free speech.

The factual setting of *Collin* suggests that the proposed activities of the NSPA were intended to harass the Jewish residents of Skokie. A real possibility exists, however, that the court might not find the proposed activities to be of sufficient abusiveness to meet this test. The activities were not overly intrusive if carried out according to plan. The march was not to take place in a residential area, involved a limited number of demonstrators, and was to last only half an

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62 See note 38 supra (discussion of the dispute over the effect of such concession).
63 The effect of the actions of the NSPA should not be confused with the effect of the national publicity aroused by the situation. Any added impact resulting from the media attention should not be charged to the actors in weighing the effect, since if this were done any attempt to publicly communicate views on a controversial issue would be open to limitation because of the likelihood of a multiplier effect from the press.
hour. Although the presence of the espoused Nazis was, itself, enough to upset some of the Skokie residents, it is unlikely that a court would find mere presence in a business area disturbing enough to outweigh the values of freedom of speech.

Whether or not the Seventh Circuit had decided to recognize an independent right of protection in the targeted listeners, it is thus likely that in the circumstances of Collin the same conclusion would have been reached. In a future situation, however, where the circumstances of the speech were more offensive or intrusive, whether or not such a right is considered in the weighing process could be outcome determinative.

Recognizing the practical considerations that have heretofore prevented the court from protecting this right, the question naturally arises whether there is a means by which protection could be afforded without undue infringement upon free speech. Can a government body, such as the Village of Skokie, assert violation of such a personal right of its citizens as a justification for first amendment regulation?

The power of a government to enact regulation to protect and promote the welfare of its citizens has long been recognized as within the police power of a state. This power has included regulation of activities such as obscenity which, although not threatening breach of the peace, infringe upon the rights of other citizens. Use of the police powers to restrict speech which inflicts psychological or emotional injury upon its audience received additional support from the Supreme Court in Chaplinsky v. New Hampshire. In Chaplinsky the court spoke not only of “fighting words,” but also of words “which by their very utterance inflict injury,” as invoking state interest.

Assuming the power of a state to protect the rights of its citizens under the police power, the final question of how a government body could protect this right without undue burden upon speech is ripe for consideration.

The Seventh Circuit's disapproval of the Skokie ordinances that attempted such regulation was basically of two types. First, several of the ordinances, such as that requiring insurance coverage, were inherently unacceptable burdens upon speech, and thus unconstitutional. The second type were those which were phrased so broadly as to prohibit legitimate exercise of speech as well as that which could be regulated. This second category, overbreadth, can be interpreted to imply that legislation can be used to restrict abusive speech, in narrowly defined circumstances.

In view of the foregoing, it appears that such legislation could be enacted subject to close scrutiny by the court. This scrutiny could be satisfied if two criteria were met:

1) The language in the law must be very specific so as to restrict or prohibit only speech which is abusive, and not speech which is constitutionally protected. This would require very careful drafting of the statute or ordinance with very specific definitions of abusive speech and strict standards for its identification.
2) The activities proposed to be regulated must fit the prohibitions of the statute very tightly.

Strict adherence to detail in drafting and in finding statutory coverage of a given situation would severely limit the power of a state to regulate the exercise of speech. Strict limitation, however, is essential if the regulation is to pass constitutional muster as a valid restriction upon free speech.

Some abusive speech would always evade regulation, particularly that which is only questionably abusive. Collin would probably fall into this category of nonregulation. Yet protection would be available for the more distinct cases in which speech has mentally abusive effects, and nonabusive exercise of speech would continue to receive full constitutional protection.

V. Conclusion

In deciding Collin, the Seventh Circuit was faced with a situation in which exercise of rights of free speech under the first amendment would cause mental and emotional disturbance of the target audience. Consistent with the traditional view, the court did not recognize any right of the targeted listeners to remain free from such speech, and ultimately found the attempts of the Village of Skokie to regulate the exercise of speech to constitute undue burdens upon free speech.

In doing so, the court forfeited an opportunity to expressly establish this right, which has been implicitly recognized in other legal contexts. The court's unwillingness to take this step seemingly did not disturb the outcome in Collin. The precedent established by this decision, however, could adversely affect the position of targeted audiences in future cases in which the speech might be more disturbing than that in Collin. Determination of the impact of the Seventh Circuit's decision in Collin therefore must be postponed until such cases arise.

Ruth Ann Beyer

United States v. Kuehn*

"The power of government to compel persons to testify in court or before grand juries and other governmental agencies is firmly established in Anglo-American jurisprudence."1 The enactment of the immunity provisions of the Organized Crime Control Act of 19702 reflects the recognition of this power as crucial in attacking organized crime.3 The act gives a witness immunity from prosecution and thereby supplants his fifth-amendment privilege against self-incrimination in exchange for his future testimony. Yet it is sometimes difficult to conceptualize whether the witness or the government is the beneficiary of the immunity order and, consequently, to determine who has standing.

In United States v. Kuehn, the Seventh Circuit addressed the question of whether a U.S. Attorney had standing to seek an injunction prohibiting the continuation of an ongoing state prosecution of a federal witness on the grounds that the state prosecutor had used evidence derived from the witness's federally immunized testimony. The district court issued an injunction and was reversed by the Seventh Circuit on the grounds that the United States lacked standing.

The Seventh Circuit's rationale for holding that the United States lacked standing was superficial because it failed to give due consideration to the purposes of the immunity provisions and to the practical considerations involved in organized crime investigations. These considerations warrant a more sophisticated interpretation of the immunity provisions of the Act. With the benefit of hindsight, this comment will analyze the rationale of the Seventh Circuit's holding in Kuehn and will suggest how U.S. Attorneys should assert standing to protect immunity orders issued to their witnesses. Finally, measures will be proposed by which Congress could definitively solve the standing problems which accompany immunity orders.

I. Statement of the Case

On October 22, 1974, the United States District Court for the Eastern District of Illinois issued an immunity order compelling Marvin C. Schwartz to testify before a federal grand jury investigating widespread corruption of public officials. Schwartz had previously asserted his fifth-amendment privilege against self-incrimination before that grand jury. The immunity order was issued by the court, upon the request of the U.S. Attorney, pursuant to the immunity pro-

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3 NATIONAL ASSOCIATION OF ATTORNEYS GENERAL, Organized Crime Control Legislation, 133 (1972).

* 562 F.2d 427 (7th Cir. 1977), rev'g, United States v. Rice, 421 F.Supp. 871 (E.D. Ill. 1976).

One of the seven subsequent federal criminal trials at which Schwartz testified was the prosecution of Robert Rice, the State's Attorney for St. Clair County, Illinois. Rice was indicted on March 3, 1976, for extorting Schwartz. Thereafter, pursuant to the criminal discovery process, Rice received a copy of Schwartz's immunized grand jury testimony. Schwartz's immunized testimony included an admission that he had given $1,000 to Albert S. Rolek for the purpose of bribing John Hoban, a state court judge. Having read the immunized testimony, Rice caused evidence, including the testimony of Rolek, to be presented to a state grand jury. On June 17, 1976, almost two years after Schwartz's immunized testimony and immediately following Rice's acquittal in federal court, the state grand jury indicted Schwartz for bribing the state judge. Rice then proceeded to prosecute Schwartz in state court.

Schwartz filed a motion in the state court to dismiss the indictment on the grounds that Rice had used evidence derived from Schwartz's immunized testimony. This motion was denied by the state court after it found an independent basis for the evidence presented to the state grand jury.

On September 24, 1976, the U.S. Attorney sought an injunction in the federal district court to enjoin Rice from continuing his state prosecution against Schwartz on the grounds that evidence derived from Schwartz's federally immunized grand jury testimony was being used against Schwartz. Following the federal court's issuance of a temporary injunction, Schwartz was permitted to intervene as a plaintiff.

During the injunction hearing, Rice testified that he had begun his investigation of Schwartz before reading Schwartz's grand jury testimony and that he

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4 18 U.S.C. § 6002 (1970) reads in relevant part:
Whenever a witness refuses, on the basis of his privilege against self-incrimination, to testify or provide other information in a proceeding before or ancillary to—
(1) a court or grand jury of the United States,
(2) an agency of the United States, or
(3) either House of Congress, a joint committee of the two Houses, or a committee or a subcommittee of either House,
and the person presiding over the proceeding communicates to the witness an order issued under this part, the witness may not refuse to comply with the order on the basis of his privilege against self-incrimination; but no testimony or other information compelled under the order (or any information directly or indirectly derived from such testimony or other information) may be used against the witness in any criminal case, except a prosecution for perjury, giving a false statement, or otherwise failing to comply with the order.

5 The federal indictment alleged that Rice "did knowingly and willfully conspire . . . to obtain property in the amount of $25,000 from Marvin Schwartz, . . . under color of official right, namely the indictment of Marvin Schwartz for criminal acts and the offer to have those indictments dismissed."

6 The state court judge found that Schwartz had related substantially the same facts to a newspaper reporter prior to his being indicted by the state. 562 F.2d at 429.

The immunity afforded by § 6002 is only use immunity, not transactional immunity, so the witness may be prosecuted for offenses relating to his immunized testimony provided the prosecutor can show he has not used the immunized testimony or evidence derived from it in bringing the prosecution. "This total prohibition on use provides a comprehensive safeguard, barring the use of compelled testimony as an 'investigatory lead,' and also barring the use of any evidence obtained by focusing investigation on a witness as a result of his compelled disclosures." 421 F.Supp. at 874.
had not used derivative evidence. The district court disagreed, however, and found that an examination of the federal and state grand jury transcripts “lead[s] one to the inescapable conclusion that inquiries before the State Grand Jury are bottomed on information obtained from the Federal Grand Jury proceedings.” The court was unable to find that the inquiry before the state grand jury was wholly without the benefit of any knowledge that Rice may have acquired by reading Schwartz’s testimony and found that some of the questions presented at the state grand jury proceeding were almost identical to those asked at the federal grand jury. The court specifically found that “[t]he name of the witness Albert S. Rolek as purveyor of money [from Schwartz to the state judge] became known to the world as a direct result of the compelled testimony of Marvin Schwartz.”

The court also noted that Schwartz was still a material witness in pending federal prosecutions in which he would be required to testify pursuant to his immunity order. Accordingly, on October 14, 1976, the federal district court permanently enjoined Rice from continuing his prosecution of Schwartz. That injunction was appealed to the Seventh Circuit by Clyde Kuehn, Rice’s successor as the State’s Attorney.

II. The Seventh Circuit’s Decision

On September 19, 1977, the Seventh Circuit reversed the district court’s injunction. The court held that the government lacked standing to protect the immunity order because the government had received all that it had asked for when Schwartz testified. The court’s rationale was based upon the idea that “…the grant of immunity flows to the witness and not to the Government. Only the witness may claim its benefits.” In essence, the court found that the witness, not the government, was the beneficiary of an immunity order and, consequently, the government lacked standing to protect the order.

The court also addressed the anti-injunction statute11 which the U.S. Attorney asserted as a basis for the court’s jurisdiction. He asserted that the district court could exercise jurisdiction to effectuate its own judgment when its immunity order was being interfered with by a state prosecution. The Seventh Circuit held, however, that to overcome the anti-injunction statute, “…the Government must have a judgment in its favor to effectuate, that is, the United States must have a substantive claim to assert in the district court. Here it has none.” The U.S. Attorney has no substantive claim because, according to the Seventh Circuit, the grant of immunity flows to the witness and thereby forecloses the government from claiming its benefits. Based upon this rationale, the court reversed the injunction.

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7 421 F.Supp. at 876.
8 Id. at 873.
9 Id.
10 562 F.2d at 431.
11 The Anti-Injunction Act, 28 U.S.C. § 2283 (1948), which states: “A court of the United States may not grant an injunction to stay court proceedings in a State Court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments.”
12 562 F.2d at 431.
The Seventh Circuit also found Schwartz's claim as an intervenor to be defective. It held that he was barred by collateral estoppel since he had lost his motion in the state court. Furthermore, he had failed to make allegations sufficient to overcome the Younger abstention doctrine.\(^{13}\)

Although the court found it unnecessary to reach a decision on the merits of the independent source issue, the court indicated that, were it necessary to do so, it would have ruled that the district court's finding that the state prosecutor did not have independent sources of evidence on which to base the indictment was clearly erroneous.\(^{14}\)

The Seventh Circuit's rationale for concluding that the government lacked standing was superficial because it failed to consider either the purposes of the immunity provisions, as revealed by their legislative history, or the pragmatics of organized crime investigations. These considerations indicate that although the witness receives use immunity as the quid pro quo for his fifth-amendment privilege, it is in fact the government which is the true beneficiary of an immunity order which is coupled with an order to compel testimony. To demonstrate this point, it is necessary to take "a glimpse at standing" to ascertain the requirements which a party must fulfill for standing.

### III. A Glimpse at Standing

Over two decades ago the Supreme Court stated that the law of standing was a "... complicated specialty of federal jurisdiction. ..."\(^{15}\) This statement is even more accurate today. The Court has decided over twenty cases on standing since 1970 and confusion over the application of this concept still persists.\(^{16}\)

The ultimate value sought to be preserved is the notion that, "[t]he very essence of civil liberty certainly consists in the right of every individual to claim the protection of the laws, whenever he receives an injury."\(^{17}\)

The formulation of a concise list of the prerequisites for standing has proved to be an elusive task, as evidenced by the frequency with which the Supreme Court has addressed this issue since 1970. The difficulty arises in part because of the overlapping restrictions involved: the case or controversy requirement of

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13 Younger v. Harris, 401 U.S. 37 (1971). This doctrine prohibits, for reasons of comity and federalism, a federal court from enjoining a state criminal prosecution, absent exceptional circumstances.

14 562 F.2d at 432.


17 Marbury v. Madison, 5 U.S. (1 Cranch) 137, 163 (1803).
Article III and the prudential limitations of judicial self-restraint. Further difficulty results because the Court has focused on the individual claimant's potential for presenting his particular case in a justiciable manner. This necessarily requires the Court to peek around the claimant "to look to the substantive issues... to determine whether there is a logical nexus between the status asserted and the claim sought to be adjudicated." Nevertheless, it is possible to distill from the Court's opinions three prerequisites for standing.

The first prerequisite is that the claimant must allege he has received or been threatened with a distinct and palpable injury in fact, although the injury may be indirect and need not be economic. This requirement represents the Supreme Court's recognition of the limits of judicial competency. Its underlying rationale is to insure that the claimant will present his case in the proper adversarial posture. Without true adversaries before it, a court, due to its traditional manner of processing controversies, cannot feel comfortable with a case.

Virtually every opinion on standing begins with this proposition by quoting Baker v. Carr: "Have the appellants alleged such a personal stake in the outcome of the controversy as to assure that concrete adverseness which sharpens the presentation of issues [upon] which the court so largely depends for the illumination of difficult questions? This is the gist of standing." The Court has consistently required the claimant to allege a clear injury in fact to satisfy the case or controversy requirement of Article III. Absent such a showing, exercise of its power by a federal court would be gratuitous and thus inconsistent with the Art. III limitation.

The second prerequisite for standing is that the claimant must, in any concretely demonstrable way... allege facts from which it could be reasonably
inferred that...there is a substantial probability\(^{28}\) that his injury was caused by the complained of action. A demonstration of "but for" causation became mandatory after Simon v. Eastern Kentucky Welfare Rights Organization\(^{29}\) and Warth v. Seldin.\(^{30}\) In Warth, Justice Powell warned that conclusory allegations of resulting injury will not be enough; the Court will not speculate on causal relationships.\(^{31}\)

The final requirement for standing is that the Court feel capable of granting effective relief. This requirement may be viewed as flowing from the Court's concern over speculative causation, since a court can hardly feel capable of granting effective relief if the source of the injury is undiscernable.

This third prerequisite emphasizes the judicial restraint side\(^{32}\) of justiciability, namely, that the court feel comfortable with its ability to handle the case with the parties before it, to reach a competent and reasoned decision, and to grant and enforce effective relief. Once again, the claimant must allege specific facts, this time to show the substantial likelihood that the court is capable of correcting the injury he has suffered.\(^{33}\) He must show "that he personally would benefit in a tangible way from the court's intervention."\(^{34}\)

These prerequisites for standing, which have been referred to as the "direct injury-effective relief test,"\(^{35}\) have been capsulized best by the Ninth Circuit, which held that the "test for standing... is that the plaintiffs must have alleged (a) a particularized injury (b) concretely and demonstrably resulting from the defendant's action (c) which injury will be redressed by the remedy sought."\(^{36}\) These requirements have been endorsed by the Seventh Circuit in Mulquenny v. National Commission on the Observance, Etc.\(^{37}\)

Whether or not both a witness and the government can fulfill these prerequisites when seeking to enforce an immunity order merits further analysis. In such analysis the issue of the government's standing must take into account the purpose of the immunity provisions as revealed by their legislative history as well as the pragmatic considerations integral to organized crime investigations.

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\(^{28}\) 422 U.S. at 504. Likewise, in Arlington Heights v. Metropolitan Housing Corp., 429 U.S. 252 (1977), the Court stated: "the complaint must indicate that the injury is indeed fairly traceable to the defendant's acts or omissions." Id. at 261. Accord, 426 U.S. at 41-42; 410 U.S. at 618.

\(^{29}\) 426 U.S. at 25 n.25. See United States v. SCRAP, 412 U.S. 669, 688 (1973); 397 U.S. at 152.

\(^{30}\) 422 U.S. at 504-07.


\(^{32}\) For a list of the Court's considerations on the subject of judicial restraint, see Ashwander v. TVA, 297 U.S. 288, 346-48 (1936) (Brandeis, J., concurring).

\(^{33}\) See 429 U.S. at 262; 426 U.S. at 45-46. "Federal judicial power is limited to those disputes... which are traditionally thought to be capable of resolution through the judicial process." 392 U.S. at 97.

\(^{34}\) 422 U.S. at 508.

\(^{35}\) Comment, SANTA CLARA L. REV., supra note 16.

\(^{36}\) Bowker v. Morton, 541 F.2d 1347, 1349 (9th Cir. 1976).

\(^{37}\) In Mulquenny v. National Comm'n on the Observance, Etc., 549 F.2d 1115 (7th Cir. 1977), the Seventh Circuit recognized the requirements: (1) injury in fact, (2) resulting from the defendant's conduct, and (3) that the judicial relief requested will ameliorate the complained-of harm. Id. at 1120.
IV. Government Standing in Kuehn

In Kuehn the Seventh Circuit held that “the Government has no standing to protect the grant of immunity. Once the witness has testified, the Government received all that it asked for—the compelled testimony.” In short, the “grant of immunity flows to the witness and not to the Government. Only the witness may claim its benefits.”

This conclusion suggests erroneously, however, that the government could never satisfy the prerequisites for standing discussed previously. As revealed by the legislative history of the immunity sections of the Organized Crime Control Act of 1970, the government was meant to benefit from grants of immunity. As a result, compliance with the standing prerequisites by the government cannot be foreclosed by simply concluding that “only the witness may claim its benefits.”

The Organized Crime Control Act of 1970 was aimed at “strengthening the legal tools in the evidence-gathering process” of the government for the “development of legally admissible evidence.” In 1969, President Nixon recommended the adoption of a general witness immunity law by stating: “With this new law, Government should be better able to gather evidence. . . .” The congressional committee which studied the Act also believed “that the legislation would have a beneficial effect on law enforcement.”

The use of immunity granted by § 6002 was not designed to benefit the witness, but rather was only the quid pro quo for the witness’s fifth-amendment privilege of silence. Immunity is the price which the government must pay to secure the testimony of a recalcitrant witness. Given the choice, a witness in an organized crime investigation would likely prefer his fifth-amendment privilege to remain silent to the imposition of immunity which accompanies an order to compel testimony.

Finally, the wording of the statute itself suggests that it may be properly understood as granting the United States a right to judicial relief because of the emphasis it places upon the U.S. Attorney in the immunity process. The statute provides that only the U.S. Attorney may request an immunity order from the district court and then only if he decides that it is in the public interest.
Neither the court, upon its own request, nor the witness can initiate the immunity order process. Furthermore, the court has little discretion on whether to issue the immunity order because the statute says the court "shall" issue, rather than "may" issue the immunity order upon proper application.

A. Injury in Fact

The first prerequisite which the U.S. Attorney had to fulfill in order to gain standing in Kuehn was to allege that the government had been injured in fact. Since the statute was enacted to provide the U.S. Attorney with an "evidence-gathering tool," the government has an interest in obtaining the fruits which the tool was designed to provide. Additionally, the pragmatic difficulties inherent in developing witnesses in organized crime investigations suggest that the government has a legitimate interest in maintaining its credibility in the future use of immunity orders. The government merely seeks to insure that the tool remains effective for future use.

If a U.S. Attorney is perceived as lacking credibility because his previous immunity orders have been ineffective, future witnesses who are compelled to testify pursuant to an immunity order are likely to be uncooperative, forgetful of certain facts, and less apt to volunteer additional information. Granted, the government can seek perjury or contempt sanctions against an immunized witness who lies or withholds information, and the witness can lose the protection of the immunity order, but any litigator can attest to the difference between a friendly and hostile witness, even if the hostile witness can be compelled to give the evidence the attorney is seeking to elicit. To deny the legitimacy of the government's concern over its credibility in the future use of immunity orders is to ignore the dynamics of developing the testimony of immunized witnesses in organized crime investigations.

In Kuehn, the United States had not received "all that it asked for," as the Seventh Circuit held, because Schwartz was still a "material witness in cases pending before the Federal Court." He could still be compelled by the immunity order to testify for the government at those future trials. If Rice, the State's Attorney, used evidence derived from Schwartz's immunized federal grand jury testimony as the government alleged, then the government would be

51 562 F.2d at 430.
52 421 F.Supp. at 873.
53 "For purposes of ruling on a motion to dismiss for want of standing, both the trial and reviewing courts must accept as true all material allegations of the complaint, and must construe the complaint in favor of the complaining party." 422 U.S. at 501. Accord, Jenkins v. McKeithen, 395 U.S. 411, 421-22 (1969).
threatened with injury by Schwartz becoming a hostile and uncooperative witness and thus jeopardizing those future trials.\textsuperscript{54}

The Seventh Circuit’s denial of standing is explainable, however, in view of the government’s failure to allege in a concretely demonstrable way that it was threatened with injury in fact. Speculative pleadings that the government’s position would be enhanced by the absence of Rice’s actions are insufficient.\textsuperscript{55}

Ideally, the government, in a case like \textit{Kuehn}, should allege specific facts in its complaint, supported by affidavits, attesting to the witness’s change in attitude following his state prosecution and that this change was jeopardizing the future government prosecutions in which he was to testify.\textsuperscript{56}

The government also has a legitimate concern for its future credibility when evidence derived from a witness’s immunized testimony is used to convict him in state court. In organized crime investigations, prosecutors are especially concerned with their credibility\textsuperscript{57} because they realize the practical necessity of this trait for success in dealing with future witnesses.\textsuperscript{58} The district court which issued the injunction seemed to recognize this concern:

\begin{quote}
If the defendants are permitted to use the testimony directly or indirectly obtained from Marvin Charles Schwartz’s own testimony given under order of this Court, there would be immediate and irreparable harm to the United States and to the United States jurisdiction over pending and future organized crime and racketeering cases.\textsuperscript{59}
\end{quote}

The pragmatics of using immunity orders indicate that in some cases there will be a threatened injury in fact to the government’s credibility.

A court faced with the question of whether the United States was injured in fact, as the Seventh Circuit was in \textit{Kuehn}, should find that the injury-in-fact requirement of standing is satisfied when the government’s future pending trials are being jeopardized by an uncooperative witness and its credibility with respect to future immunity orders is being threatened. Such a holding would be supported by the underlying rationale of the injury-in-fact requirement: a “personal stake”\textsuperscript{60} to insure the adversary context in which courts feel comfortable. Fur-
thermore, when the judge "peeks around" the litigant to the substantive issues, he should be satisfied that there is a logical nexus between the U.S. Attorney and his interest in insuring that the terms of the immunity order are not violated. The holding that the government was without standing in Kuehn demonstrates the importance of alleging specifically the facts necessary to allow the court to conclude there has been an injury in fact.

B. But For Causation

The second prerequisite of standing, "but for causation," would have been relatively easy for the U.S. Attorney to fulfill in Kuehn. He would merely have had to allege that the government's injuries in fact, namely, Schwartz becoming a hostile witness and the threatened damage to credibility, were due to Rice's use of evidence derived from Schwartz's immunized testimony. Although courts will not speculate on causation, the facts in Kuehn support a clear inference that the government's injuries were the result of Rice using derivative evidence, contrary to the terms of Schwartz's immunity order.

C. Effective Relief

The final requirement for standing, that the court feel capable of granting effective relief, requires the government to allege that it would "benefit in a tangible way" if the federal court enjoined Rice's prosecution of Schwartz. Had the Seventh Circuit found that the United States had been injured in fact by Rice's prosecution, this requirement would have been fulfilled. The district court's injunction would maintain the government's cooperative witness and enhance the government's credibility in the future use of immunity orders.

This requirement in particular, however, is subject to the judicial restraint side of justiciability. Whether a court feels comfortable with the parties before it and capable of reaching a reasoned and enforceable decision depends on the court's interpretation of the immunity provisions and its assessment of the pragmatics of immunizing witnesses in organized crime investigations.

The government should be able to satisfy the three prerequisites for standing in a case like Kuehn by alleging specific facts which show that it was injured in fact by the state prosecutor's conduct and that the court is capable of granting effective relief. The legislative history and the wording of the statute itself, plus the pragmatic credibility concern for its effective use, all demonstrate that the government has a substantial interest in insuring that its use immunity is not violated. Although the Seventh Circuit's failure to address these considerations might be explained in that they were not alleged in the government's complaint, the court's holding that the benefit of the "grant of immunity flows to the witness and not to the Government" is still troublesome. It implies that the government could never have standing to enforce an immunity order in a case like

61 See note 19 supra.
62 See text accompanying note 29-31 supra.
63 See text accompanying notes 32-34 supra.
64 562 F.2d at 431.
Kuehn. In so holding, the Seventh Circuit failed to give due consideration to the purpose of the immunity sections and their intended effect of facilitating government prosecutions.

V. Additional Considerations

Even if the Seventh Circuit had recognized the government’s standing in Kuehn, the government would have had to overcome two remaining hurdles: the anti-injunction statute and the Younger abstention doctrine.

A. The Anti-Injunction Act

In Kuehn, the court held that to initiate an action permitted under the Anti-Injunction Act, the government needed a judgment in its favor to effectuate, and since the grant of immunity flowed to the witness, the government did not have a substantive claim to assert. This holding, however, was actually nothing more than a reaffirmation of the denial of standing. If the government had had standing in Kuehn, the Anti-Injunction Act would not have been a barrier.

"[I]t is settled law that the prohibition of the anti-injunction statute does not apply to the Government of the United States." The issue of whether the anti-injunction statute is applicable to the government has been decided by the Supreme Court in Leiter Minerals, Inc. v. United States. In a precise opinion by Justice Frankfurter, a leading spokesman for judicial restraint, the Court stated:

There is, however, a persuasive reason why the federal court’s power to stay state court proceedings might have been restricted when a private party was seeking the stay but not when the United States was seeking similar relief. The statute is designed to prevent conflicts between state and federal courts. This policy is much more compelling when it is the litigation of private parties which threatens to draw the two judicial systems into conflict than when it is the United States which seeks a stay to prevent threatened irremovable injury to a national interest.

Not only did the Court believe the potential conflict between the state and federal government was less compelling when the suit was bought by the United States,

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66 562 F.2d at 431.


it also refused to interpret the Act as being designed to frustrate "superior federal interests." This interpretation of the anti-injunction statute remains viable today, even after *Younger v. Harris*.

If the United States has standing, then its "superior federal interest" serves to bypass the prohibition of the anti-injunction statute. Although a court may deny the government standing, as the Seventh Circuit did in *Kuehn*, such a decision must rest upon the principles of standing and not the prohibition of the anti-injunction statute. "For the Federal Government and its agencies, the federal courts are the forum of choice. For them, as *Leiter* indicates, access to the federal courts is preferable in the context of healthy federal-state relations."

**B. Younger Abstention**

Even if the Seventh Circuit had found that the government had standing in *Kuehn*, the government would have been faced with the problem of overcoming the *Younger* abstention doctrine. Although the court did not apply this doctrine to the government in *Kuehn*, it did raise the issue in dismissing Schwartz's intervenor claim and would have raised it with respect to the government, had its claim not been resolved on the basis of standing.

In *Younger*, the Supreme Court announced the concept of "Our Federalism" which, for reasons of comity and federalism, prohibits a federal court

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70 352 U.S. at 226.
71 "The purpose of § 2283 was to avoid unseemly conflict between the state and federal courts where the litigants were private persons, not to hamstring the Federal Government and its agencies in the use of federal courts to protect federal rights." NLRB v. Nash-Finch Co., 404 U.S. 138, 146 (1971).
73 401 U.S. 37 (1971). The *Leiter* interpretation of the Act is concerned with whether the court has jurisdictional power to proceed. The *Younger* abstention doctrine is based on concerns for "Our Federalism."
74 The "superior federal interest" in *Leiter* was the loss of royalties for mineral rights. This hardly seems overwhelming when compared to the government's interests in *Kuehn* which was derived from the Organized Crime Control Act of 1970. The Act was enacted because "organized crime activities in the United States weakened the stability of the Nation's economic system, harm innocent investors and competing organizations, interfere with free competition, seriously burden interstate and foreign commerce, threaten domestic security, and undermine the general welfare of the Nation and its citizens." Statement of Findings and Purpose, Organized Crime Control Act of 1970, *supra* note 43. Furthermore, an immunity order may only be issued by the district court upon the request of the U.S. Attorney (with the approval of the Attorney General, Deputy Attorney General or designated Assistant Attorney General), when he believes the testimony may be necessary for the "public interest." 18 U.S.C. § 6003(a). *Accord,* "He must be satisfied that the testimony is needed for the public interest." H.R. REP. No. 1188, 91st Cong., 2d Sess. 13 (1970).
75 404 U.S. at 147.
78 401 U.S. at 44.
from enjoining a state criminal prosecution except upon a "showing of bad faith, harassment, or any other unusual circumstance that would call for equitable relief." As applied to the government's position in *Kuehn*, "Our Federalism" appears to be an insurmountable hurdle and would have been another way by which the Seventh Circuit could have dismissed the government's claim.

There are some unanswered questions, however, concerning *Younger*’s application to the government in a case like *Kuehn*. To date, all of the cases involving the *Younger* abstention doctrine have been brought by private parties. Arguably, the same concerns for comity and federalism do not exist when the United States is the moving party, asserting a "superior federal interest," and the government is not a party before the state court proceeding. Some of *Younger*’s concerns for federalism and comity are similar to those behind the Anti-Injunction Act, and as discussed previously, the Court in *Leiter* found that Act inapplicable when the United States was the moving party. 81

VI. Conclusion

The Seventh Circuit’s decision in *Kuehn*, that the benefits of an immunity order flow to the witness, restricts the effectiveness of immunity orders in organized crime investigations and ignores the goals sought to be achieved by the statute. The immunity sections were enacted to provide the government with a new tool for combating organized crime. Since the government is the beneficiary of the Act, it should have standing to protect immunity orders when its future trials are jeopardized because the witness is becoming uncooperative or when the government’s future credibility is threatened.

With the benefit of hindsight, the Seventh Circuit’s failure to address these issues may be explainable in that the U.S. Attorney’s complaint only alleged jurisdiction under § 1345 and § 2283. The court’s holding that only the witness may claim the benefits of the immunity order, however, reflects a failure to give due consideration to the purpose of the Organized Crime Control Act of 1970. Furthermore, since the court not only “peeked around” to the merits but actually indicated that it believed there was an independent basis for the evidence used in the state prosecution, the court’s superficial treatment of the question of

79 *Id.* at 54.
80 In *Perez v. Ledesma*, 401 U.S. 82 (1971), the Court held that a federal injunction may not be used to challenge the admissibility of evidence in a state court proceeding. *Id.* at 83-85.
81 See text accompanying notes 65-75 *supra*. It would be interesting to speculate on how the Supreme Court would respond to the argument that *Younger* is inapplicable when the government is the moving party asserting a superior federal interest as in *Leiter*. In *Mitchum*, the concurring opinion stated that although § 1983 was an expressed statutory exception to the anti-injunction statute, “it does nothing to question or qualify in any way the principles of equity, comity, and federalism that must restrain a federal court when asked to enjoin a state court proceeding.” 407 U.S. at 244. Once again, however, that case is distinguishable because the plaintiff was not the United States asserting a superior federal interest. Furthermore, the Court said the test is “whether an Act of Congress, clearly creating a federal right, [such as the government’s right to remain credible and take full advantage of its immunized witness] . . . could be given its intended scope only by the stay of a state court proceeding.” *Id.* at 238.
82 28 U.S.C. § 1345 (1948), which provides generally that district courts shall have original jurisdiction of all civil actions commenced by the United States.
standing may be explainable on the grounds that the court was unimpressed with the case on its substantive merits.

The essential lesson to be derived from Kuehn is the need for claimants to make specific factual allegations which guide the court through its inquiry of standing. Not only is this the message of the Supreme Court's recent cases on standing, but the consequence of failing to do so is apparent in Kuehn. Claimants must allege specific facts which permit the court to conclude that the three requirements of standing have been satisfied.

The more effective solution to the problem posed by Kuehn, however, is for Congress to amend § 6002 to remove any doubt as to whom the intended beneficiary of immunity orders is and to give the United States the express right to enforce them.84 Such an amendment would recognize the pragmatics of immunity orders in organized crime cases. A U.S. Attorney who is dependent upon an immunized witness for the successful prosecution of a series of organized crime cases should not be without a means of relief when a state prosecutor's violation of the immunity order threatens to alienate the witness. Nor should the government be dependent for its reputation for credibility upon a state prosecutor's scruples. Whether or not Rice had an independent basis in Kuehn, cases will arise in which the immunity order has been violated to the detriment of the United States, and in such cases the government should have a right to relief. "Congress may create a statutory right or entitlement the alleged deprivation of which can confer standing to sue . . . ,"85 and it should do so by amending the immunity provisions of the Organized Crime Control Act.

Jerome R. Doak

84 For an excellent discussion of implying standing from statutory authority, see Note, Implying Standing to Sue from Statutory Authority: Applicability of a "Fair Reading" Standard, 54 NOTRE DAME LAW. 102 (1978).
85 422 U.S. at 514. "Essentially, the standing question in such cases is whether the constitutional or statutory provisions on which the claim rests properly can be understood as granting persons in the plaintiff's position a right to judicial relief." Id. at 500. Such an amendment might also eliminate the hurdle posed by Younger. See the test stated at the end of note 81 supra.
Civil Procedure—The Clayton Act as an Expressly Authorized Exception to the Anti-Injunction Act—Factual Showing Is Insufficient to Justify an Injunction to Stay a State Court Proceeding.

*Kurek v. Pleasure Driveway & Park Dist.*

I. Introduction

The relationship between the federal judicial system and state judicial systems has been a rich source of complex substantive and procedural problems. The conditions under which injunctive relief may be granted by a federal court to stay a proceeding in a state court have proven recalcitrant to adequate analysis.

A question that is of central importance in antitrust litigation concerns the nature of such injunctive relief, namely, is the Clayton Act an expressly authorized exception to the Anti-Injunction Act? The Seventh Circuit addressed this question in *Kurek v. Pleasure Driveway & Park Dist.*

The nature of injunctive relief and the conditions under which such relief can be granted have been hotly contested in recent years and little coherent direction has emerged from the Supreme Court. Although the Seventh Circuit was correct in ultimately denying injunctive relief on the facts of *Kurek*, the court ignored an opportunity to clarify important policy considerations and failed to generate guidelines for district courts to apply when granting or denying injunctive relief.

II. The *Kurek* Decision

*Kurek* is a complex case involving an extended series of procedural maneuvers. Several golf professionals held pro shop concessions at golf courses operated by the Peoria, Illinois, park district. During 1972 and 1973, an extended series of negotiations were conducted between the golf professionals and the park district concerning rental rates for the pro shops. These negotiations resulted in a contract for the year 1973. Similar negotiations were conducted in 1973 to procure a contract for 1974, but these negotiations failed.

On January 19, 1974, the park district awarded a three-year contract to Golf Shops Management, Inc., for the pro shop franchises. On January 21, 1974, the golf professionals were served with a 30-day notice to terminate the tenancy. The golf professionals refused to vacate, and the park district filed a forcible entry- and detainer proceeding against them. The park district lost the forcible entry and detainer action, but later won reversal by the Illinois Appellate Court.*
On July 25, 1975, the park district filed an action to recover damages for the wrongful possession of the pro shops. The park district recovered a judgment for $127,605, and the judgment was sustained by the Illinois Appellate Court. An antitrust claim was filed by the golf professionals in federal district court charging that increases in concession fees demanded by the park district during the negotiations for the 1974 contracts were part of an unlawful conspiracy to fix prices. In addition, the golf professionals alleged that as retribution for refusing to participate in the price fixing scheme, the park district awarded a monopolistic concession contract to Golf Shops Management. The district court dismissed the case on the basis of state action immunity, namely that the activities of governmental units are not covered by the Sherman Act.

The Seventh Circuit reversed the judgment of the district court on the antitrust claim. Finding that recent decisions of the Supreme Court had restricted the scope of the state action immunity defense, the Seventh Circuit returned the case to the district court to consider the merits of the antitrust claim. The park district appealed to the Supreme Court. Certiorari was granted and the case was subsequently returned to the Seventh Circuit for reconsideration in light of a recent Supreme Court holding on the state action immunity doctrine. On remand, the Seventh Circuit re-affirmed its original judgment, and the case was returned to federal district court.

While the antitrust litigation proceeded, the park district sought enforcement of the state court judgment. The golf professionals advocated enjoining such enforcement. The issue before the Seventh Circuit in *Kurek* was whether the facts of this case justified federal injunctive relief to stay the enforcement of a state court proceeding. Although the denial of the injunction by the Seventh Circuit was correct, the reasoning of the court merits further analysis.

### III. Current Law

The threshold question that must be answered before any federal injunction against a state court proceeding can be issued is whether the injunction falls within one of the express exceptions to the Anti-Injunction Act. The prevailing

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6 Kurek v. Pleasure Driveway and Park Dist., No. 76-9 (S.D. Ill., filed June 1, 1976).
7 Kurek v. Pleasure Driveway and Park Dist., 557 F.2d 580 (7th Cir. 1977).
10 Kurek v. Pleasure Driveway and Park Dist., No. 76-1791 (7th Cir., filed September 11, 1978).
11 574 F.2d at 895.
rule is that the Act is "an absolute prohibition against enjoining state court pro-
ceedings, unless the injunction falls within one of three specifically defined ex-
ceptions." The three exceptions to the Anti-Injunction Act are that "a court of
the United States may not grant an injunction to stay proceedings in a state
necessary in the aid of its jurisdiction, or [3] to protect or effectuate its judg-
mants." 14

Kurek centered on the first of these exceptions, and hence the precise
objective was to determine whether Congress had "expressly authorized" an
exception to the Anti-Injunction Act which was applicable to the Kurek facts.

The relevant test in resolving this inquiry was articulated in Mitchum v. Foster 16 in which the Supreme Court stated that the test is "whether an act of Congress, clearly creating a federal right or remedy enforceable in a federal
court of equity, could be given its intended scope only by the stay of a state court
provision." 16

Neither the meaning nor the justification of this standard is clear. If
Congress expressly states that an injunction may be granted against a proceeding
in state court, then clearly the exception applies. 17 If an act of Congress permits
a federal court to stay a proceeding, even though the act does not mention state
proceedings specifically, a sufficient authorization probably exists. 18 If a statute
does not fall within one of these categories, however, then the precise reach of
the Mitchum standard is unclear and must be determined.

The Clayton Act is a statute in this borderline category requiring interpre-
tation and application of the Mitchum standard. Thus, it is unclear whether a
private party seeking federal relief under the Clayton Act for alleged antitrust
violations can get injunctive relief from a federal court to stay a state court pro-
ceeding, and this is precisely the problem sought to be resolved in Kurek.

In Vendo Co. v. Lektro-Vend Corp., 19 the Supreme Court addressed the
issue that proved to be dispositive in Kurek. Is Section 16 of the Clayton Act, 20

§ 2283, Reviser's Note (1970). For a more detailed discussion of the anti-injunction statute
see C. WRIGHT, LAW OF FEDERAL COURTS § 37 (3d ed. 1976).
Reaves & Golden, The Federal Anti-Injunction Statute in the Aftermath of Atlantic Coast Line
16 407 U.S. at 238.
17 See C. WRIGHT, supra note 12, at 203.
18 Id.
Corp.: One Step Forward, Two Steps Back, 44 Brooklyn L. Rev. 317 (1978); Note, Vendo Co.
v. Lektro-Vend Corp.: The Interface of the Clayton Act and the Anti-Injunction Act, 56 N.
Any person, firm, corporation, or association shall be entitled to sue for and have
injunctive relief, in any court of the United States having jurisdiction over the parties,
against threatened loss or damage by a violation of the antitrust laws, including sec-
tions 13, 14, 18, and 19 of this title, when and under the same conditions and princi-
bles as injunctive relief against threatened conduct that will cause loss or damage
is granted by courts of equity, under the rules governing such proceedings, and upon
the execution of proper bond against damages for an injunction improvidently granted
and a showing that the danger of irreparable loss or damage is immediate, a prelimi-
inary injunction may issue. . . .
which permits private injunctive relief in federal court against Sherman antitrust violations, an exception to the Anti-Injunction Act? In particular, can a party seeking antitrust relief in federal court under the Clayton Act seek to enjoin a state court proceeding brought by the party against whom he is seeking relief in federal court?

The plurality opinion in *Vendo Co.* indicates that the Clayton Act does not constitute an express Congressional exception to the Anti-Injunction Act.\(^\text{21}\) Were this the *holding* of the Supreme Court, *Kurek* would be a simple case; no injunctive relief could be granted. Six justices were of the opinion, however, that the Clayton Act *is* an expressly authorized exception to the Anti-Injunction Act. The four dissenting justices maintain that the Clayton Act is a *per se* exception.\(^\text{22}\) Two concurring justices suggested that although the Clayton Act is an exception to the Anti-Injunction Act, the circumstances required to trigger the exception were not present in *Vendo Co.* and thus joined the plurality in denying injunctive relief.\(^\text{23}\)

According to the concurring opinion of Justice Blackmun, a plaintiff seeking injunctive relief under the Clayton Act is required to show a pattern of baseless repetitive claims or some equivalent grave abuse of the state court system for a federal court to issue an injunction to stay a state court proceeding. On a lesser showing, such an injunction may not be issued.\(^\text{24}\)

Although six justices of the Supreme Court are apparently prepared to hold that the Clayton Act is an expressly authorized exception to the Anti-Injunction Act, this is not yet a holding of the Supreme Court. Thus, *Vendo Co.* is of dubious precedential value. Further, only two justices adopted the Blackmun standard for deciding when an injunction may properly issue, and neither the meaning nor justification of the Blackmun standard is clear. Nonetheless, the Seventh Circuit relied on the Blackmun standard as the basis for its holding in *Kurek.*\(^\text{25}\)

IV. The Seventh Circuit's Analysis

The issue presented in *Kurek* is to determine whether a federal court has the power to enjoin collection of the state judgment against the golf professionals. The Seventh Circuit concluded that it could not issue the injunction. Although a number of approaches might justify this result, the Seventh Circuit relied on an application of the Blackmun standard proposed in *Vendo Co.*

The crux of *Kurek* is the judgment by the Seventh Circuit that the Blackmun standard had not been met. The court explained:

\(^\text{21}\) 433 U.S. at 641.
\(^\text{22}\) *Id.* at 654 (Stevens, J., dissenting). Justice Stevens' dissent was joined by Justices Brennan, White and Marshall.
\(^\text{23}\) *Id.* at 643 (Blackmun, J., concurring). The Chief Justice joined the concurring opinion.
\(^\text{24}\) *Id.* at 644. For an analysis of each element of the Blackmun standard, *see* text accompanying notes 29-33 *infra.*
\(^\text{25}\) Full faith and credit, comity, federalism and the collateral attack on the state judgment are all mentioned as possible bases for the holding in *Kurek.* None of these alternatives was explored, however, and hence lend no analytical support to the result reached in *Kurek.* The justification of *Kurek* stands squarely on the authority of *Vendo Co.*
Reading the opinions as indicating that at least if the exceptional circumstances described in the concurring opinion are made out, the court could grant an injunction under the Clayton Act, we are not persuaded that such circumstances have been shown here. Mr. Justice Blackmun, writing for himself and the Chief Justice referred to a pattern of baseless repetitive claims or an abuse of the state adjudicative process as a prerequisite to issuance of an injunction. He found that Vendo was not using the state court proceedings as an anti-competitive device in and of itself. In the case before us, the golf pros attempt to show us that this was done and suggest strongly that park district misled the Illinois courts. We decline, however, to give credence to these conclusionary assertions. Golf pros at all times participated in the state proceedings and although some ex parte rulings were made, golf pros were there given an opportunity to, and did, seek to set aside the challenged rulings. There is no showing that there was a failure of due process in the picture which has been presented to us. The state litigation which was vigorously contested appears to us to come within the ambit of Mr. Justice Blackmun’s finding in Vendo that the state court proceedings were not an anti-competitive device in and of themselves.  

The Kurek rationale is a cautious one. On the one hand, the Seventh Circuit rejects the plurality opinion in Vendo Co. that injunctions cannot issue under the Clayton Act. Thus, the Seventh Circuit apparently believes that the Clayton Act is an expressly authorized exception to the Anti-Injunction Act. At the same time, the Seventh Circuit adopted the Blackmun standard as determinative of what factual showing was required for an injunction to issue. Finding the factual showing insufficient, the injunctive relief was denied.  

A second possible exception to the Anti-Injunction Act exists in that a federal court may issue an injunction if it is “necessary in aid of its jurisdiction.” The Seventh Circuit dismissed this principle as a basis for issuing the injunction. The justification for dismissing such a claim is a reference to the plurality opinion in Vendo Co. in which it was claimed that “no case of this Court has ever held that an injunction to ‘preserve’ a case or controversy fits within the ‘necessary in aid of its jurisdiction’ exception; neither have the parties directed us to any other federal court decisions so holding.” Hence, the motion for injunctive relief was denied.  

V. Analysis  

The Kurek result was justified on the grounds that the Blackmun standard in Vendo Co. had not been met. Consequently, in order to assess the holding in Kurek properly, a close examination of the Blackmun standard is required. In Vendo Co., Justice Blackmun argued,
I would hold that no injunction may issue against currently pending state-court proceedings unless those proceedings are themselves part of a “pattern of baseless, repetitive claims” that are being used as an anti-competitive device, all the traditional prerequisites for equitable relief are satisfied, and the only way to give the anti-trust laws their intended scope is by staying the proceedings.29

The meaning of this test is unclear. No content is given to the concept of an anti-competitive device as evidenced by a “pattern of baseless, repetitive claims.” Further, no indication is given of the circumstances that might invoke the concept of giving the antitrust laws their intended scope by staying a state proceeding.

Notwithstanding these difficulties, one might argue that these conditions are individually necessary conditions for granting injunctive relief, and consequently, the failure of even one condition is sufficient to deny the injunction. Apparently, this was the Seventh Circuit’s reasoning in Kurek. Since no “pattern of baseless repetitive claims” had been shown, the injunction could not issue. Hence no other element in the Blackmun standard need be analyzed to reach the Kurek result.

Such an analysis, however, is unduly restrictive. Even the initiation of a single judicial proceeding could constitute part of a wider scheme to violate the antitrust laws. Accordingly, neither the logic nor the policy involved in granting injunctive relief under the Clayton Act depends on a violation committed by a multiplicity of lawsuits as opposed to a violation involving only one lawsuit.30

Justice Blackmun is not insensitive to this point, and accordingly, he suggests an alternative test: an injunction may issue from a federal court by showing either a pattern of baseless repetitive state claims or “some equivalent grave abuse of the state courts.”31 Yet, the meaning of equivalent grave abuse is left undetermined by the remainder of the opinion.

The foregoing analysis of the Blackmun standard undermines the justification given by the Seventh Circuit for the result in Kurek. There is no question that pressing the enforcement of a state court judgment while the antitrust litigation continues could fall well within the ambit of the “equivalent grave abuse” standard. Since this is so, the failure to show a “pattern of baseless repetitive claims” should not have been fatal to the argument of the golf professionals.

If so, the Seventh Circuit should have explored the meaning of “equivalent grave abuse” to justify the Kurek result. Although the Seventh Circuit refused to find any equivalent showing of grave abuse on the facts of Kurek,32 no

29 433 U.S. at 644.
30 The standard of “baseless repetitive claims” is taken from Justice Douglas’ opinion in Cal. Motor Trans. Co. v. Trucking Unlimited, 404 U.S. 508, 513 (1972). To be sure, the Vendo Court was split on both the meaning and significance of the “baseless repetitive claims” standard. See 443 U.S. at 644 (Blackmun, J., concurring) and 443 U.S. at 661 (Stevens, J., dissenting). Since Justice Blackmun does suggest an alternative test (see text accompanying note 31 infra), adjudication of the dispute over the “baseless repetitive claims” standard is not required for present purposes. In theory, Justice Blackmun would issue an injunction on a showing of something other than a pattern of “baseless repetitive claims.”
31 433 U.S. at 644 n.1.
32 574 F.2d at 895.
analysis of the concept is given by the *Kurek* court. Since a showing of "grave abuse" would have made federal injunctive relief permissible, a search of the *Kurek* facts for such abuse was warranted. Further, without this explication of "equivalent grave abuse," the standard employed to justify the result in *Kurek* is indeterminate. Consequently, no adequate justification is given by the Seventh Circuit for the result in *Kurek*.

No clear standard emerges from *Vendo Co.* as controlling. Rather, a number of principles are suggested, each with little justification and each giving little direction to determine how the standard might apply to different fact situations. *Kurek*, rather than advancing toward clarifying the uncertainty left after *Vendo Co.*, merely reflects this uncertainty. As a result, no progress has been made toward formulating coherent guidelines for future application by district courts.

A more serious problem with the rationale of *Kurek* is the use of the Blackmun standard as dispositive. The Supreme Court has not yet given a definitive opinion concerning the Clayton Act as an exception to the Anti-Injunction Act, and only two justices have expressed a preference for the Blackmun standard. Given the lack of available precedent on the relevant issues, a more perspicuous approach to the problem in *Kurek* could have been anchored in an analysis of the policies served in granting or denying federal injunctive relief in factual situations like the one involved in *Kurek*. When these issues are definitively decided in the Supreme Court, the quality of this policy analysis—and not the application of indeterminate and unjustified standards—will be dispositive.

VI. Conclusion

*Kurek* yields two hints about the future of the Clayton Act as an exception to the Anti-Injunction Act in the Seventh Circuit. First, it seems clear that the plurality opinion in *Vendo Co.* regarding the Clayton Act as an exception to the Anti-Injunction Act has been rejected. On a proper showing, the Seventh Circuit apparently would issue an injunction. Second, the Blackmun standard seems to be the standard that will be followed in the Seventh Circuit in determining when an injunction can issue. What is clear about this standard is that it will take an extraordinary showing to justify the stay of a state court proceeding by a federal court.

Nothing in this comment suggests that the result in *Kurek* is wrong and this is easily demonstrated. In *Vendo Co.*, specific findings of likelihood of ultimate success on the merits, likelihood of irreparable harm, and protection of the public

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33 The only clue as to what constitutes "equivalent grave abuse" is the reference in *Kurek* to the fact that there was no failure of due process in the state court proceedings. 574 F.2d at 895-96. The use of due process language adds further uncertainty to the meaning of "equivalent grave abuse," for there are a number of possible interpretations of "due process" with respect to the granting of the injunction under analysis. First, the Seventh Circuit may mean to imply that some violation of due process is a necessary condition for an injunction to issue. Second, the court may be suggesting that a violation of due process is one of a number of other (unspecified) conditions that meet the *Vendo Co.* standard. Third, the Seventh Circuit may merely have used infelicitous language. The due process issue is not reached by the *Vendo Co.* Court and hence it is difficult to specify what genuine justificatory role, if any, the due process element plays in *Kurek*.
interest were made by the district court, and an injunction issued and was upheld by the Seventh Circuit. The Supreme Court reversed. No such findings of fact were made in *Kurek*, and if the injunction did not properly issue in *Vendo Co.*, then *a fortiori*, it should not issue in *Kurek*.34

Whatever the rationale for *Kurek*, however, the justification given for the analysis is flawed by the dubious value of *Vendo Co.* as a precedent. Thus, little has been established in the way of setting rational guidelines with respect to the issuance of injunctions under the Clayton Act as an exception to the Anti-Injunction Act.

*Harold F. Moore*

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34 Even if the application of a *standard* for analyzing a given fact situation justifies injunctive relief, such a result yields only the permissibility of injunctive relief. A federal court may still decide, perhaps on grounds of comity, that a federal injunction should not issue to stay the state court proceeding. *See* Mitchum v. Foster, 407 U.S. 255, 243 (1972); Atl. Coast Line R.R. v. Bhd. of Locomotive Engineers, 298 U.S. 281, 286-87 (1970).
I. Introduction

On April 20, 1973, appellant Raymond Leannais was injured while operating a coil slitting machine incident to his employment at Fullerton Metals Company in Milwaukee, Wisconsin. The machine on which the appellant was injured had been manufactured by Forte Equipment Company and sold to Fullerton in 1964.

In late 1967, Forte sold its assets to Cincinnati, Inc., the defendant-appellant, for cash and certain employment agreements. Cincinnati, Inc. created a subsidiary, Cincinnati-Forte, to accept the Forte assets. The subsidiary was dissolved in 1973 after the assets were purchased by Cincinnati.

In the purchase agreement between Cincinnati and Forte, Cincinnati expressly limited its liability for personal injuries caused by Forte-produced machines to five years from the December 6, 1967, closing date of the contract, and agreed to use its best efforts to secure insurance against such claims during that time. No other liability for personal injury was assumed.

In this diversity action, Leannais and his wife sought damages from Cincinnati, Inc. and Cincinnati-Forte Co., the corporate successors to the original manufacturer of the machine. The complaint alleged strict liability in tort, negligence in the design and manufacture of the machine, and failure to warn potential users after serious injuries had occurred. After reviewing the affidavits submitted by both parties, the United States District Court for the Eastern District of Wisconsin granted summary judgment in favor of defendant-appellee.

The United States Court of Appeals for the Seventh Circuit, applying the law of Wisconsin, reversed and remanded. The court held: (1) the district court properly held that Cincinnati, the corporate successor to the manufacturer of the machine, did not assume the liabilities of the transferor corporation by virtue of the purchase of assets; (2) the district court properly found that the record

* 565 F.2d 437 (7th Cir. 1977).

1 Cincinnati, Inc. (hereinafter cited as Cincinnati) is an Ohio corporation; appellant is a resident of Wisconsin. Jurisdiction is invoked under 28 U.S.C. §1332 (1970). Cincinnati-Forte was later dismissed from the suit.

2 The general rule in the majority of American jurisdictions, including Wisconsin, is that a corporation which purchases the assets of another corporation does not succeed to the liabilities of the selling corporation. Bazan v. Kux Machine Co., 358 F. Supp. 1250 (E.D. Wis. 1973). Here, Cincinnati had no part in the design, manufacture, sale or distribution of the allegedly defective machine and the general rule accords with the fundamental principle of justice and fairness, under which the law imposes responsibility for one's own act and not for the totally independent acts of others. There are, however, four well-recognized exceptions to the general rule under which liability may be imposed on a purchasing corporation: (1) when the purchasing corporation expressly or impliedly agreed to assume the selling corporation's liability; (2) when the transaction amounts to a consolidation or merger of the purchaser and seller corporation; (3) when the purchaser corporation is merely a continuation of the seller corporation; or (4) when the transaction is entered into fraudulently to escape liability for such obligations. 565 F.2d at 439 (citing Bazan v. Kux Machine Co., 358 F. Supp. 1250 (E.D. Wis. 1973) and Forest Laboratories, Inc. v. Pillsbury Co., 452 F.2d 621 (7th Cir. 1971)).
here did not indicate the existence, under Wisconsin law, of a cause of action under the “product line” theory\(^3\) of strict liability in tort; and (3) the district court resolution of whether Cincinnati had, and breached, a legal duty to warn Leannais’ employer was improper because the issue turned on material questions of fact\(^4\) to be decided by a jury. Accordingly, the summary judgment in favor of Cincinnati was reversed.

The product line theory in *Leannais v. Cincinnati, Inc.* presented the Seventh Circuit with a products liability question under Wisconsin law. In ruling on the cause of action under the product line theory, the court concluded that neither the record nor the briefs before it contained the slightest indication that the courts of Wisconsin had created or would create such a far-reaching exception to the non-liability of asset-purchasers, a well-established principle which strongly affected the economic decisions of the citizens and corporations of Wisconsin.

The Seventh Circuit cast the product line theory in terms of a broad public policy issue and held that such an issue would best be handled by the state legislature since it possesses comprehensive machinery for public input and debate. The majority reasoned that the Wisconsin Supreme Court would, in an area such as the one presented here, defer to the legislature.\(^5\) This determination concluded the court’s analysis of the product line theory; no attempt was made to discern the merits of the theory under the current Wisconsin law.

II. The Scope of This Inquiry

*Leannais v. Cincinnati, Inc.* is an important case because of what it does not, or appears not to do. This diversity action, brought in the federal court to adjudicate a products liability question, presented a theory never before addressed by the courts of the forum state. The Seventh Circuit, faced with a classic dilemma of a federal court applying the appropriate state law as required by the doctrine of *Erie R. Co. v. Tompkins*,\(^6\) concluded that the highest court of Wisconsin, if it were confronted with this precise issue, would defer to the legislature to formulate extensions of the law in the products liability area. The

\(^3\) The product line theory of strict liability in tort is set forth in the California case of Ray v. Alad Corp., 136 Cal. Rptr. 574, 560 P.2d 3 (Ct. App. 1977). In *Ray*, a ladder manufacturer in 1968 was sued for injuries allegedly caused by a ladder manufactured by the transferor corporation in 1952. The court propounded a theory that, henceforth, product liability should run with the manufacturing business as such. No inquiry should be made as to the corporate principals of merger, consolidation or asset purchase surrounding the transfer of the business to the successor corporation. The rule of liability is to be one of tort, and not of corporate law, with liability following the business as long as it retained its distinctive identity or character.

\(^4\) Cincinnati, Inc. assumed all service obligations of Forte. Whether Cincinnati’s succession to the service contracts provides sufficient nexus to establish a legal duty to warn Leannais’ employer of the dangerous condition of the particular machine here involved, or of prior serious injuries incurred on other machines, is unclear from the bare pleadings and affidavits of record, and must await determination on remand. The existence of such a duty may be dependent upon such unanswered factual questions as whether the particular machine involved was under a service contract, whether Cincinnati had ever serviced that machine, or whether Cincinnati had information on present or prior ownership of Forte-built machines. 565 F.2d at 442.

\(^5\) The court cited as support for this conclusion, Holifield v. Setco Industries, Inc., 42 Wis.2d 750, 168 N.W.2d 177 (1969).

\(^6\) 304 U.S. 64 (1938).
court's holding on the product line theory was predicated on a single Wisconsin case of questionable relevance. The specific case cited as support by the court, Holifield v. Setco Industries, Inc., raised an issue clearly distinct from the one presented to the Seventh Circuit here; the citation of Holifield was inappropriate to resolve the precise question before the court.

In rendering a judicial opinion, the process is as important as the outcome. In this instance, the Seventh Circuit neglected the process in favor of the outcome in its abbreviated Erie analysis. The court forfeited the opportunity to rule on an issue of significant import which was properly before it. Furthermore, the court may have damaged the image of the federal judiciary as the authoritative forum for the determination of state law in cases involving parties of diverse citizenship.

The relative merits of the product line theory will not be debated here, nor will the actual outcome of the case be challenged. Rather, this analysis is directed to the incomplete reasoning of the Seventh Circuit, to the departure by the Seventh Circuit from traditional avenues of inquiry available to a federal court under Erie, and to the broad declaration by the Seventh Circuit of the proper scope of judicial power.

III. The Erie Doctrine

In 1938, the Supreme Court of the United States rendered its decision in Erie R. Co. v. Tompkins. Mr. Tompkins had been injured in Pennsylvania by a freight train while walking on a path beside the tracks of the Erie Railroad Company. He brought suit in the United States District Court for the Southern District of New York and recovered a judgment of $30,000 against the railroad. The railroad appealed on the ground that, under the Pennsylvania law, Tompkins could not claim the status of licensee, but only that of a trespasser since he was on a path which ran along, not across, the tracks. The circuit court affirmed on the basis of general law without examination of the Pennsylvania cases. The Supreme Court reversed and remanded the case to the appellate court for a determination of the local law which it held to be controlling.

The Erie Court held that the term "laws of the several states" in the Rules of Decision Act included all state law, decisional as well as statutory, general as well as local. Writing for the Court, Mr. Justice Brandeis suggested that this construction of the Act was constitutionally compelled:

7 42 Wis.2d 750, 168 N.W.2d 177 (1969).
8 304 U.S. 64 (1938).
9 Tompkins v. Erie R. Co., 90 F.2d 603 (2d Cir. 1937).
10 On remand, Tompkins v. Erie R. Co., 98 F.2d 49 (2d Cir.), cert. denied, 305 U.S. 637, rehearing denied, 305 U.S. 673 (1938). The Second Circuit, following the Supreme Court directive, reversed, determining that Pennsylvania law denied Tompkins recovery. Accordingly, the action was dismissed and the Supreme Court denied further review.
11 The Rules of Decision Act, Section 34 of the Judiciary Act of 1789, provided that "[t]he laws of the several states, except where the Constitution, treaties or statutes of the United States shall otherwise require or provide, shall be regarded as rules of decision in trials at common law in the courts of the United States in cases where they apply." The Act underlies the whole of the Erie Doctrine. 28 U.S.C. §1652 (1970).
Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State. And whether the law of the State shall be declared by its Legislature in a statute or by its highest court in a decision is not a matter of federal concern. There is no federal general common law. Congress has no power to declare substantive rules of common law applicable in a State. . . . And no clause in the Constitution purports to confer such a power upon the federal courts. 15

As a matter of constitutional law, Mr. Justice Brandeis argued, Congress had no lawmaking authority over a class of state substantive issues; thus, lawmaking by the federal courts on such matters must also be beyond the constitutional authority of the federal government. 13

Underlying Erie is the policy that, in any given controversy, the selection of a federal court as a forum rather than a state court "a block away" 14 should not lead to a substantially different result. Consequently, the doctrine demands that in a diversity action in a federal court, the law of the forum state must govern the federal court in ruling on the merits. 15

The Erie Doctrine, as modified by Guaranty Trust Co. v. York, 16 also described the proper distribution of power between federal and state courts. When a federal court has jurisdiction over a case involving a state right solely because of the diversity of the parties, the court acts only as another court of the state. The federal court cannot award recovery if recovery would be unavailable under state law, nor can the court substantially alter the enforcement of the right as defined by the state. Once a federal court undertakes to apply state law to any or all issues in a particular case, the court is presented with the task of ascertaining exactly what the state law is. The mandate of Erie is unmistakable; the federal court is bound to ascertain and apply state law, whether it be decisional or statutory.

When the state's highest court has not acted, the federal court's duty is to predict what the highest state court would rule if confronted with the issue and not to formulate state law. 17 Accordingly, the federal court will employ all available legal resources in an effort to ascertain accurately the law of the forum state. Legislative expressions or intent may be considered, as well as well-reasoned lower state court decisions. Virtually any reliable data tending to show what the state law is may be considered within the scope of federal court inquiry. Pursuant to anticipating an analysis which would be outlined by a state court, relevant decisions in other jurisdictions, the principles of common law, other federal court decisions, the American Law Institute's Restatements of the Law, opinions of attorneys-general as well as scholarly treatments of the law including law reviews and hornbooks may also be granted some weight in the court's

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12 304 U.S. at 78.
15 Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487 (1941). The law of the forum state as controlling the case includes state choice of law rules. Hence, the federal court should apply the law which the state court would apply.
17 See text accompanying notes 27-39 infra.
In ruling in a diversity action, the federal court is bound to look at the full range of legal sources which a state court would examine in reaching a decision. The thrust of the Erie Doctrine is that the federal court is not at liberty to choose the rule it would adopt for itself were it free to do so, but rather must choose the rule it believes the state's highest court would adopt under these circumstances.

IV. Leannais v. Cincinnati, Inc.: The Erie Doctrine in the Seventh Circuit

Leannais is a diversity case squarely within the parameters of an Erie inquiry. The Seventh Circuit had to apply Wisconsin state law to an issue not yet addressed by any court in the forum state. Ignoring jurisprudence on both the process of the Erie Doctrine and the substantive issue, the court declined to address the products liability issue, characterizing it as an area of broad public policy consideration. As a public policy consideration, the products liability issue was deemed to be controlled by Holifield v. Setco Industries, Inc. and thus required deference to the state legislature. The Holifield case, however, which was so fundamental to the integrity of the court's opinion here, is readily distinguishable and does not support the holding of the Seventh Circuit.

The precise issue before the Holifield court was the time at which the Wisconsin statute of limitations began to run in a products liability case. The duration of liability, a question of legislative choice, is totally distinguishable from the issue in Leannais of the very existence and scope of corporate liability, a question usually resolved by a court. Statutes of limitation are, by definition, statutory. The statutes reflect particular legislative judgments, often arbitrary, concerning the temporal limitations to distinct classes of causes of action. Ordinarily, these laws are regarded as statutes of repose which do not involve matters of substantive rights but are available only as defenses. Courts have held that these statutes are for the benefit and repose of individuals and not to secure general objects of policy and morals. Unlike statutes of limitation, the product line theory does raise a substantive issue: does liability exist at all? The competing factors, including policy considerations, which would affect the determination of liability, at least in the first instance, might be better handled by the courts, which have traditionally been immune from the pressures of various interest groups and lobbies. A disinterested judiciary would be better able to weigh the questions of justice and fairness which necessarily attend this analysis. Furthermore, the courts have traditionally controlled the expansion of the products liability field. The citation of Holifield by the court was both inaccurate and unfortunate. By misconstruing the decision in Holifield, the Seventh Circuit relied on an irrelevant case thus forfeiting an opportunity to contribute significantly to the growing body of products liability law. The Seventh Circuit's pre-

18 I Moore's Federal Practice ¶ 0.307, at 3077 (1978).
20 As a matter of historical fact, the courts have traditionally determined the character and bounds of products liability law. See generally Thomas v. Winchester, 6 N.Y. 397 (1852); MacPherson v. Buick Motor Co., 217 N.Y. 382, 11 N.E. 1050 (1916); Henningsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A.2d 69 (1960).
mature termination of its analysis precluded an examination of an important amount of Wisconsin state law which may have affected the courts holding on the issue of product line liability.

In 1967, the Wisconsin Supreme Court first applied the rule of strict liability in tort to the manufacturers and sellers of defective goods in *Dippel v. Sciano.* Although the facts of *Dippel* make the case distinguishable from *Leannais,* the focus and direction of the former opinion are directly relevant to the question presented in the latter. Consequently, the Erie Doctrine would compel an analysis of the factors which gave rise to the holding in that case; the discussion of expanded consumer protection in *Dippel,* when read in light of contemporary experience, could have contributed to a fruitful analysis in *Leannais.* The significance of the court's departure from an accepted manner of proceeding in a diversity action becomes more pronounced when compared to its treatment of such cases in the past as well as the treatment accorded such cases by other circuit courts.

Two weeks prior to its decision in *Leannais,* the court rendered a decision in an analogous case, *Huff v. White Motor Corp.* The two cases were similar in that they were both diversity actions involving questions of products liability law. In neither situation had the respective state supreme court rendered a controlling decision. Additionally, in both cases, the lower federal court failed to engage in an *Erie* analysis.

The *Huff* case presented the Seventh Circuit with the issue whether, under Indiana law, a manufacturer had a duty to design a vehicle so as to eliminate or diminish the risk of injury which would be sustained in a collision. Although the Seventh Circuit itself had formulated a rule in an earlier Indiana case that would deny liability here, the rule had become a distinct minority position among the other American jurisdictions. The question presented in *Huff* was not novel; numerous rulings of Indiana state courts had expressed increasing support of the basic policy considerations justifying the imposition of the broader majority rule. In outlining its approach to a decision, the Seventh Circuit stated that, "[t]he federal court must decide what rule the Indiana Supreme Court would adopt in such a case and apply it. In doing so, that court should consider all the data which the highest court of the state would consider." Having determined that the Supreme Court of Indiana would apply the majority rule, the court was compelled to abandon its own minority position and overturn the earlier rule which it had formulated. The Seventh Circuit thus undertook a complete

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21 3 Wis.2d 443, 155 N.W.2d 55 (1967).
22 565 F.2d 104 (7th Cir. 1977).
24 The presence in the *Huff* situation of a number of lower Indiana state court cases somewhat distinguishes it from *Leannais* but does not justify the disparity in the depth of treatment between the cases. The effect of these cases might have been to circumscribe the research and analysis of the Seventh Circuit in *Huff.* The actual reasoning, nevertheless, was still precise and exhaustive. *Leannais,* on the other hand, was decided without the benefit of state court guidance. The Seventh Circuit's analysis, however, fell far short of the effort made in *Huff.* It would seem reasonable that the Seventh Circuit sitting as a state supreme court would expend more effort in analysis where the lower courts had not done any work.
25 565 F.2d at 106.
examination of the relevant law and arrived at its conclusion only after exhaustive research.

Fourteen days later, however, the Seventh Circuit, in Leannais, asserted that no authority existed to guide its reasoning and terminated its analysis after a cursory reading of a single case of questionable relevance. The issue in Leannais was novel; the product line theory was a recent innovation of the California courts. Furthermore, jurisprudence on product line theory was scarce. The Leannais situation thus allowed the court infinitely more latitude in terms of its analytical scope than did the Huff case. Yet the court’s analysis in Leannais was more confined and rigid than in Huff. Since the two cases were similar procedurally in that they both required extensive Erie analysis, the variant treatment accorded the cases by the Seventh Circuit is disconcerting. The Huff decision is emblematic of honest judicial inquiry and is illustrative of traditional Erie procedure. The opinion explored all relevant and proper avenues of jurisprudence and resolved the issue in a manner calculated to mirror that of the forum state’s supreme court. The opinion in Leannais, however, is an exercise in conclusionary decision writing. The opinion is a superficial analysis of only a fractional portion of the law which the state court would actually have scrutinized.

Factual differences in the two cases adequately explain different substantive outcomes but cannot account for the unjustified analytical differences in the cases. Two federal diversity proceedings involving analogous issues before the same federal court should have received similar analytical treatment. The nature of the products liability issue did not relieve the Seventh Circuit of the obligation to engage in a thorough Erie analysis. The overriding principle of the Erie Doctrine is that it applies irrespective of the issue involved. The universality of the principle is illustrated by the following cases in which Erie was applied in a variety of legal contexts in other circuit courts of the United States.

V. The Erie Doctrine Among the Circuits

The pattern of application of the Erie Doctrine in the circuit courts of the United States is remarkably uniform. The doctrine is well established and admits of only minor deviation. Moreover, the uniform pattern appears unaffected by the nature of the issue presented by each individual case. Whether the issue is novel or familiar, controversial or commonplace, or traditionally within the ambit of either the legislature or judiciary, the courts’ application of fundamental Erie Doctrine principles remains unaffected. The consistency which characterizes the treatment of diversity cases under Erie is highlighted in this section with particular attention given to the nature of the issue presented to the court and the specific factors which tended to be the most decisive in the court’s estimation. Here, at the juncture of federalism, jurisprudence and public policy,

will the workings of the federal courts in cases involving parties of diverse citizenship become most clear.  

The First Circuit's per curiam opinion in *Mustapha v. Liberty Mutual Insurance Company* involved a question of interpretation of the Rhode Island Workman's Compensation Act. *Mustapha* was a case of first impression and the problem of statutory interpretation under this statutory cause of action was traditionally a judicial task. Originally, the suit had been brought as common law negligence; however, the court's research had revealed no Rhode Island rulings which provided reasonable guidance. Invoking the Erie Doctrine, the First Circuit distinguished a lower state court case, cited by counsel as relevant, which the court believed would be inappropriate as part of the analysis of the state’s highest court. Hence, even in this area of the law which exists solely by legislative fiat, the court pursued an *Erie* analysis beyond state statutory law and gave meaning to the state enactment by critical examination of state cases.

Corporation law, also exclusively the creation of state legislation, was the basis of the action in *Schein v. Chasen*. *Schein* involved a question of joint and several liability under state corporation law for profits realized from trading in stock with confidential information. As in *Mustapha*, *Schein* was introduced under a common law theory (fraud), there was no clearly enunciated state rule upon which the circuit court could rely, and the issue again was one of statutory interpretation. The Second Circuit pursued its *Erie* analysis, finding guidance in the law of other jurisdictions and the Restatements of the American Law Institute. *Mustapha* and *Schein* thus employed common law principles to deal with modern statutory causes of action in the absence of authoritative state court decisions. The mere fact that the legislature had given birth to those legal rights did not affect the treatment of those rights under the doctrine of *Erie R. Co. v. Tompkins*.

The Uniform Commercial Code, unquestionably a product of legislative impetus, has both created new causes of action and codified old ones. When the Third Circuit was required to interpret a specific provision of the Pennsylvania Uniform Commercial Code (UCC) for the first time, no decisions of the Pennsylvania Supreme Court or lower Pennsylvania courts were found to be applicable to the issue. In addition, the court found a dearth of relevant cases on the issue in other circuits. The Third Circuit discerned the projected holding of the Pennsylvania Supreme Court by considering the legislative intent behind the Code, the comments of the drafters, and, not surprisingly, the public policy of business and banking stability. The court’s function here was essentially an interpretive one; it construed the statute as courts traditionally have done in

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27 The first three cases were selected to demonstrate that, even in areas of law specifically developed by the legislature, federal courts in diversity actions will, nevertheless, try to ascertain what reading the state supreme court would give to the law in question. Theoretically, the court in *Leannais* did this but with only one citation of case law and no reasoning. These cases will highlight the avenues of inquiry missing in the *Leannais* decision.
28 387 F.2d 631 (1st Cir. 1967).
30 478 F.2d 817 (2d Cir. 1973).
31 PA. STAT. ANN. tit. 12A, §3-405 (1)(c) (Purdon).
typical Erie Doctrine applications. It is clear that if a federal court is to be true to the mandate of Erie, i.e., to sit as an appellate court of the forum state, it is compelled to examine the panoply of factors which a state court would actually consider.

A more traditional cause of action was presented to the Fourth Circuit in Sherby v. Weather Brothers Transfer Company, a diversity action based on negligence. This legal theory differs from those present in the prior cases in that negligence is more susceptible of judicial development and expansion than are the statutory causes of action. Again, however, the federal court was without relevant state court guidance. Nevertheless, the Fourth Circuit's treatment of the negligence issue was consistent with the treatment of the statutory issues above:

In the absence of a state statute or a controlling decision on point, a federal court will attempt to determine what the highest state court would hold if confronted with the same issue. Considered dicta in opinions of the highest state courts should not be ignored and dictum which is a clear exposition of the law must be followed unless in conflict with other decisions of that court.3

The breadth of federal court discretion under Erie in dealing with a common law cause of action (libel) is evident in a recent Fifth Circuit case, Hood v. Dun and Bradstreet, Inc. Libel, an area which, at times, embraces controversial arguments, would appear to be especially well suited to judicial deference to legislative judgement. The Fifth Circuit noted that:

Federal courts are not immutably bound under Erie R. Co. v. Tompkins to follow state court decisions where it appears that a state court considering the identical issue would not rely on such precedent. The federal court, like the state court, can consider all information and data that the highest court of the state would consider in determining whether strictly to adhere to a prior ruling.3

The court here held that it could anticipate a change in state libel law. The court did not limit its analysis to existing libel cases but went further and reviewed and analyzed questions of public policy. Hood is more significant than the previously cited cases because relevant state precedent did exist which the federal court refused to accept passively. Fulfilling its obligation defined by the Erie Doctrine, the Fifth Circuit aggressively reevaluated the legal reasoning as the state court would and adopted the rule the highest court would enunciate.

The Seventh Circuit had recently addressed the issue of contributory negligence in the products liability setting in Collins v. Ridge Tool Company. Like Leannais, Collins was a diversity action requiring the application of Wisconsin law. Prior to Collins, the Seventh Circuit had favored the "open and obvious"
rule, a theory based on New York and Indiana law. The court here, however, reiterated that the main objective of its ruling in a diversity action would be to resolve the issues as would the Wisconsin Supreme Court under the same circumstances. The decision is virtually indistinguishable procedurally from any of the cases in the foregoing analysis. The Seventh Circuit did not suggest that the issue of products liability was in any way distinguishable from other substantive legal questions for purposes of analysis. The opinion did not contain an indication that the question was beyond judicial competence or called for legislative answers. The Seventh Circuit, in this case at least, discerned no compelling interest in deferring the task to an alternate branch of government. The issue was squarely and properly before the court and was resolved by the court.

A consideration of recent Erie Doctrine applications mandates the conclusion that the issue before the federal court, be it liberal or conservative, judicial or legislative, traditional or innovative, should not affect the nature or the depth of the treatment rendered by the federal court sitting in a diversity action. Unless radical factual situations or policy considerations demand a different approach, the federal court should pursue the Erie analysis to its complete and accurate legal conclusion.

VI. Leannais v. Cincinnati, Inc.: A Postscript

The major issue unaddressed by the Seventh Circuit in Leannais v. Cincinnati, Inc., the product line theory, may itself provide the explanation for the departure from such a well-established postulate of federal civil procedure. Does extension of products liability theory to a product line approach require a deferential judicial treatment or occasion judicial restraint? Products liability law has developed so rapidly that its ultimate effects and implications are not yet fully clear. The Leannais case presented the Seventh Circuit with a volatile but vital issue and an opportunity to clarify and define fundamental unanswered questions of state law. Clearly, the product line theory is a new and controversial response to expanded notions of corporate responsibility. Nevertheless, the case provided an excellent vehicle for the court by their reading of Wisconsin law either to reaffirm old principles or erect bold new standards in products liability.

The opinion in Leannais confesses a certain amount of result-orientation. Fearful of controversy, the Seventh Circuit was reluctant to discuss an area of law which had direct and significant impact on legal relationships within its jurisdiction. The thrust of the preceding analysis, however, is that the Erie Doctrine compels a full and fair analysis of state law irrespective of the issue involved. The complexity of products liability law does not, of itself, counsel judicial restraint. Indeed, the courts are best suited to treat the intricate legal

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38 The open and obvious rule means that a manufacturer of a product is under no duty to guard against or give notice of dangers which are obvious or patent to the user. The rule was originally articulated in Campo v. Scofield, 301 N.Y. 468, 95 N.E.2d 802 (1950).

39 Meredith v. City of Winterhaven, 320 U.S. 228 (1943). "In the absence of some recognized public policy or defined principle guiding the exercise of jurisdiction conferred, which would in exceptional cases warrant its nonexercise, it has from the first been deemed to be the duty of the federal courts, if their jurisdiction is properly invoked, to decide questions of state law whenever necessary to the rendition of a judgment." Id. at 234.
doctrines involved in this area in a principled and dispassionate way. Furthermore, the body of products liability law is largely a product of judicial development. Therefore, the abnegation by the Seventh Circuit of its judicial duties under the doctrine of *Erie R. Co. v. Tompkins* was unjustified.

VII. Conclusion

The decision of the Seventh Circuit in *Leannais* was unfortunate for a number of reasons. Notwithstanding the importance of the doctrinal questions presented for the court, care should have been taken not to lose sight of the duty to provide redress to the parties to the controversy. The court's refusal to engage in a full consideration and analysis of relevant sources of the law worked an injustice to the parties involved. Moreover, the Seventh Circuit denied its historic common law duty to foster the growth of the law. The case manifested a need for a well-reasoned appraisal of relevant facts, current needs, and expanded concepts of consumer protection; the Seventh Circuit refused to provide an answer. The Seventh Circuit failed to make an honest analysis of the product line liability theory; the refusal by the court to rule on an issue properly before it affected not only the parties to the litigation, but also other purchasers, consumers and users of goods.

Certainly, the federal courts today operate under the burden of an awesome case load. This burden, however, does not excuse the courts from pursuing a full and fair analysis in each case they accept.

*Russell Thomas Alba*
The need for vigorously protecting the proper exercise of both grand jury and trial jury functions has long been recognized by the judiciary. In United States v. Clavey, the United States Court of Appeals for the Seventh Circuit was confronted with issues relating to the proper conduct of both juries. Clavey involved an attempt to invade the secrecy of the grand jury as well as an attempt to excuse an inappropriate interference with trial jury deliberations.

Traditionally, grand jury proceedings have been cloaked with a veil of secrecy. The veil has generally been lifted only in narrowly circumscribed situations. A growing recognition exists, however, that disclosure of the contents of grand jury proceedings, rather than suppression, ordinarily serves the administration of criminal justice. The general relaxation of barriers protecting the secrecy of the grand jury has been gradual, however, and many courts still rigidly adhere to an inflexible policy of nondisclosure.

The conflict between more liberalized disclosure and traditional adherence to the secrecy of the grand jury proceedings materialized in Clavey. The precise issue addressed by the Clavey court involved fixing guidelines to be met by a witness seeking disclosure of his own grand jury testimony. The court denied release of such testimony because Clavey failed to establish a particularized need which would compel disclosure. To the extent this approach departs from general trends in favor of limited disclosure, the Clavey result merits further analysis.

In Clavey, the Seventh Circuit was also required to address the consequences of private communications between the judge and the deliberating jury. To ensure that the jury trial process is not inappropriately disrupted, courts have carefully scrutinized interferences with jury deliberations. Accordingly, a longstanding rule exists that any communication between the judge and the deliberating jury must be made in the presence of the defendant. To preserve the adversarial context of the trial, defense counsel must have an opportunity to

* 565 F.2d 111 (7th Cir. 1977), vacated, 578 F.2d 1219 (1978) (on the grand jury issue), aff'g by an equally divided court, In re Clavey, No. 71 GJ 3567 (N.D. Ill. Dec. 23, 1974).
2 565 F.2d 111 (7th Cir. 1977).
3 Comment, Grand Jury Secrecy, supra note 1, at 804.
5 See, e.g., cases cited in note 1 supra.
advance suggestions regarding the appropriate content of the communication. If this rule is violated, courts will readily find error.\(^6\)

In \textit{Clavey}, the appellant assigned as error the trial judge's failure to respond to the jury's request for supplementary instructions as well as the judge's failure to advise counsel of the jury's inquiries. The error in the trial judge's conduct was freely admitted.

Such an error does not, however, ordinarily require reversal. The error is excusable if the court finds it harmless. In \textit{Clavey}, the Seventh Circuit found that the wrongful conduct was harmless but failed to enunciate clearly the precise formulation of the "harmless error" test employed in reaching its decision. This failure merits further analysis since a careful application of the generally accepted formulation of this test would seem to have required reversal.

\section*{II. Statement of the Facts}

Sheriff Orville Clavey twice appeared before the Special March, 1974, Grand Jury in the Northern District of Illinois. On both occasions he testified without the assistance of counsel. Approximately five weeks after his second appearance, Clavey retained counsel. The day after retention, his counsel requested that the government produce a transcript of Clavey's grand jury testimony. The request was made in order to enable counsel to advise Clavey whether or not to recant aspects of his testimony pursuant to 18 U.S.C. § 1623(d),\(^7\) which allows a witness to avoid a perjury prosecution by admitting the falsity of certain declarations.

Clavey's request was denied and, on two subsequent occasions, he petitioned the Chief Judge of the United States District Court for the Northern District of Illinois to compel production of a copy of his testimony. Clavey alleged that he was unable to tell counsel the substance of his testimony before the grand jury due to the debilitating effect on his memory of several physical impairments.\(^8\) The court denied both petitions because Clavey had failed to demonstrate with particularity a "compelling necessity" for disclosure.\(^9\)

Clavey was indicted four months later under an eight-count indictment including four counts of false swearing before the grand jury.\(^10\) Clavey moved to suppress the indictment on the ground that he was denied effective assistance of counsel in asserting his right to recant under § 1623(d).\(^7\) This motion was denied.

Clavey went to trial on May 20, 1976. While the jury was deliberating, the foreman sent a note to the court at 5 p.m. on the evening before the verdict was

\begin{itemize}
  \item \textbf{6} 3 C. \textsc{Wright}, \textsc{Federal Practice & Procedure} § 724 (1969).
  \item \textbf{7} 18 U.S.C.A. § 1623(d) (1978) provides:
  \begin{quote}
  Where, in the same continuous court or grand jury proceeding in which a declaration is made, the person making the declaration admits such declaration to be false, such admission shall bar prosecution under this section if, at the time the admission is made, the declaration has not substantially affected the proceeding, or it has not become manifest that such falsity has been or will be exposed.
  \end{quote}
  \item \textbf{8} Clavey claimed that an illness and a skull fracture adversely affected his memory.
  \item \textbf{9} The district court judge who denied Clavey's petition for a transcript did not preside at his trial.
  \item \textbf{10} The eight-count indictment specified four counts of false swearing before the grand jury, three counts of failure to report income on his tax returns, and one count of conspiracy to extort funds from a liquor license holder.
\end{itemize}
reached. The note requested a copy of the court's instructions. Without notifying Clavey or his counsel, the court refused the request. Later, apparently during that same evening, the jury sent another note to the court requesting that the judge clarify some aspects of the indictment. The judge, again without notifying counsel and in the absence of the defendant, refused to answer the question and simply instructed the jury to "continue to deliberate."

The next morning the jury sent another note to the court which said in part: "The counts in the indictment are related to one another, some more than others. For example, count two is related to count five. In this respect, if we find the defendant guilty on count two and on count three, must we also find him guilty on count one?" The court, again without notice to Clavey or his counsel, replied that the jury should "continue to deliberate." Ten minutes later the jury reached a verdict. The jury acquitted Clavey on three of the false swearing counts (1, 2 and 4) and the extortion charge (count 8). Clavey was convicted of one count of false swearing (count 3) and three counts of tax evasion (5, 6 and 7).

On November 10, 1977, Clavey filed a petition for rehearing en banc. The petition was granted, but only with respect to the grand jury issue and, accordingly, the decision of the original panel on this issue was vacated. The Seventh Circuit, after a rehearing en banc, affirmed the order of the district court denying disclosure.

III. Disclosure of Grand Jury Transcripts

A. Policies Supporting Secrecy and the Development of the Standard for Disclosure

As the Seventh Circuit's decision in Clavey evidences, many courts rigidly protect the historical secrecy of grand jury proceedings. The "secrecy of grand jury proceedings" is considered "indispensable." The reasons which lie behind this secrecy have been traditionally summarized as follows:

11 565 F.2d at 118.
12 The judge advised counsel:
   The answer to that [inquiry] was No, because I will not become the thirteenth juror in this case, and I shall not invade the province of the jury, which I did not do. The answer to the question to the jury, carried to them by the deputy United States Marshall, was to "continue to deliberate."
565 F.2d at 118.
13  Id.
14 Although the opinion of the original panel on the issue is no longer authority in the Seventh Circuit, the original opinion still merits careful scrutiny. It is difficult to discern exactly what the Seventh Circuit's position is on the standard to be applied to a witness' request for a copy of his own grand-jury testimony. The majority indicated a departure from Sarbaugh, at least in attitude, and yet the dissent would utilize a completely different approach. Illinois v. Sarbaugh, 552 F.2d 768 (7th Cir.), cert. denied, 334 U.S. 889 (1977). See text accompanying notes 37-42 supra. An analysis of Sarbaugh and Clavey in light of the pertinent case authority and the relevant policy considerations may serve to clarify matters. See text accompanying notes 130-40 infra. Hereinafter the opinion of the majority of the original panel will be referred to as the majority.
(1) To prevent the escape of those whose indictment may be contemplated;
(2) to insure the utmost freedom to the grand jury in its deliberations, and to prevent persons subject to indictment or their friends from importuning the grand jurors;
(3) to prevent subornation of perjury or tampering with the witnesses who may testify before the grand jury and later appear at the trial of those indicted by it;
(4) to encourage free and untrammeled disclosure by persons who may have information with respect to the commission of crimes;
(5) to prevent the innocent accused who is exonerated from disclosure of the fact that he has been under investigation, and from the exposure of standing trial where there was no probability of guilt.\footnote{16}

The protection of the secrecy of the grand jury and of the policy reasons justifying secrecy is presently governed by Federal Rule of Criminal Procedure \footnote{17} 6(e).\footnote{18} Rule 6(e) becomes operative when a person, who does not have access to the grand jury transcript as a matter of right, requests a transcript. Rule 6(e) was applied in \textit{Clavey}, and so a close analysis of the Rule and those decisions which have outlined the standards for disclosure under that Rule is necessary.

Rule 6(e) provides in part that “[d]isclosure otherwise prohibited by this rule of matters occurring before the grand jury may be made—(i) when so directed by a court preliminary to or in connection with a judicial proceeding.”\footnote{19} Thus, the decision regarding the propriety of disclosure rests within the sound discretion of the trial court.\footnote{20} The Rule itself does not define a precise standard. The United States Supreme Court, however, has enunciated guidelines for the exercise of this discretion. The Supreme Court has determined that disclosure should not be made unless the party seeking disclosure has shown a “particularized need” for the transcripts.\footnote{21}

1. Supreme Court Decisions

The “particularized need” standard was first articulated in \textit{United States v. Procter \\& Gamble}\footnote{22} in the context of a discovery request for the production of a

\footnote{17} \textit{Fed. R. Crim. P. 6(e) provides, in relevant part:}
\begin{itemize}
  \item \textit{(e) Secrecy of Proceedings and Disclosure.}
  \begin{itemize}
    \item \textit{(1) General rule. A grand juror, an interpreter, a stenographer, an operator of a recording device, a typist who transcribes recorded testimony, an attorney for the Government, or any person to whom disclosure is made under paragraph (2) (A) (ii) of this subdivision shall not disclose matters occurring before the grand jury, except as otherwise provided for in these rules. No obligation of secrecy may be imposed on any person except in accordance with this rule. A knowing violation of rule 6 may be punished as a contempt of court.}
    \item \textit{(2) Exceptions.}
    \begin{itemize}
      \item \textit{(C) Disclosure otherwise prohibited by this rule of matters occurring before the grand jury may also be made—}
    \begin{itemize}
      \item \textit{(i) when so directed by a court preliminarily to or in connection with a judicial proceeding; or}
      \item \textit{(ii) when permitted by a court at the request of the defendant, upon a showing that grounds may exist for a motion to dismiss the indictment because of matters occurring before the grand jury.}
    \end{itemize}
    \end{itemize}
  \end{itemize}
\end{itemize}
\footnote{18} \textit{Fed. R. Crim. P. 6(e) (emphasis added). See note 17 supra.}
\footnote{19} United States v. Parker, 469 F.2d 884 (10th Cir. 1972).
\footnote{21} \textit{Id.}
grand jury transcript under Federal Rule of Civil Procedure 34. Following a
grand jury investigation of possible criminal antitrust violations in which no
indictment was returned, the government brought a civil suit to enjoin the alleged
violations. The government made use of the grand jury transcripts from the
previous investigation to prepare for trial. The defendants moved for wholesale
discovery and production of the transcript under Rule 34. This motion was
granted by the district court but was subsequently reversed by the Supreme
Court. The Court held that "it is only where the criminal procedure is sub-
verted that 'good cause' for wholesale discovery and production of a grand jury
transcript would be warranted."

The Supreme Court recognized that strong public policies weighed against
disclosure of grand jury testimony and recited the five traditional justifications
for secrecy. The Court emphasized that the secrecy of the grand jury was
particularly important in furthering the policy of encouraging all witnesses to
step forward and testify freely without fear of retaliation. Thus, the Court con-
cluded that the "'indispensable secrecy of grand jury proceedings' must not be
broken except where there is a compelling necessity. There are instances when
that need will outweigh the countervailing policy. But they must be shown with
particularity." Notwithstanding a showing of "particularized need," the
secrecy of the proceedings is to be lifted only "discretely and limitedly." Ac-
cordingly, the court found the defendants' request for wholesale disclosure par-
ticularly inappropriate.

In *Pittsburgh Plate Glass Co. v. United States*, the Supreme Court affirmed
that the "particularized need" standard was to guide the exercise of judicial
discretion under Rule 6(e). A key government witness admitted on cross-ex-
amination that he had testified regarding the same general subject before the
grand jury which had indicted the defendant. Counsel for the defendant
moved for production of the grand jury minutes of the witness' testimony regard-

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22 *Fed. R. Civ. P. 34*, at the time of *Procter & Gamble*, provided in part:
Upon motion of any part showing good cause therefor and upon notice to all the
parties, and subject to the provisions of Rule 30(b), the court in which an action is
pending may (1) order any party to produce and permit the inspection and copying
or photographing, by or on behalf of the moving party of any designated documents,
not privileged, which constitute or contain evidence relating to any of the
matters within the scope of the examination permitted by Rule 26(b) and which are
in his possession, custody or control.

In 1970 the rule was amended to eliminate the "good cause" requirement.

23 356 U.S. at 678.

24 In order to expedite review of this ruling, the order requiring production, on the
motion of the government, included a provision whereby the complaint would be dismissed if
the government failed to comply. The government persisted in its refusal to produce the
transcripts and the complaint was dismissed. The government appealed to the Supreme Court.

25 356 U.S. at 684.

26 *Id.* at 682.

27 *Id.* at 682 (footnote omitted).

28 *Id.* at 683. The Court said that when the transcript was to be used at trial to impeach
a witness, to refresh his recollection, or to test his credibility, particularized need would be
shown. The defendants, in this instance, contemplated the use of the transcript only as an aid
in their general preparation for trial.

29 *Id.*


31 Although the witness' testimony was important, the Supreme Court noted that the
proof was overwhelming aside from his testimony. *Id.* at 398.
The Supreme Court rejected the defendant’s claim that there existed an absolute right to production. The court said that the decision to disclose was committed to the sound discretion of the trial judge. Since the defendant had not attempted to show “particularized need,” and had not even attempted to invoke the discretion of the trial judge, the denial of the motion did not constitute an abuse of discretion.\(^2\)

The “particularized need” standard attained some measure of practical significance in *Dennis v. United States*.\(^3\) The Court, for the first time, was forced to deal with the implications of the “particularized need” standard developed in *Procter & Gamble* and *Pittsburgh Plate Glass* in the context of a limited request for disclosure.

*Dennis* clearly suggests that the “particularized need” standard is to be infused with the “realization that disclosure, rather than suppression, of relevant materials ordinarily promotes the proper administration of criminal justice.”\(^3^4\) This statement suggests that the “particularized need” standard is to be given a pragmatic construction in that the requisite level of “particularized need” is to be balanced against the strength of the reasons for maintaining secrecy.

The criminal defendants in *Dennis* made a substantial showing of “particularized need.”\(^3^5\) Various factors contributed to this finding of “particularized need”: some of the grand jury testimony was as much as fifteen years old at the time of the trial, the testimony sought was that of key prosecution witnesses, the testimony concerned conversations and was largely uncorroborated, the witnesses had reason for hostility toward the defendants, and one witness had earlier admitted to being mistaken as to important dates.\(^3^6\) These factors were all relevant to the impeachment of the witnesses. Such a showing of “particularized need” must be balanced against the need for maintaining secrecy. Since the government conceded that the importance of preserving the secrecy of the grand jury minutes was minimal, the balance was clearly tipped in favor of disclosure.

The implication of *Dennis* is that the exercise of discretion should involve a realistic assessment of the competing policy considerations. The application of the balancing test is to be undertaken with the realization that disclosure of relevant materials promotes the proper administration of justice.

2. Seventh Circuit

In *Illinois v. Sarbaugh*,\(^3^7\) the Seventh Circuit recently dealt with the standard for disclosure of grand jury transcripts. In *Sarbaugh*, the state of Illinois brought a civil antitrust action against a number of corporations. Some

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\(^2\) The result may have been different had the defendant appealed to the discretion of the trial judge since the Court in *Procter & Gamble* had mentioned that the use of a grand jury transcript to impeach a trial witness would constitute “particularized need.” 356 U.S. at 683.

\(^3\) 384 U.S. 835 (1966).

\(^4\) Id. at 870.

\(^5\) Id. at 872.

\(^6\) Id. at 872-73.

\(^7\) 552 F.2d 768 (7th Cir.), cert. denied, 334 U.S. 884 (1977).
of the defendant corporations had obtained transcripts of their employees' grand jury testimony during a criminal antitrust proceeding which had since been terminated. The state attempted to obtain those transcripts from John Sarbaugh, Chief of the Antitrust Division of the Justice Department's Midwest Office. This office had been involved in the earlier criminal proceeding.

The district court found that the required showing of "particularized need" was not made. On appeal, the Seventh Circuit reversed and emphasized that the application of the "particularized need" standard involved a pragmatic balancing approach between competing interests. A party seeking disclosure must establish a need for such disclosure commensurate with the need for secrecy remaining. "The level of need has been said to diminish as the reason for preserving secrecy becomes less compelling."38

The Seventh Circuit found that a "particularized need" had been shown due to (1) the litigant's interest in securing accurate and truthful testimony from witnesses, for impeachment purposes or to refresh the recollection of witnesses, (2) the unfairness in permitting one side to have exclusive access to a storehouse of relevant facts, and (3) the lapse of time.39 The Seventh Circuit adhered to the Supreme Court's language in Procter & Gamble which required that even with a showing of "particularized need," the secrecy of the proceedings is to be lifted "discretely and limitedly."40 Thus, the Seventh Circuit granted disclosure, but imposed some rather severe restrictions on the use of the transcript.41

The Seventh Circuit's approach in Sarbaugh was clearly pragmatic. The court made a thorough assessment of the reasons for protecting secrecy. The court made clear that secrecy would be maintained only when the reasons for preserving secrecy prevailed over those mandating disclosure. The court also evinced a willingness to disclose the requested grand jury transcripts when restrictions could obviate any possible threats to policy reasons underlying the secrecy of the grand jury.

Sarbaugh and the previously discussed Supreme Court cases dealt with the situation in which a party sought the transcript of a witness' grand jury testimony. In this context, the protection of the grand jury witness himself is the prime reason for maintaining secrecy.42 In Clavey, however, the Seventh Circuit dealt with a grand jury witness' request for a copy of his own testimony. Since the historical justifications for secrecy bear differently on this factual circumstance, it is necessary to scrutinize closely the need to maintain secrecy. Then, to determine whether secrecy prevails over disclosure, the justification for keeping information secret must be balanced against the "particularized need" of the witness in securing a copy of his own testimony.

38 Id. at 774.
39 Id. at 775-76.
40 356 U.S. at 683.
41 The Court required that the attorney file a log with the court showing to whom and when each transcript was shown, that no copies were to be made, and that the transcript was to be returned when it was no longer needed. The attorney was limited in his use of the transcript to the litigation in process and only for the purposes of impeachment, refreshing the witness' recollection and testing credibility. 552 F.2d at 777.
42 356 U.S. at 682.
B. A Grand Jury Witness' Request for a Copy of His Own Testimony

Little attention has been paid to the problems surrounding a witness' attempt to secure a copy of his own grand jury testimony. The case authority is limited and the Supreme Court has not had occasion to analyze a witness' request for such disclosure.

Since no specific statutory provision deals with this situation, presumably the general disclosure principle of Rule 6(e) applies. Rule 6(e) imposes no bond of secrecy on a grand jury witness. The witness is free to disclose all that transpired while he was present.

The existence of this freedom raises serious doubts whether there should be restrictions on a witness' access to a transcript of his testimony. Arguably, the values protected by the policy reasons in favor of secrecy are no more threatened by the release to a witness of a copy of his testimony than by permitting a witness to publish the contents of his testimony as sanctioned by Rule 6(e).

Indeed, in In re Russo the United States District Court for the Central District of California commented that it could "conceive of no reason why furnishing a witness a written transcript of his testimony should interfere with the valid functions of the grand jury any more than does the existing practice. The provision of a transcript does not weigh differently on the justifications for secrecy than the present rule." This statement suggests that, at a minimum, the requirement of "particularized need" and a strong presumption in favor of secrecy should not be extended blindly to a grand jury witness' request for a copy of his own testimony.

Courts that have considered the issue of disclosure pursuant to a grand jury witness' request for a transcript of his testimony have split regarding the approach to be taken. Some courts have adopted the "particularized need" standard. Other courts have found that the disclosure should be made in the absence of a compelling government interest for maintaining secrecy. Under either approach, however, the courts will, in the typical situation, be faced with a balancing test to determine which interest prevails.

1. The Use of the "Particularized Need" Standard

Several decisions have extended the "particularized need" standard, which

43 See, e.g., Comment, Grand Jury Secrecy, supra note 1, at 810.
44 See note 17 supra.
45 The Original Advisory Committee Notes to Rule 6(e) stated that a seal of secrecy was an unnecessary hardship to impose on the witness. Secrecy might lead to injustice if a witness was not permitted to make a disclosure to counsel or to an associate. The view that the witness has the freedom to disclose is consonant with the view expressed by one eminent commentator that:

The privilege, therefore, is not the grand juror's, for he is merely an indifferent mouthpiece of the disclosure. Nor is it entirely the state's, for the state's interest is merely the motive for constituting the privilege. The theory of the privilege is that the witness is guaranteed against compulsory disclosure; the privilege must therefore be that of the witness and rests upon his consent.

46 See text accompanying note 16 supra.
48 Id. at 576.
was formulated in the context of a party's request for the disclosure of the grand jury testimony of a witness, to a witness' request for a copy of his own grand jury testimony. In *Bast v. United States*, the Fourth Circuit endorsed a stringent application of the "particularized need" approach.

Bast, a grand jury witness who had brought a civil suit against the United States, applied for a transcript of his testimony before the grand jury. The grand jury had been dismissed without returning an indictment. The district court entered an order denying the request on the ground that Bast had not shown the requisite "particularized need." The Fourth Circuit stated that the standard for review of a district judge's order respecting the release of proceedings before a grand jury is that of abuse of discretion, and that in this instance abuse had not been shown.

The Fourth Circuit reasoned that although Rule 6(e) imposes no condition of secrecy on the witness, it does not lift the general veil of secrecy which covers the grand jury. The court felt that the established practice of shielding grand jury proceedings justified the requirement that "particularized need" be shown.

The United States District Court for the Southern District of Florida, in *In re Grand Jury Witness Subpoenas*, also applied the "particularized need" standard to the requests of four witnesses for a transcript of their grand jury testimony. The Florida District Court stated that the decision to disclose such testimony rests on a determination whether the policies for maintaining secrecy will be undermined by disclosure. The court expressed its concern that a witness with an absolute right to disclosure might exercise poor judgment in seeking a transcript. Witnesses need to be protected, the court reasoned, since a witness who had obtained a transcript might succumb to the intimidation of a person who was the target of the investigation and be compelled to furnish a copy of his testimony.

The court found it significant that the person under investigation in *In re Grand Jury Witness Subpoenas* "was not brought to trial on an indictment in a previous case because of the disappearance of the government's main witness."
The inference was that the witnesses seeking disclosure, therefore, had testified against a person not at all averse to seeking retaliation against such witnesses. Thus, the threat to these witnesses was substantial. The court also found it significant that any potential subornation of perjury would be facilitated by the assistance of a transcript since it would be easier for a potential defendant to piece together a contrived defense in a complicated case if he had access to a transcript.\textsuperscript{56} Otherwise, much of the effectiveness of the perjured statements would depend on the witnesses' ability to accurately recall their testimony. The concern that disclosure would pose a threat to an innocent target of the ongoing investigation was also expressed.\textsuperscript{57}

The court did not find a "particularized need" on account of the witnesses' fear that an inadvertent misstatement might subject them to a possible perjury prosecution.\textsuperscript{58} This threat was no different with regard to these witnesses than it would be for any other witness testifying before the grand jury.\textsuperscript{59}

2. The Liberal Approach to Access

Some courts have disdained the use of the "particularized need" test in determining whether a witness is entitled to a transcript of his own grand jury testimony. In re Russo,\textsuperscript{60} a decision of the United States District Court for the Central District of California, is the leading case endorsing disclosure without requiring a showing of "particularized need." The court found that "[a]n examination of the justifications for the policy of grand jury secrecy demonstrates that requiring secrecy of witnesses would serve no useful purpose."\textsuperscript{61} The court saw no threatened loss of grand jury effectiveness by giving the witness a written copy of what he was already free to disclose. The court noted that Procter & Gamble, in which the Supreme Court formulated the "particularized need" standard, placed particular reliance on the need to encourage witnesses to step forward and testify freely without fear of retaliation. The court stated that to provide a witness with a transcript of his own testimony would not be inconsistent with this policy.\textsuperscript{62}

In addition, the Russo court determined that to provide a transcript would further the interests of justice and benefit the grand jury and the witness. A written transcript would insure that the witness' attorney was provided an accurate record of the proceedings. The existence of a written transcript would also minimize the possibility of the witness publicizing false information regarding the proceeding. A review of the written transcript would give the witness an opportunity to correct errors in the transcript or inadvertent mistakes in the testimony itself.\textsuperscript{63}

\textsuperscript{56} 370 F.Supp. at 1286.  
\textsuperscript{57} Id.  
\textsuperscript{58} The witnesses had been granted "use" immunity but had expressed concern that they were still exposed to possible perjury charges. Id. at 1285.  
\textsuperscript{59} Id. at 1286.  
\textsuperscript{60} 53 F.R.D. 564 (C.D. Calif. 1971).  
\textsuperscript{61} Id. at 571.  
\textsuperscript{62} See In re Minkoff, 349 F.Supp. 154, 157 (D.R.I. 1972), which suggests that the assurance that a witness would have a copy of his statement might function as a catalyst to his testimony.  
\textsuperscript{63} 53 F.R.D. at 571.
The court was not concerned about the witness' inability to protect himself. It noted that providing a witness a transcript does not force him to divulge the contents of his testimony. The witness would be free to keep the transcript confidential or to reveal it.\textsuperscript{64} The Russo court concluded that "furnishing a grand jury witness a transcript of his testimony shortly after his appearance is not inconsistent with valid reasons for grand jury secrecy and will not diminish the effectiveness of the grand jury system or interfere with governmental efforts to investigate crime."\textsuperscript{65} Thus, according to Russo, the witness should only have to show that his testimony was recorded and that a transcript could be made.\textsuperscript{66}

In \textit{In re Craven},\textsuperscript{67} the Northern District of California followed the Russo approach.\textsuperscript{68} In addition, the court argued that a protective order would be available to ensure that no prejudice to the government or to third parties would be done. If the court ordered that the transcript could be seen only by the witness and his attorney during the life of the grand jury, the possibility that third parties would be able to "piece together" references to them in the transcript and either change their testimony or flee the jurisdiction would be obviated.\textsuperscript{69}

\textbf{C. The Rationale of Clavey}

1. Majority

In Clavey, the Seventh Circuit was faced with the claim that a grand jury witness was deprived the effective assistance of counsel during the grand jury proceedings which led to his indictment.\textsuperscript{70} This deprivation allegedly resulted from the district court judge's denial of Clavey's request for a copy of his grand jury testimony. Clavey argued that the denial of access to his transcript deprived him of his statutory defense of recantation.

In reviewing the propriety of this ruling, the court determined that it was proper to apply the "particularized need" standard to a grand jury witness' request for a transcript of his own testimony. The court agreed with the district court judge's ruling that Clavey had not satisfied this requirement. The court, in making this determination, found it significant that Clavey's petition for disclosure was not verified. The Seventh Circuit believed the district court judge was "appropriately skeptical" of Clavey's claim that as a result of his physical ailments he was unable to recall the substance or detail of his testimony.\textsuperscript{71} The

\textsuperscript{64} Id. at 572.
\textsuperscript{65} Id.
\textsuperscript{66} Id. at 572-73.
\textsuperscript{67} 13 CRIM. L. REP. (BNA) 2100 (N.D. Calif. 1973).
\textsuperscript{68} The \textit{Craven} court argued that the privilege of secrecy is the witness' and concluded that when the witness voluntarily waived his right, disclosure should be made. This is consistent with the view espoused by Wigmore. See note 45 supra.
\textsuperscript{69} Id. There is dictum in Bursey v. United States, 466 F.2d 1059 (9th Cir. 1972), which supports the Russo-Craven position. The grand jury witness had been subjected to repetitious questioning. In order to protect the witness from substantial risks of perjury for inconsistencies, the court stated that the witness should be able to get a copy of his testimony unless there are demonstrated some particularized and substantial reasons why it should not be allowed. The precedential value of Bursey is limited, however, since it was abusive tactics, rather than an inherent right, which led to disclosure.
\textsuperscript{70} 565 F.2d at 113.
\textsuperscript{71} 565 F.2d at 114.
court recited the traditional justifications for secrecy and found that they should not be discounted because a witness asserted an unverified need for a transcript. Because Clavey failed "to verify with particularity a compelling necessity for a transcript of his prior testimony, [the Seventh Circuit did] not believe the district court denied him the effective assistance of counsel by refusing to release a transcript to him."

2. Dissent

The lone dissenting judge vehemently contested both the majority's use of the "particularized need" standard and the majority's conclusion that Clavey had not shown "particularized need." He argued that a witness should have a prima facie right to his own testimony unless the government could show overriding reasons for nondisclosure. He correctly noted that the "particularized need" standard was formulated to deal with a request for a copy of the grand jury testimony of another witness. "To avoid blindly extending the 'particularized need' standard and preserving secrecy for secrecy's sake, [it is necessary to] carefully consider whether that standard should be applied in this context." He concurred with the approach in Russo in arguing that any danger to the function of the grand jury arises from the witness' freedom to disclose and not in allowing him to disclose an accurate account of the proceedings.

The dissent also addressed the argument that the witness needs to be protected from his own poor judgment. The witness might succumb to the intimidation of the person who was the target of the investigation and be persuaded to furnish a copy of his testimony. The dissent opined that a witness' need for protection could best be evaluated by the one who knew his interests best, namely, the witness himself.

The dissent concurred with Mr. Justice Brennan's rationale that "[g]rand jury secrecy is, of course, not an end in itself. Grand jury secrecy is maintained to serve particular ends. But when secrecy will not serve those ends . . . secrecy may and should be lifted." The dissent believed that since none of the policies in favor of grand jury secrecy are served when a witness seeks a copy of his own testimony, the witness should have access to a transcript as a matter of right.

The dissenting judge also disagreed with the majority's conclusion that Clavey had not made a showing of "particularized need." He pointed to a number of factors which he felt established a "particularized need." Clavey had alleged that he could not recall the substance of his testimony because of an illness and a skull fracture that allegedly had an adverse effect on his memory. Clavey claimed that due to memory lapses he needed a transcript so that he could seek legal advice as to whether to exercise his right to recant. The majority had

72 Id. at 114-15 n.2.
73 Id. at 114.
74 Id. at 115.
75 Id. at 120 (dissenting opinion).
76 Id.
77 Id. at 121 n.4.
78 360 U.S. at 403 (dissenting opinion).
79 See note 7 supra.
argued that the lack of a verified petition and of a verification of Clavey's ailments (such as doctors' reports) militated against a finding in favor of disclosure. Yet, the dissent did not recognize these failures as having a debilitating effect on Clavey's claim. There is no reason to believe that Clavey's attorney's request for a transcript was based on an outright fabrication. The allegation, albeit unverified, did constitute at least some showing of "particularized need."

The dissent also argued that the recent enactment of the recantation statute strengthened Clavey's case of "particularized need." The purpose of the statute—to induce witnesses to give truthful testimony by permitting them to correct false statements without incurring the risk of prosecution—would be served by allowing disclosure. This policy strengthens the showing of need but it does not particularize it since every witness testifying before the grand jury would be similarly situated.

D. Critique

The majority and the dissent in Clavey disagreed on the proper method of handling a grand jury witness' request for a copy of his own transcript. The majority opted to allow disclosure to be dealt with in the discretion of the court. The dissent argued that, in this context, there should be a prima facie right to disclosure.

Due to the absence of any statutory provision affording a grand jury witness disclosure as a matter of right, the general disclosure provision of Rule 6(e) must be utilized. The Rule indicates that disclosure, otherwise prohibited, may be made when so directed by the court. Thus, under existing law, the majority's position adopting a discretionary standard finds support. On the other hand, those cases adopting the more liberal approach, which advocates disclosure when the reasons for maintaining secrecy do not apply, are clearly consonant with the Supreme Court's approach in Dennis.

If the balancing test in Sarbaugh is to have any efficacy, there must be close scrutiny of the competing considerations. Clearly, a frustration of the values to be served by the test exists if the general assertion that secrecy is necessary to protect the grand jury "is used as a talisman to ward off further inquiry whether [the secrecy] serves a legitimate function." The majority in Clavey appears to have adopted just such an approach. The majority indicated that it exercised a strong presumption in favor of maintaining secrecy. Yet, the Clavey court never specifically addressed the question whether the historical justifications for secrecy are applicable in the context of a grand jury witness' request for a copy of his own testimony. Both the Clavey holding and the majority's failure to make a thorough analysis of the competing considerations serve to frustrate any effectuation of the principle recognized in Dennis that disclosure, rather than suppression, of relevant material ordinarily promotes the administration of justice.

80 565 F.2d at 133 (dissenting opinion).
81 See note 17 supra.
82 565 F.2d at 122 (dissenting opinion).
The inadequacies of the approach in the majority are apparent. A thorough analysis of the policy justifications for maintaining the secrecy of grand jury proceedings leads to the conclusion that such justifications are without force in this particular fact situation.

The courts have recognized that since a grand jury witness is already free to disclose his testimony, providing him with a transcript does not present any greater danger to the values protected by the secrecy of the grand jury proceedings. Yet, two policy considerations are often relied upon by the courts in denying a witness' request for disclosure of a copy of his grand jury testimony. These two considerations, the danger of intimidation and harassment of the witness and the danger of subornation of perjury, were both emphasized in In re Grand Jury Witness Subpoenas. The existence of such valid concerns, however, does not justify the result in Clayey. The values underlying these policy considerations are not endangered in every factual setting, as the fact pattern in Clayey makes clear. Any threat to these values may be avoided if disclosure is made on a limited basis.

Clearly, the importance of maintaining secrecy pursuant to these considerations will vary significantly with the factual circumstances. It would be of particular importance to know who was the target of the grand jury investigation. If the witness himself was the sole target, then the traditional reasons for maintaining secrecy are clearly inapplicable. For in this situation there would be no threat of intimidation, no increased possibility of escape of the potential defendant, no threat to the innocent accused, and no additional assistance to the subornation of perjury since the witness would have access to the testimony on becoming a defendant.

The grand jury which indicted Clayey was primarily investigating his activities alone even though others were involved who might have been implicated by his testimony. Only to the extent that the existence of these other potential defendants presented threats of intimidation or subornation of perjury should disclosure be denied when such a potential defendant is seeking a copy of his grand jury testimony for recantation purposes.

Clayey was clearly not as vulnerable to intimidation as were the witnesses in In re Grand Jury Witness Subpoenas. If the witness is not in need of protection, that reason for denying disclosure clearly loses its force. The possibility of perjury arising from disclosure was also relatively trivial. Clayey was the key target of the grand jury investigation and he would undoubtedly be indicted along with any others. Even assuming that he would use the transcript of his testimony to aid the others in contriving a perjured defense, the only situation in which this option would not be available at some point in the proceedings would be if

83 370 F.Supp. at 1285, 1286. See text accompanying notes 55-57 supra.
84 Fed. R. Crim. P. 16(a)(1) (A) provides in part:
Upon request of a defendant the government shall permit the defendant to inspect and copy or photograph . . . recorded testimony of the defendant before a grand jury which related to the offense charged.
85 This is clear from an examination of the indictment which reveals the substance of Clayey's grand jury testimony. See Brief for Appellant at 6-7, United States v. Clayey, 565 F.2d 111 (7th Cir. 1977).
86 Those witnesses had testified against a man who, apparently, was not averse to retaliating against witnesses. See text accompanying note 55 supra.
Clavey did not become a defendant. This eventuality was not probable, and the district court judge, even at the stage of the grand jury proceeding at which the request for disclosure was made, could undoubtedly have discerned this.

These considerations, admittedly, would demand a thorough factual inquiry. Such a searching factual inquiry is necessary, however, to determine if and when there remain any justifications for maintaining the secrecy of the grand jury. In the Clavey factual situation, a thorough inquiry compels the conclusion that the justifications for secrecy are relatively trivial.

Although some circumstances exist in which it would be desirable to maintain the secrecy of grand jury proceedings when a witness is seeking a copy of his own testimony, in Clavey, the potential dangers do not appear so insuperable that they could not have been avoided by restrictions on the use of the transcript. This failure to discuss the possible use of a protective order in Clavey is particularly surprising in light of Sarbaugh. The Seventh Circuit in Sarbaugh exercised a cautious approach to disclosure of grand jury transcripts, as is evidenced by the severity of the court’s protective order.87

Curiously, in a situation in which there exists, at best, minimal justification for maintaining secrecy and when a protective order would have been particularly successful in avoiding the dangers of subornation of perjury and of intimidation of the witness, the court did not even mention the possibility of its use. Clavey even offered to receive the transcript under any restrictions that might be required to preserve the secrecy of the grand jury.89

The reasons for maintaining secrecy in Clavey are virtually nonexistent. Admittedly, however, the showing of “particularized need” was weak. Even with this limited showing, the denial of disclosure in Clavey seems to have been improper because by the imposition of restrictions on such disclosure, any improper use of the grand jury transcript could have been avoided.

Notwithstanding the foregoing analysis, the Seventh Circuit could only reverse the district court’s denial to release if the initial refusal were an abuse of discretion.90 Had the Seventh Circuit given careful scrutiny to the applicability of the reasons in favor of secrecy, a basis might have existed for finding an abuse of discretion. To maintain secrecy for secrecy’s sake is improper and if a restricted disclosure could uphold any reasons for maintaining secrecy, a denial of the request should be considered an abuse, even if the showing of “particularized need” was not substantial. In fact, the conclusion that the denial of the request for disclosure would constitute an abuse in factual circumstances like Clavey is strongly suggested by Sarbaugh. If the Seventh Circuit, in Clavey, had con-

88 See note 41 supra.
89 This offer was made in defense counsel’s letter of November 25, 1974, to the Assistant United States Attorney. Government’s Response to Petition for Rehearing and Suggestions in Support of Rehearing En Banc, at C-4, 5.
90 This is the standard that is generally applied. See text accompanying note 50 supra.
Clavey argued on appeal that he was denied the effective assistance of counsel and not that the district court judge had abused his discretion. This was apparently an attempt to induce the court to focus on Clavey’s “right” to his transcript. The majority, however, applied the familiar approach of Pittsburgh Plate Glass which used a “discretionary” standard. Use of the “particularized need” standard was proper, for as United States v. Mandujano, 425 U.S. 564, 581 (1976), indicates, the sixth amendment right to counsel does not apply in the grand jury context since no criminal proceedings have been instituted.
scientiously applied the balancing test of Sarbaugh and had shown the same amenability to use restrictions on disclosure, the conclusion that disclosure should have been granted would have been unavoidable. Any contrary result, such as the one reached by the district court judge, can only be characterized as an abuse of discretion. There is no justification for falling back on the presumption in favor of secrecy. A proper application of the balancing test requires a rigorous inquiry into the justifications remaining for that secrecy.

Clavey leaves uncertain what approach the Seventh Circuit will take in applying the “particularized need” standard. Sarbaugh indicated that the court would make a thorough inquiry into the competing considerations. Sarbaugh also recognized the usefulness of placing restrictions on disclosure in preserving the values protected by maintaining disclosure. Clavey appears to be a step back towards the inflexible, unreasonable position that grand jury secrecy is an end in itself. This result is clearly inconsistent with the Supreme Court’s pragmatic approach in Dennis, which emphasized that the balancing process was to be infused with the realization that disclosure, rather than suppression, promotes justice.

IV. Private Judge-Jury Communications

Since the deliberation of the trial jury is more closely tied to the determination of guilt than is the grand jury proceeding, it is even more important to the proper administration of the criminal system and to the rights of the criminal defendant that the proper conduct of trial jury deliberations be vigorously protected. In Clavey, the Seventh Circuit had to deal with two errors by the trial judge that involved the trial jury’s deliberations. The trial judge had failed to respond adequately to the jury’s requests for additional instructions and had failed to notify either defendant or his defense counsel of these communications with the court. The court ruled, however, that these errors were harmless and that reversal was not required.

A. Early Recognition of the Impropriety Inherent in Private Judge-Jury Communications

In order to analyze the Seventh Circuit’s conclusion that the trial judge’s wrongful conduct regarding the trial jury’s deliberations was harmless, two early Supreme Court cases which were cited as authority in Clavey must be reviewed.

The United States Supreme Court has long recognized the error manifest in private judge-jury communications. In Fillippon v. Albion Vein Slate Company, the jury, during deliberation, asked the judge for assistance on the issue of contributory negligence. The court reinstructed in the absence of the parties or their counsel, without their consent, and without calling the jury into open court. The Supreme Court found this to be an obvious error. The

91 250 U.S. 76 (1919).
92 Id. at 80.
93 The Court stated:
We entertain no doubt that the orderly conduct of a trial by jury, essential to the proper protection of the right to be heard, entitles the parties who attend for the
Court rejected a simple reliance on the ameliorative effect of a later defense exception to the error to cure any possible prejudice.

It is not correct, however, to regard the opportunity of afterwards excepting to the instruction and to the manner of giving it as equivalent to an opportunity to be present during the proceedings. To so hold would be to overlook the primary and essential function of an exception, which is to direct the mind of the trial judge to the point in which it is supposed that he has erred in the law, so that he may reconsider it and change his ruling if convinced of error, and that injustice and mistrials may thus be obviated.\(^9\)

Thus, the Supreme Court clearly indicated that it would not readily excuse such an error. The Court found that such an error was "presumptively injurious" and that the error would require reversal unless "it affirmatively appears that [it was] harmless."\(^9\)

The rationale of *Fillippon* was reaffirmed in *Shields v. United States.*\(^9\) *Shields* established the right of a criminal defendant to be present when supplementary instructions are given to a deliberating jury. The jury, unable to agree as to the guilt or innocence of Shields and two of his codefendants, sent the judge notice to that effect. The judge, from his chambers, sent a written reply without the presence of or notice to Shields or his counsel. The note instructed the jury to find whether these three defendants were guilty or not guilty. Shortly after the communication, the jury returned a guilty verdict on one of the four counts along with a recommendation of mercy. The Supreme Court, in finding error, quoted *Fillippon* with approval and found that if it was true that the defendant had the right to notice and an opportunity to be heard in a civil suit, "a fortiori . . . [it was] true in a criminal case."\(^9\)

The purpose to be present in person or by counsel at all proceedings from the time the jury is impaneled until it is discharged after rendering the verdict. Where a jury has retired to consider its verdict, the supplementary instructions are required, either because asked for by the jury or for other reasons, they ought to be given either in the presence of counsel or after notice and an opportunity to be present; and written instructions ought not to be sent to the jury without notice to counsel and an opportunity to object. Under ordinary circumstances, and wherever practicable, the jury ought to be recalled to the court room, where counsel are entitled to anticipate, and bound to presume, in the absence of notice to the contrary, that all proceedings in the trial will be had. In this case the trial court erred in giving a supplementary instruction to the jury in the absence of the parties and without affording them an opportunity either to be present or to make timely objection to the instruction.

\(\text{Id. at 81.}\)

\(^9\) \(\text{Id. at 82.}\)

\(^9\) \(\text{Id. In finding that the presumption of reversible error was not overcome, the Court found that the supplementary instruction given was far from harmless. The instruction incorrectly stated Pennsylvania law on contributory negligence and was so worded as to mislead the jury.}\)

\(^9\) \(273\) U.S. \(583\) (1927).

\(^9\) \(\text{Id. at 588. The Court reversed without even considering the possibility of excusing this error. (The prejudice in this instance, however, was obvious.) It should be noted that because the Court reversed on the basis of *Fillippon*, it did not discuss the merits of defendant's claim that the communication violated his right to due process of law.}\)
B. Bases of the Defendant's Right to be Present During Judge-Jury Communications

Cases such as Fillippon and Shields established the right of the defendant to be present during judge-jury communications, the policy reasons for such a requirement, and a rather stringent standard to be met in excusing such violations. A number of sources exist in which the courts find support for this right.

In Lewis v. United States, the Supreme Court stated that "[a] leading principle that pervades the entire law of criminal procedure is that, after indictment . . . , nothing shall be done in the absence of the prisoner." Although Lewis may not support the conclusion that the right of the defendant to be present during judge-jury communications is of constitutional dimension, significant authority exists in support of that proposition.

1. Constitutional Bases

The cases which deal with the right of the defendant to be present during judge-jury communications as constitutionally based cite a variety of constitutional provisions. The due process clause of the fifth or fourteenth amendment is most often cited. As one commentator says, "[i]t is hard to believe that a right recognized even during the harsh common law administration of the criminal law, and never doubted since, is not part of the due process of law protected by the Fifth Amendment."  

Some courts consider the propriety of judge-jury communications in the defendant's absence in the context of the general right to trial by jury guaranteed by the sixth amendment. Other courts consider such private communications
to be a violation of the right to a public trial.\textsuperscript{104} When the defense counsel is also absent during the communications, some courts discuss the right in terms of the sixth amendment's guarantee of assistance of counsel.\textsuperscript{105} This is particularly important since defense counsel could play a prominent role in helping the trial judge frame a response to the jury's inquiry which would best facilitate the jury's consideration of the issue involved.\textsuperscript{106}

2. Statutory Base

The most commonly cited source guaranteeing the defendant's right to be present is Federal Rule of Criminal Procedure 43(a).\textsuperscript{107} In Rogers \textit{v. United States},\textsuperscript{108} the Supreme Court addressed a situation in which the jury sent a note to the trial judge inquiring whether the court would accept a guilty verdict with a recommendation of extreme mercy. The court, without notifying the defendant or his counsel, instructed the marshal to deliver a note advising the jury that the court would accept such a verdict. The Supreme Court concluded that "cases interpreting the Rule make it clear, . . . that the jury's message should have been answered in open court and that petitioner's counsel should have been given an opportunity to be heard before the trial judge responded."\textsuperscript{109} The error involved went beyond the absence of the defendant and counsel from the courtroom during the communications with the jury in that counsel is also to be given an opportunity to be heard before the trial judge responds. It is generally recognized that there is great value in allowing the parties an input into the judge's thinking so that the resulting communication will be the best possible.\textsuperscript{110}

\begin{footnotes}
\item[104] See note 110 and accompanying text infra. The right to be present is essential to ensure the proper protection of the defendant's rights. See note 93 supra. Therefore, it is imperative that the defendant have the assistance of counsel. "It is essential to that principle that . . . the accused is guaranteed that he need not stand alone against the State at any stage of the prosecution, formal or informal, where counsel's absence might derogate the accused's right to a fair trial." United States \textit{v. Wade}, 388 U.S. 218, 226 (1967).
\item[105] Federal Rule of Criminal Procedure 43(a) provides:

\begin{quote}
The defendant shall be present at the arraignment, at the time of the plea, at every stage of the trial including the impaneling of the jury and the return of the verdict, and at the imposition of sentence, except as otherwise provided by this rule.
\end{quote}

\item[107] Id. at 39.
\item[108] 422 U.S. 35 (1975).
\item[109] Id. at 39.
\item[110] Filippone \textit{v. Albion Vein Slate Co.}, 250 U.S. 76 (1919) (See text accompanying note 95 supra); United States \textit{v. Dellinger}, 472 F.2d 340, 379 (7th Cir.), \textit{cert. denied}, 410 U.S. 970 (1963); 526 P.2d at 106; Klesser \textit{v. Stone}, 201 S.E.2d 269 (W. Va. 1973). In Klesser, the Court commented:

\begin{quote}
Our system recognizes that neither litigants, lawyers, judges nor jurors are perfect and that each principal participant in the mechanics of trial must be openly and uninhibitedly receptive to receiving the assistance of others in insuring a fair trial. This is true throughout the conduct of the trial and perhaps with greater force in the cumulative jury deliberation. If there is a communication to be had between the jury and the judge or vice versa, and it appears there is even a possibility that one of the parties might be prejudiced, it is essential that the party litigants be aware of that communication in order that they have the opportunity not only to protect their direct rights, but to assist the court in achieving a fair determination of the issues and in maintaining the appropriate aura of dignity and fairness.
\end{quote}
\end{footnotes}
C. Effect of a Violation

1. Automatic Reversal

When private communications between the court and jury are made, appellate courts have uniformly assigned error. A difference of opinion exists, however, as to what effect such a violation should have on the proceedings. Limited authority exists for the view that such communications per se require reversal. In Arrington v. Robertson, the Third Circuit stated in a civil case that the action of the trial judge in . . . sending instructions to the jury from his chambers in the absence of the defendant or his counsel and without giving them notice and an opportunity to be present amounted to a denial of due process of law. We hold that it was a denial of a right so fundamental as necessarily to affect the substantial rights of the defendant regardless of the nature or propriety of the instructions given.

In Evans v. United States, supplemental instructions were given in open court with defense counsel present but with the defendant inadvertently absent. The judge immediately recalled the jury and the court reporter reread the instructions in the presence of the defendant. Defense counsel made it clear that he was satisfied with this handling of the matter. There was no claim that the instructions given were in any way erroneous. Despite the fact that there was little chance of prejudice, the Sixth Circuit found that the error required reversal.

2. Harmless Error

Generally, the rule requiring reversal is recognized as much too strict. The fear exists that a per se rule would require the sacrifice of considerable time and effort. It has been held that the substantial rights of the criminal defendant can be protected through rigid judicial scrutiny of the error. When it can be determined that the error has only a relatively minor impact on the proceedings

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111 See, e.g., 422 U.S. 35; 273 U.S. 583; 250 U.S. 76; 3 C. WRIGHT, supra note 6, at 202.
112 114 F.2d 821 (3rd Cir. 1940).
113 Id. at 823.
114 284 F.2d 393 (6th Cir. 1960).
115 Evans was followed in Neal v. United States, 320 F.2d 533 (3rd Cir. 1963). In Neal, the court, in reversing a narcotics conviction, identified the critical fact as being the defendant's absence when the jury's inquiry was received and when it was answered by the trial judge. The court felt that consideration of the government's harmless error theory was not necessary to their disposition of the case.

Pennsylvania has adopted the rule, in both civil and criminal cases, that a communication of this nature requires reversal regardless of prejudice. Argiro v. Phillips Oil Co., 422 Pa. 433, 220 A.2d 654 (1966). The Supreme Court of Pennsylvania has recognized that such communications occur too frequently and has said that "the practice of trial judges in communicating with the jury or instructing the jury in any manner whatsoever, other than in the presence of counsel for all parties, must be terminated." Kersey Mfg. Co. v. Rozic, 422 Pa. 564, 569, 222 A.2d 713, 715 (1966). This strict approach was said to be the only safe course since the practice of determining the influence of any such communications is plagued by a lack of certainty. The practice of deciding such cases on an ad hoc basis through a determination of actual prejudice would surely lead to confusion and inconsistent results. Yarsunas v. Boros, 423 Pa. 364, 223 A.2d 696 (1966).
116 See 3 C. WRIGHT, supra note 6, at 204, and the cases cited therein.
it would be an insistence on form to reverse. Thus, most courts apply some variety of the “harmless error” rule in their consideration of the effect the violation of this right should have on the proceedings.117

If the defendant’s right to be present and to have an opportunity to be heard before response by the trial judge is deemed of constitutional dimension, a stringent form of the “harmless error” doctrine is to be applied. In Chapman v. California,118 the Supreme Court enunciated the standard by which federal constitutional errors were to be judged:

We conclude that there may be some constitutional errors which in the setting of a particular case are so unimportant and insignificant that they may, consistent with the Federal Constitution, be deemed harmless, not requiring the automatic reversal of the conviction.*** [W]e hold . . . that before a federal constitutional error can be held harmless, the court must be able to declare a belief that it was harmless beyond a reasonable doubt.119

The Chapman formulation of the “harmless error” standard has been applied by at least six circuits.120 This is true even in those cases which base the defendant's right on Rule 43. “It is true that as a general rule a violation of Rule 43 does not require reversal if the record affirmatively indicates beyond a reasonable doubt that the error did not affect the verdict.”121

A significant minority of courts apply a slightly less strict formulation of the “harmless error” standard. These courts sustain a conviction if the court can say with a reasonable certainty that no harm was done.122

Determining exactly which standard is being applied is often a difficult task.123 In fact, a thorough study of the cases leads to the conclusion that courts

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117 See cases cited in note 118 infra.
118 386 U.S. 18 (1967).
119 565 F.2d at 126 (dissenting opinion) (quoting 386 U.S. at 22, 24).
120 The “harmless beyond a reasonable doubt” and the “absence of a reasonable possibility of prejudice” formulations amount to virtually the same test. 386 U.S. at 24. Among the cases that indicate that either of these formulations is to be applied are: United States v. Nelson, 570 F.2d 258 (8th Cir. 1978); United States v. Benavides, 549 F.2d 392, 393 (5th Cir. 1977); United States v. Mesteth, 528 F.2d 333, 335 (8th Cir. 1976); United States v. Bach, 494 F.2d 424, 428 (10th Cir. 1974); United States v. Reynolds, 499 F.2d 4, 8 (6th Cir. 1973), cert. denied, 415 U.S. 988 (1974); United States v. Arriagada, 451 F.2d 487, 488 (4th Cir. 1971); 405 F.2d at 884; United States v. DiPietto, 396 F.2d 283, 287 (7th Cir. 1968); 405 F.2d at 244; 376 F.2d at 719; Estes v. United States, 335 F.2d 609, 618 (5th Cir. 1964), cert. denied, 379 U.S. 964 (1965); 322 F.2d at 436; Jones v. United States, 299 F.2d 661, 662 (10th Cir.), cert. denied, 371 U.S. 864 (1962).
121 405 F.2d at 244 (emphasis added).
123 This uncertainty is evidenced by the court’s treatment of Walker v. United States, 322 F.2d 434 (D.C. Cir. 1963), cert. denied, 375 U.S. 976 (1964); Walker is variously cited as standing for either the “harmless beyond a reasonable doubt” standard, 405 F.2d at 244, or the “reasonable certainty that no harm was done” test, 522 F.2d at 1321. And there is language in Walker that would support either conclusion, at 435 in favor of the latter approach, and at 436 where the court ultimately opted for the former, saying that the conviction must be reversed “unless the record completely negatives any reasonable possibility of prejudice.”
The majority opinion in Clavey is also marked by a careless approach to the resolution of the issue. After relating the factual setting, the court admitted that the trial judge committed an obvious error. The Seventh Circuit agreed that the trial court judge should have advised counsel of the jury's inquiries and made an effort to respond to them. The court quoted Rogers with approval and thus made it clear that the court recognized the seriousness of the error. As the language in Rogers made plain, the concern over the absence of the defendant involved much more than the fear that he would not later be able to remedy any injury arising from the improprieties in the communications. The opportunity to be heard before such communications are made was also involved. The input of defense counsel is important in order to ensure that the trial judge's response to the jury is the one that is most calculated to facilitate the jury's consideration of the issues involved.

124 This confusion is apparent when one examines the impact several important factual variants have had on the formulation of the harmless error test. The presence of defense counsel during the improper communications would certainly seem to militate against reversal. Most of the cases in which counsel was present, however, have applied the more stringent standard (i.e., Chapman). 970 F.2d 253; United States v. Jorgenson, 451 F.2d 516 (10th Cir. 1971), cert. denied, 405 U.S. 922 (1972); 434 F.2d 480; 376 F.2d 717; 335 F.2d 609; 299 F.2d 661. Although it would seem that if counsel were present the court could more easily deem an error harmless without a derogation of the rights of the defendant, the courts have not taken this approach.

Another factor that is sometimes stated as controlling is the nature of the communication. In United States v. Dellinger, 472 F.2d at 378, the Seventh Circuit said that courts are more willing to reverse when the communication to the jury involved a substantive matter. If the communication is unequivocal (i.e., a mere refusal to reinstruct) the courts are more willing to find harmless error. 472 F.2d at 378. The position espoused in Dellinger is not supported by the cases. The distinction between substantive and nonsubstantive communications is of little import regarding the formulation of the harmless error rule that the courts will apply. This is illustrated by two cases from the Seventh Circuit. In United States v. DiPietro, 396 F.2d 283 (7th Cir. 1968), in which the judge simply told the jury to continue deliberations, the court used the "harmless beyond a reasonable doubt" standard. In United States v. Higgans, 507 F.2d 808, in which the judge denied the jury's request to see a transcript of the testimony, the court was satisfied with applying a less severe standard (the "reasonable certainty" test) before upholding a conviction.

The Supreme Court has done little to clarify matters. In Rogers, the Court noted that a violation of Rule 43 would have to be considered in conjunction with Rule 52(a). 422 U.S. at 40. Fed. R. Crim. P. 52(a) provides that "[a]ny error, defect, irregularity or variance which does not affect substantial rights shall be disregarded." The Court cited United States v. Schor, 418 F.2d 26, 30 (2d Cir. 1969), as supporting this approach. Unfortunately, Schor failed to determine if Chapman or a less severe standard ("fair assurance that the verdict was not affected") should be applied.

This confusion is exacerbated when one considers that some courts apply even another standard of harmless error. There is language in a few cases which indicates that the error will not be considered harmless unless the defendant makes a showing of prejudice. 507 F.2d at 813; United States v. Woodner, 317 F.2d 649 (2d Cir.), cert. denied, 375 U.S. 903 (1963). This position is in the distinct minority. Most of the cases adhere to the position in Rice v. United States, 356 F.2d 709 (8th Cir. 1966), which states that there is a presumption of prejudice which needs to be rebutted.

126 See notes 106 and 110 and accompanying text supra. Some authority exists which holds that the denial of this opportunity is not to be tolerated under any circumstances.

"Harmless error" analysis of an ex parte judge-jury communication neglects a significant reason underpinning the requirement that the judge afford the parties an opportunity to be present prior to the communication—the importance of allowing
The opportunity for input by defense counsel is particularly important when the jury, in a complex case, is experiencing difficulty with the instructions. The majority cited the Supreme Court's decision in *Bollenbach v. United States*\(^7\) regarding the trial judge's duty in this situation:

Discharge of the jury's responsibility . . . depends on discharge of the judge's responsibility to give the jury the required guidance by a lucid statement of the relevant legal criteria. When a jury makes explicit its difficulties a trial judge should clear them away with complete accuracy.\(^{128}\)

In *Clavey*, the Seventh Circuit stated that the "judge's perfunctory answers were clearly inadequate in this respect."\(^{129}\) The input of counsel might have remedied this deficiency.

The court admitted that the errors involved in the judge's behavior were clear and then proceeded to determine whether these errors were "harmless." The *Clavey* court found that due to the nature of the particular questions asked by the jury, the trial court's errors were harmless. The *Clavey* court centered its discussion on the jury's second and third questions to the judge. The third question was considered to be merely a particularization of the second. The court read the jury's inquiry as asking whether Clavey had to be found guilty on counts one and two if they found him guilty on the related counts three and five. Since Clavey was acquitted on counts one and two, the court determined that the jury resolved its uncertainty in the defendant's favor. The judge's error in privately communicating with the jury was considered to be harmless since the court felt that the judge's answer to the jury's questions could not have produced a result more favorable to Clavey.

**E. Critique**

The majority followed the usual approach in analyzing the problem of judge-jury communications in the absence of the defendant or his counsel. First, the error in failing to give Clavey or his counsel an opportunity to be heard and in communicating with the jury in the absence of the defendant was readily admitted. Then the court, as is typical, proceeded to apply a "harmless error" standard. The majority's analysis in applying this test, however, is somewhat less than straightforward and merits further examination.

The *Clavey* court failed to articulate clearly which construction of the harmless error rule it applied. United States *v. Dellinger*\(^{130}\) and *Ware v. United States*\(^{131}\) were both cited without a recognition that they ostensibly set forth different approaches. *Ware* applied the strict *Chapman* formulation of the
“harmless error” standard.\textsuperscript{132} Dellinger, however, articulated the position that it would excuse such an error “where it appear[ed] with certainty that no harm was done.”\textsuperscript{133} A closer scrutiny of Dellinger, however, indicates that as a practical matter its approach is nearly as strict as the test in Ware. Yet, the Seventh Circuit, in Clavey, failed to acknowledge this fact.

Dellinger emphasized that reversible error may arise because counsel was not afforded the opportunity to make suggestions which might well have been of assistance to the judge in framing his response to the jury. The possibility that defense counsel might have been of some assistance to the judge militated against the conclusion that, with reasonable certainty, the communications were harmless. If this factor is taken into consideration, less certainty of the harmlessness of the error will exist. This adds a great deal of stringency to the “reasonable certainty” standard and, at least in Dellinger, makes that standard more akin to that articulated in Ware. Thus, the court’s citation of Ware and Dellinger, without any attempt at reconciliation whatsoever, leaves significant doubts as to which standard was actually applied.

The dissent provides some assistance in the resolution of this issue. The dissent argued that the Chapman-Ware formulation should be applied in this context.\textsuperscript{134} The implication is that it was not in this instance. A standard less stringent than the “harmless beyond a reasonable doubt” standard may have been applied, but the majority leaves little guidance as to the precise nature of its formulation.

The lack of clarity with which the “harmless error” test is defined by the court precipitates a great deal of confusion. The court’s discussion of the harmlessness of the error is equally troublesome. There is little discussion of the effect that defense counsel’s intervention might have had given an opportunity to be heard prior to the communications. Yet, a different response, prompted by counsel’s input, might have produced a different result. The possibility of a different outcome certainly weakens the persuasiveness of the conclusion that the error was harmless.

The possible coerciveness of the trial judge’s curt responses to the jury was not addressed by the Seventh Circuit. His abrupt responses to the jury’s undoubtedly serious concern about the proper discharge of their function may have indicated a growing impatience with their inability to return a verdict. Indeed, the comments of one juror interviewed by the sentencing judge prompts a concern whether the jury’s resolution of their difficulties ought to be countenanced. The juror indicated that there was a strong urge to go home\textsuperscript{135} and was quoted as saying:

\begin{quote}
I signed it for the simple reason that about three or four of those ladies, they didn’t want to spend the weekend down here. . . . If he was found guilty on one he should have been found guilty on all of them and if he was innocent on one he should have been innocent on all of them.\textsuperscript{136}
\end{quote}

\textsuperscript{132} Id. at 719.
\textsuperscript{133} 472 F.2d at 378.
\textsuperscript{134} 565 F.2d at 126 (dissenting opinion).
\textsuperscript{135} Brief for Appellant at 41.
\textsuperscript{136} Id. at 43.
The possibility that the verdict may have been a compromise has been recognized as bearing on the issue of "harmless error" in this context, yet the Clavey court did not discuss this possibility.

Under either formulation of the "harmless error" rule the court's reasoning in finding the error harmless appears, at first glance, to be convincing. The court's conclusion that the judge's answer could not have produced a result more favorable to Clavey is one possible interpretation. This reasoning is based on the supposition that the jury had already made their determination as to the guilt of the defendant on the third count of the indictment. Yet, such an assumption is not clearly true and the propriety of indulging in such a presumption is therefore questionable. "The majority apparently rule[d] out the possibility of a complete acquittal had the judge taken the steps the majority says he should have taken."

Much of this analysis involves speculation on the possible assistance of defense counsel's input and the impact of the communications on the mental processes of the jurors. This speculation is, however, inherent in any assessment of the impact of a trial error on the jury's determination of guilt or innocence. Because such speculation exists, however, it is essential that there be some degree of clarity as to the standard the court is to apply in finding an error harmless. There must also be the realization that this speculation must necessarily weaken the certainty with which the court can adjudge an error harmless.

The dissent suggested that the Chapman standard should have been applied. Arguably, the application of this standard could have produced a different result. Convincing reasons exist for explicitly adopting the Chapman formulation of the "harmless error" doctrine in the context of improper judge-jury communications. The denial of the opportunity to be heard and to be present during judge-jury communications implicates serious constitutional rights. Such private judge-jury communications pose a serious threat to both the right to due process and the right of assistance of counsel. When a violation of a right of such dimension exists, the Chapman standard should be applied in order to afford maximum protection to that right. In addition, the frequency with which such improper judge-jury communications occur gives one cause for serious concern.

A more stringent standard of harmless error would help remedy this situation. These considerations compel the conclusion that the Chapman formulation of the "harmless error" standard should have been clearly articulated and then applied in Clavey. The violation of the defendant's rights from private judge-jury communications should be deemed harmless only when it is clearly shown that it is so unimportant and insignificant that it can be considered harmless beyond a reasonable doubt. In Clavey, the harmlessness of the error did not appear with such a degree of conviction.

137 472 F.2d at 380.
138 565 F.2d at 126 (dissenting opinion).
139 "When the errors here are so judged, it is clear that they were far from harmless." Id.
V. Conclusion

In *Clavey*, the Seventh Circuit was faced with two important issues. The court was presented with an attempted incursion into the secrecy of the grand jury and with an actual interference with the proper conduct of the trial jury's deliberations.

The *Clavey* result protected the secrecy of the grand jury, but it may have done so at the expense of the rights of Sheriff Clavey. The protection of the secrecy of the grand jury is sometimes based more upon a simple adherence to long-established tradition than upon a thoughtful assessment of the persuasiveness of the justifications for secrecy in the particular fact situation before the court. *Clavey* appears to be just such a situation.

Clavey asserted the claim that a grand jury witness has a right to receive a copy of his testimony. The Seventh Circuit rejected this argument and applied a discretionary standard which required a balancing of Clavey's "particularized need" for a transcript against the need for maintaining the secrecy of the grand jury proceedings. A proper application of this balancing test necessarily involves a thorough evaluation of the justifications for secrecy in the context of this witness' request for disclosure. The Seventh Circuit failed to adequately discharge this obligation.

The use of restrictions on disclosure of transcripts has been recognized by the Seventh Circuit as a means by which any potential dangers to the values protected by secrecy might be obviated. This practice is a logical means through which to effectuate the Supreme Court's recognition in *Dennis* that disclosure, rather than suppression, of relevant materials most often promotes the proper administration of criminal justice. The court, however, failed to investigate the possibility of restrictions on disclosure in this instance. The whole tenor of the majority, in fact, seems to evince a predisposition against disclosure which is clearly contrary to the rationale in *Dennis*.

The opinion of the majority on the grand jury issue is no longer mandatory authority in the Seventh Circuit. The opinion and the subsequent proceedings leave the state of the law in considerable confusion. The approach of the majority is at odds with the court's recent opinion in *Sarbaugh*. And the majority's rationale indicates a return to a more inflexible, and less thorough, approach to possible intrusions into the secrecy of the grand jury. This is unfortunate, for if the "protection" is not necessary to serve any of the values sought to be safeguarded by secrecy, the denial of a request for disclosure in this context can only accomplish an abridgement of the witness' rights.

The Seventh Circuit, through an application of a "harmless error" standard, excused a violation of the defendant's rights arising from the trial judge's wrongful conduct regarding the trial jury's deliberation. The court, however, carelessly failed to articulate the precise formulation of the "harmless error" rule that it applied.

141 See text accompanying note 90 supra.
142 See text accompanying note 34 supra.
143 See text accompanying note 14 supra.
The most disturbing aspect of the court's disposition of this issue was its willingness to find the error in the private judge-jury communications to be harmless. The error involved carries with it a presumption of prejudice. This presumption should only be rebutted after careful consideration. The determination whether this presumption has been rebutted must involve a consideration of both the error in the failure to answer the jury's message in open court and in not affording defense counsel an opportunity to be heard. This second factor must be dealt with openly if the defendant's rights are to be fully protected.

Rigid scrutiny of the error in improper judge-jury communications should be made through the use of the stricter Chapman approach to "harmless error." The right being protected, if not clearly of constitutional magnitude, at least has constitutional implications. The improper communications involve an interference with a very sensitive area—the deliberations of the trial jury. This interference involves a great potential for prejudice. When the application of the "harmless error" standard necessarily involves speculation into such imprecise areas as the effect on the jury of the communications and of the prejudice resulting from a denial of the opportunity to be heard, a violation must be closely scrutinized under a well-defined approach. An error should be excused only when it is so insignificant that the court can declare the belief that it is harmless beyond a reasonable doubt.

Richard S. Myers

Trinity Memorial Hospital of Cudahy, Inc. v. Associated Hospital Service*

I. Introduction

Administrative agencies have traditionally functioned as autonomous decision-making bodies. Although courts have been reluctant to interfere with the administrative process, in recent years there has been increasing concern over the excessive degree of power which agencies have exercised. As a check on that power, several commentators have called for a less restrictive policy for judicial review of administrative decisions, particularly where agency actions or regulations can be questioned on constitutional grounds.1 In Trinity Memorial Hospital of Cudahy, Inc. v. Associated Hospital Service,2 the United States Court of Appeals for the Seventh Circuit considered whether the federal district court had jurisdiction to review a decision of the Secretary of Health, Education and Welfare when constitutional objections were raised.

II. Statement of Facts

The Secretary of HEW (the Secretary) is primarily responsible for the administration of the Medicare program. In 1966, Trinity entered into an agreement with the Secretary to provide services, without charge, to patients eligible for treatment under the Medicare Act.³

In accordance with the provisions of the Medicare Act, Trinity nominated Blue Cross Association (Blue Cross) as its fiscal intermediary.⁴ As agent of the

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* 570 F.2d 660 (7th Cir. 1977).
2 570 F.2d 660 (7th Cir. 1977).
4 Reimbursement for Medicare services provided by a health care facility is usually effected through a fiscal intermediary, such as Blue Cross Association, Aetna Life and Casualty Co., Mutual of Omaha, and Travelers Insurance Co. The fiscal intermediary is nominated by a group of providers on behalf of their members. Although most providers nominate a private organization as fiscal intermediary, the law also permits nomination of a public agency, such as a state public health agency.
Secretary, the organization or agency selected as fiscal intermediary determines the amount of payments due a provider. Blue Cross delegated its duties as fiscal intermediary to Associated Hospital Service (the Plan). As the agent of Blue Cross, the Plan ultimately determined the Medicare reimbursable costs incurred by Trinity as a provider of services.

Trinity received interim reimbursements based on billings submitted to the Plan during the year. At the close of each fiscal year, Trinity submitted an annual cost report to the Plan to enable it to determine the actual amount of reimbursement due. Pursuant to existing regulations, Trinity employed the “combination method” of reimbursement accounting to prepare the cost reports for fiscal years ending September 30, 1968, September 30, 1969, and September 30, 1970. The combination method requires the provider to distinguish between the cost of “routine services” and the cost of “ancillary services” when preparing annual cost reports. After conducting year-end audits for fiscal years ending 1968 and 1969, the Plan reclassified certain costs as “routine” which Trinity had determined to be “ancillary,” and made the corresponding adjustments to the cost report. The Plan reduced current interim payments to reflect the changes, and informed Trinity that the revised classification scheme must be followed in future cost reports.

Trinity paid the amount of disputed reimbursement as determined by the Plan’s audit and subsequently engaged in negotiations with the Plan’s representatives to resolve the cost dispute. The Plan maintained that the disputed costs must be classified as “routine” and refused to accept amended cost reports as proposed by Trinity.

Trinity appealed to the Blue Cross Medicare Providers Appeals Committee (the Committee). During the proceedings, Trinity objected to the composition

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6 The Plan, as agent of the Secretary, periodically reimbursed Trinity in accordance with 42 U.S.C. § 1395(g) (1970), which provides that:
   The Secretary shall periodically determine the amount which should be paid . . . to each provider of services with respect to the services furnished by it, and the provider of services shall be paid, at such times or at times as the Secretary believes appropriate (but not less often than monthly) and prior to audit or settlement by the General Accounting Office, from the Federal Hospital Insurance Trust Fund, the amounts so determined, with necessary adjustments on account of previously made overpayment or overpayments; except that no such payments shall be made to any provider unless it has furnished such information as the Secretary may request in order to determine the amounts due such provider under this part for the period with respect to which amounts are being paid . . .
8 20 C.F.R. § 405.452 (1970), in pertinent part, provides:
   (a) Principle. Total allowable costs of a provider shall be apportioned between program beneficiaries and other patients so that the share borne by the program is based upon actual services received by program beneficiaries. To accomplish this apportionment the provider shall have the option of either of the two following methods:
      (1) Departmental method. The ratio of beneficiary charges to total patient charges for the services of each department is applied to the cost of the department.
      (2) Combination method. The cost of “routine services” for program beneficiaries is determined on the basis of average cost per diem of such services for all patients; to this is added the cost of ancillary services used by beneficiaries, determined by apportioning the total cost of ancillary services on the basis of the ratio of beneficiary charges for ancillary services to total patient charges for such services . . .
and procedure of the Committee as violating its right to due process.\(^9\) Notwithstanding Trinity's constitutional objection, the Committee affirmed the Plan's original determination and denied Trinity's claim.\(^{10}\)

Prior to 1972, neither the Medicare Act nor its accompanying regulations authorized a provider of services to appeal a fiscal intermediary's final cost determinations.\(^1\) Upon Trinity's request, however, the Secretary agreed to review the decision of the Plan and the Committee, but ultimately refused to set the decisions aside.\(^2\)

Trinity thereupon instituted an action in the United States District Court for the Eastern District of Wisconsin. In its complaint, Trinity renewed its due process objection to the Committee's composition and procedure and alleged that the Committee's action in denying reimbursement failed to conform to the described standards for adjudication by an administrative agency. Trinity requested that the Committee decision be vacated and that the Secretary be ordered to refund the reimbursable costs. In the alternative, Trinity requested that the case be remanded for a hearing before an impartial decision-maker.

Trinity predicated jurisdiction on § 10 of the Administrative Procedure Act (APA)\(^3\) and the federal question jurisdiction statute, 28 U.S.C. § 1331 (1970).\(^4\) The Secretary claimed that neither the APA nor § 1331 authorized the district court to hear Trinity's case. Accordingly, the Secretary moved to dismiss, for lack of jurisdiction over the subject matter.

The district court found that it had jurisdiction over Trinity's claim by virtue of the APA and proceeded to render a decision on the merits. The court concluded that the composition of the Appeals Committee and the participation by counsel for Blue Cross constituted a clear violation of due process. Accordingly, summary judgment was entered in Trinity's behalf.\(^5\)

On appeal to the Seventh Circuit, the Secretary claimed absolute discretion

\(^9\) 570 F.2d at 663. One of the principal grounds of objection was that the extensive participation of Blue Cross employees as members of the Committee resulted in there being no impartial decision maker. Other procedures of Blue Cross in the decisional process were also challenged.

\(^10\) Id.


\(^12\) 570 F.2d at 663.

\(^13\) Section 10 of the Administrative Procedure Act (APA) is embodied in 5 U.S.C. §§ 701-06 (1970). Specifically, § 702 provides, in pertinent part, that "a person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute, is entitled to judicial relief thereof . . . ." In addition, § 704, in relevant part, provides that "agency action made reviewable by statute and final agency action for which there is no other adequate remedy in a court are subject to judicial review . . . ."

\(^14\) 28 U.S.C. § 1331 (1970) provides, in relevant part, that "the district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $10,000 exclusive of interest and costs, and arises under the Constitution, laws, or treaties of the United States . . . ."

\(^15\) 570 F.2d at 663.
regarding pre-1973 determinations of Medicare reimbursable costs. He asserted that the district court had no jurisdiction, despite Trinity's due process challenge to the procedure by which the cost decision was reached.

The Seventh Circuit held that the Secretary's decision regarding Trinity's determination of Medicare reimbursable costs could not be reviewed. In addition, the court found that neither the APA nor § 1331 provided a basis for review of Trinity's due process objection. Despite these findings, the court disagreed with the Secretary's contention that Trinity's due process claim could not be reviewed. Conscious of the serious constitutional implications of totally precluding review of constitutional claims, the court merely dismissed the action, without prejudice, allowing Trinity to sue in the Court of Claims.

III. Jurisdiction

As previously noted, Trinity predicated jurisdiction for district court review of the Secretary's decision on two statutory provisions. First, Trinity argued that the Administrative Procedure Act provided for judicial review whenever a person suffered a legal wrong because of agency action or was aggrieved by agency action within the meaning of a relevant statute. Second, Trinity maintained that 28 U.S.C. § 1331 (1970) gave the district court federal question jurisdiction over its claim. The Seventh Circuit, however, rejected both of these provisions as a basis for review.

A. Administrative Procedure Act as an Independent Basis of Jurisdiction

In Sanders v. Weinberger, the Seventh Circuit had held that the APA provided an independent basis of subject matter jurisdiction to challenge agency action in the federal district courts. Relying on Sanders the district court in Trinity determined that it had jurisdiction over Trinity's claim by virtue of the APA. In the interim between the district court decision and the appeal to the Seventh Circuit, the United States Supreme Court reversed Sanders v. Weinberger, holding that the APA did not afford subject matter jurisdiction to review a decision of the Secretary of HEW. In accordance with this Supreme Court ruling, the Seventh Circuit, in Trinity, summarily rejected the district court's decision to base jurisdiction on the APA.

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16 Id. at 666.
17 Id. at 667.
18 Id. at 667-68.
19 522 F.2d 1167 (7th Cir. 1975).
20 570 F.2d at 663.

Having disposed of the APA as a basis of jurisdiction, the Seventh Circuit shifted its focus to the unanswered question of whether jurisdiction could be predicated on § 1331. The Secretary claimed that Trinity was statutorily precluded from obtaining review under § 1331 by virtue of 42 U.S.C. § 405(h) (1970), which provided that

[the findings and decisions of the Secretary after a hearing shall be binding upon all individuals who were parties to such a hearing. No findings of fact or decision of the Secretary shall be reviewed by any person, tribunal, or governmental agency except as herein provided. No action against the United States, the Secretary, or any officer or employee thereof shall be brought under section 41 [now section 1331] of Title 28 to recover on any claim arising under this subchapter.]

Section 405(h) originated as a preclusion of review provision of the Social Security Act, and was later incorporated by reference into the Medicare Act.

The Seventh Circuit construed the second sentence of § 405(h) to preclude all review, under § 1331 or otherwise, of the merits of the Secretary's decision regarding Trinity's cost accounting. The court stated that "[t]he second sentence of § 405(h) directly prohibits in a broad and sweeping manner all judicial review of such a decision involving promulgated regulations . . . ."

Significantly, the court gave literal effect to the second sentence of § 405(h) only with respect to the Secretary's application of the administrative regulation. Since the Secretary made no "finding of fact or decision" on Trinity's due process objection, the Seventh Circuit found that the preclusion-of-review language in the second sentence was inapplicable to the constitutional claim. The court thus found it unnecessary to decide whether § 405(h) made the Secretary's decision on constitutional claims absolutely final.

By failing to address the finality of the Secretary's decisions when constitutional objections are raised, the Seventh Circuit seemed to overlook authority which considered constitutional questions unsuited to resolution in administrative hearings. If constitutional questions cannot be resolved in administrative hearings, the Secretary might never have made a "finding of fact or a decision" on the due process claim. The Seventh Circuit, therefore, should not have refused to address the issue merely because the Secretary did not decide a constitutional question in this case. Rather, the court should have found the second sentence inapplicable to review of all constitutional matters because there may never be a "decision of the Secretary" in that regard.

25 570 F.2d at 666.
The Seventh Circuit's ultimate resolution of whether § 405(h) precluded review, under § 1331, of Trinity's due process objection rested primarily on the proper construction to be given the third sentence of § 405(h). The language of this sentence makes no distinction between review of a decision on the merits and review of a provider's constitutional claims. Likewise, the provision in the context of the entire Medicare Act and the legislative history of the Act reveal no explicit policy for judicial review of constitutional claims under § 1331.

In 1939, § 405(h) was enacted as a preclusion of review provision of the Social Security Act. At that time, Congress also amended the Social Security Act to include 42 U.S.C. § 405(g) (1970), which provided for judicial review of agency matters otherwise unreviewable under § 405(h). The original version of the Medicare Act incorporated § 405(h) as it appeared in the Social Security Act. Section 405(g), however, was incorporated merely to authorize review of an agency determination that an institution was not eligible to act as a provider. One Senate Report indicated that review of matters not specifically mentioned would be prohibited:

Hospitals, extended care facilities, and home health agencies would be entitled to a hearing and judicial review if they are dissatisfied with the Secretary's determination regarding their eligibility to participate in the program. It is intended that the remedies provided by these review procedures shall be exclusive.

According to the Senate report, therefore, provider reimbursements could not be reviewed under § 405(g).

In 1972, Congress enacted 42 U.S.C. § 1395oo(f) (1972) of the Medicare Act. This provision established the Provider Reimbursement Review Board for administrative review of a fiscal intermediary's final cost determination. The House Report accompanying this provision indicated that there could be no administrative appeal of the intermediary's decision prior to the enactment of § 1395oo:

Under present law there is no specific provision for an appeal by a provider of services of a fiscal intermediary's final reasonable cost determination. Although the HEW has developed administrative procedures to assist providers and intermediaries to reach mutually and satisfactory settlements of disputed reimbursement items, your committee believes that it is desirable to prescribe in law a specific procedure for settling disputed final determinations applying to the amount of program reimbursement. This procedure would not apply to questions of coverage or disputes involving individual beneficiary claims.

28 42 U.S.C. § 405(g) (1970) provides, in pertinent part:

Any individual, after any final decision of the Secretary made after a hearing to which he was a party irrespective of the amount in controversy, may obtain a review of such decision by a civil action commenced within sixty days after the mailing to him of notice of such decision or within such further time as the Secretary may allow.

Your committee bill, therefore, provides for the establishment of a Provider Reimbursement Review Board. . . .

In 1974, Congress further amended § 1395oo(f) to provide for district court review of any decision of the Provider Reimbursement Review Board and of any reversal, affirmance, or modification of the Board’s decision made by the Secretary. The legislative note to this amendment stated, however, that the amended provision applied only to cost reports ending after June 30, 1973. Since no express provision for district court review of disputes regarding pre-1973 accounting periods was included, at least one court concluded that no review of these claims could be made. Although such a conclusion seems logical on its face, it fails to encompass the strong policy in favor of judicial review of constitutional claims. Accordingly, other courts rejected this conclusion, preferring to presume that a constitutional claim could be reviewed in the absence of an express provision otherwise.

In Weinberger v. Salfi, the United States Supreme Court focused on the “plain language” of § 405(h) to determine whether it precluded review of constitutional claims in a Social Security context. In Salfi, the Social Security Administration had determined that a widow was not eligible to receive Social Security insurance benefits. The decision was based on a Social Security Act duration-of-relationship eligibility provision. Despite the striking language of the third sentence of § 405(h), the three-judge district court concluded that this provision of the Social Security Act was nothing more than a codification of the doctrine of exhaustion of administrative remedies. Since all administrative remedies had been pursued by the plaintiff, the district court found that it had jurisdiction under 28 U.S.C. § 1331 (1970).

On direct appeal, the United States Supreme Court reversed the district court, holding that the district court was precluded from jurisdiction under § 1331. The Court vehemently disagreed with the district court’s narrow construction of the third sentence of § 405(h):

That the third sentence of § 405(h) is more than a codified requirement of administrative exhaustion is plain from its own language which is sweeping and direct and which states that no action shall be brought under § 1331, not merely that only those actions shall be brought in which administrative remedies have been exhausted.

35 Dr. John T. MacDonald Foundation v. Mathews, 554 F.2d 714 (5th Cir. 1977); St. Louis Univ. v. Blue Cross Hosp. Serv., 537 F.2d 283 (8th Cir. 1976), cert. denied, 430 U.S. 929 (1977); St. Elizabeth Hosp. v. United States, 558 F.2d 8 (Ct. Cl. 1977); Whitecliff, Inc. v. United States, 536 F.2d 347 (Ct. Cl. 1976), cert. denied, 430 U.S. 969 (1977).
36 422 U.S. 749 (1975).
37 Id. at 759. The doctrine of exhaustion of administrative remedies requires a party to seek all remedies at the administrative level before applying to the courts for judicial review. The doctrine is designed to prevent the courts from prematurely interfering with the administrative process. B. MEZINES, J. STEIN & J. GRUFF, ADMINISTRATIVE LAW, ¶ 43.02[3] at 22 (1978).
38 422 U.S. at 757.
The Supreme Court construed the "broad and sweeping" language of § 405(h) to preclude review under § 1331 of any action seeking to recover on any Social Security claim, "irrespective of whether resort to judicial processes is necessitated by discretionary decisions of the Secretary or by his nondiscretionary application of allegedly unconstitutional statutory restrictions."39

Although this construction of § 405(h) precluded all review under § 1331, the Supreme Court found that § 405(h) did authorize review of the plaintiff's constitutional claim under the alternative jurisdictional grant contained in § 405(g) of the Social Security Act. The Court thus concluded that the plaintiff was not unconstitutionally foreclosed from district court review of her constitutional challenge.40

As incorporated into the Medicare Act, § 405(g) afforded jurisdiction for district court review of only provider eligibility and termination claims.41 Section 405(g) did not provide the district court with jurisdiction over provider cost reimbursement disputes. Unlike the plaintiff in Salfi, therefore, Trinity could not obtain review of its due process claim pursuant to § 405(g). Accordingly, Trinity argued that the Salfi construction of § 405(h) should not be extended to Medicare provider reimbursement disputes. Trinity contended that Salfi's broad construction of § 405(h) was applicable only when the Social Security Act provided for an alternative method of review, and that, in the absence of specific alternative methods, the court was free to hear the case under § 1331.42

Presented with the dilemma of whether or not to extend the Salfi construction of § 405(h) to Medicare provider reimbursement disputes, the Seventh Circuit turned to relevant case law. Prior to Salfi, the courts routinely interpreted § 405(h) as a "codification of the doctrine of exhaustion of administrative remedies."43 Since the rejection of this construction by the Supreme Court in Salfi, the circuits have differed in their interpretations of § 405. The focal point of the controversy is the constitutional problem which would be created if the Salfi construction was extended to preclude all judicial review of constitutional claims. What has emerged from this controversy are two distinct formulae for interpretation.

1. Presumption of Reviewability

The "presumption of review" doctrine was firmly established by the United States Supreme Court in Rusk v. Cort.44 In Rusk, the Court held that the courts should restrict access to judicial review only upon a showing of "clear and convincing" evidence of a contrary legislative intent.45 In Johnson v. Robison,46 the Supreme Court again invoked the presumption of review doctrine for the particular purpose of authorizing federal courts to decide the constitutionality

39 Id. at 762.
40 Id.
41 See note 28 supra.
42 570 F.2d at 664.
43 See note 37 supra.
45 Id. at 379-80.
of veterans benefit legislation. The defendant in Johnson had moved to dismiss the claim for lack of jurisdiction on the ground that review was statutorily precluded. The statute in question prohibited judicial review of decisions rendered by the Administrator of Veterans’ Affairs on any question of law or fact arising under laws providing for veterans benefits. The Supreme Court concluded that the statute should not be extended to actions challenging the constitutionality of veterans’ benefit laws because “neither the text nor the scant legislative history of [the statute] provided the ‘clear and convincing’ evidence of congressional intent required by [the Supreme] Court before a statute will be construed to restrict access to judicial review.”

Trinity urged the Seventh Circuit to respect this presumption in cases raising constitutional issues by limiting the application of Salfi’s construction of § 405(h) to circumstances in which the Social Security Act provided an alternative method for review. When § 405(g) is not available as an alternative basis for review of a constitutional claim, as in Trinity, some courts have refused to adopt Salfi’s broad construction of § 405(h). Instead, these courts have presumed that Congress did not intend § 405(h) to operate as a preclusion of § 1331 review of constitutional claims in Medicare provider reimbursement disputes.

In St. Louis University v. Blue Cross Hospital Service, the Eighth Circuit refused to find complete preclusion of federal question jurisdiction by § 405(h). This post-Salfi case arose from a Medicare provider reimbursement dispute over cost accounting periods ending August 31, 1966. The provider asserted that the Medicare statutes and regulations were violated in determining reimbursement amounts and that he was deprived of an impartial hearing by the Provider Reimbursement Review Committee. Having concluded that Congress committed the determination of plaintiff’s proper reimbursement wholly to administrative discretion, the court considered whether § 405(h) precluded jurisdiction of the plaintiff’s due process challenge.

In Salfi, the Supreme Court had authorized review of the constitutional claim under § 405(g). In St. Louis, the decision was more difficult because § 405(g) did not afford an alternative basis for review of due process claims in Medicare reimbursement disputes. The Eighth Circuit thus refused to apply the Salfi interpretation of § 405(h) in a Medicare context so as to avoid the danger of unconstitutionally foreclosing the provider of services from judicial consideration of its due process objections.

Similarly, in Dr. John T. MacDonald Foundation v. Mathews, the Fifth Circuit distinguished § 405(h) in a Social Security context from § 405(h) in a Medicare context because of the unavailability of review under § 405(g). In that case, a Medicare provider sought declaratory and injunctive relief requiring the Secretary to reopen and recompute adverse reimbursement determinations. The court found that § 405(h), as incorporated into the Medicare Act, was not intended to preclude judicial review of issues, constitutional or otherwise, which

48 415 U.S. at 373-74.
49 570 F.2d at 664.
50 537 F.2d 283 (8th Cir. 1976), cert. denied, 430 U.S. 929 (1977).
51 554 F.2d 714 (5th Cir. 1977).
could not be reviewed in any other way. Although the Fifth Circuit openly recognized its construction of § 405(h) as "strained," it found general federal question jurisdiction under § 1331 as the basis for review of the provider's claim.

In Trinity, the Seventh Circuit rejected the position taken in both St. Louis and MacDonald that § 1331 afforded jurisdiction for due process claims. The court refused to presume that § 405(h) did not preclude review under § 1331. Instead, the court adopted the Salfi construction of § 405(h) to preclude all review under § 1331.

2. The South Windsor Approach

In Salfi, the Supreme Court justified its broad construction of § 405(h) by finding an alternative basis for review of the plaintiff's constitutional claim under § 405(g). Although § 405(g) was unavailable as a basis for review in Trinity, the Seventh Circuit still adopted Salfi. To avoid the danger of totally precluding review of Trinity's due process claim, the Seventh Circuit followed the approach taken by the Second Circuit in South Windsor Convalescent Home, Inc. v. Mathews.

In South Windsor, a provider challenged the validity of a Medicare regulation permitting the government to recoup accelerated depreciation taken by a provider that had terminated its participation in the Medicare program. Despite the constitutional underpinnings of the provider's claim, the Second Circuit relied on Salfi to preclude jurisdiction under § 1331. The court found, however, that the Court of Claims had jurisdiction under 28 U.S.C. § 1491 (1970). Reasoning that the third sentence of § 405(h) merely forbade review "under section 41 [now § 1331] of Title 28," and that § 1491 was not part of the original § 41, the court found that review by the Court of Claims would not violate § 405(h).

The Seventh Circuit, in Trinity, expressly followed the reasoning of the Second Circuit in South Windsor. The court thus held that § 405(h) was not a bar to review of Trinity's case in the Court of Claims.

In Salfi, South Windsor, and Trinity, each court construed the third sentence of § 405(h) as totally precluding § 1331 jurisdiction to review constitutional objections to agency decisions. Each court expressly noted that, in the absence of an alternative grant of jurisdiction for review of a constitutional claim, this construction could render § 405(h) constitutionally invalid. Each court, however, avoided this clash with the Constitution by finding an alternative avenue for review.

52 Id. at 718.
53 541 F.2d 910 (2d Cir. 1976).
54 28 U.S.C. § 1491 (1970), in pertinent part, provides:

The Court of Claims shall have jurisdiction to render judgment upon any claim against the United States founded either upon the Constitution, or any act of Congress, or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort. In any case within its jurisdiction, the court shall have the power to remand appropriate matters to any administrative or executive body or official with such direction as it may deem proper and just.

55 See text accompanying note 22 supra.
56 570 F.2d at 667-68.
Unlike the Supreme Court in *Salfi*, the Second Circuit in *South Windsor* was unable to find an alternative basis for district court review of the constitutional claim. By merely retracing the steps taken by the Second Circuit in *South Windsor*, the Seventh Circuit in *Trinity* overlooked the inadequacies inherent in that approach. First, whether the legislative scheme permitted Trinity, as a provider of services, to seek review of its constitutional claim in federal district court was unclear. Consequently, Trinity erroneously relied on § 1331 as the basis for review of its due process claim. Although granted the opportunity to sue in the Court of Claims, Trinity must incur additional expenses in order to obtain review, after having expended the time and money to proceed in the district court. Second, such limited relief may not be available to all who express constitutional objections in the Medicare context, since the jurisdictional grant of § 1491 only extends to monetary, not equitable, relief.

Several other courts which have adopted *Salfi*'s broad construction of § 405(h) have found an alternative basis of jurisdiction under 28 U.S.C. § 1361 (1970), which gives the district court “original jurisdiction of any action in the nature of mandamus to compel an officer or employee of the U.S. or any agency thereof to perform a duty owed to the plaintiff.” Mandamus jurisdiction for review of administrative decisions has been extended to both statutory and constitutional allegations. Mandamus relief will be granted, however, only when there is, (1) a clear right in the plaintiff to the relief sought, (2) a plainly defined and peremptory duty on the part of the defendant(s) to do the act in question, and (3) no other adequate remedy available. Consequently, mandamus relief has typically been granted only in rather extraordinary circumstances. Affording a plaintiff an opportunity to initiate an action for mandamus, then, may be an even more inadequate form of relief than allowing the plaintiff to proceed with its suit in the Court of Claims.

IV. Post-Trinity Developments

The underlying constitutional question surrounding § 405(h) and other preclusion-of-review statutes resurfaced in two post-*Trinity* cases. Upon reconsideration of its earlier decision in *Dr. John T. MacDonald Foundation v. Mathews*, the Fifth Circuit held that § 405(h), as incorporated into the Medicare Act, precluded all review of the Secretary's decision by federal district courts under § 1331. The court abandoned the former distinction between § 405(h) in the Medicare context and § 405(h) in the Social Security context. Adopting the *Salfi* approach, the Fifth Circuit extended § 405(h) to preclude review of both statutory and constitutional claims, but found review available in the Court

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57 See note 65 infra.
60 City of Milwaukee v. Saxbe, 546 F.2d 693, 699-701 (7th Cir. 1976); City of Highland Park v. Train, 519 F.2d 681, 691 (7th Cir. 1975).
61 571 F.2d 328 (5th Cir. 1978).
62 Id. at 329.
of Claims. It was expressly observed that, since all review was not precluded, the constitutionality of § 405(h) was not drawn into question. As in Trinity, the court was thus excused from "intimating any view as to the constitutionality of a congressional scheme that would bar all judicial review of [Medicare provider reimbursement] disputes..." 

In another later case, American Association of Councils of Medical Staffs v. Califano, the Fifth Circuit addressed the question of § 405(h) preclusion in a somewhat different factual context. In that case, an association of medical councils of private hospitals brought an action on behalf of its physician members, challenging certain federal regulations promulgated under the Medicare Act. The court never reached the merits of the judgment against the plaintiff because it found the jurisdiction issue to be dispositive of the case. Unlike the providers in South Windsor, Trinity and MacDonald, the plaintiffs in CMS sought injunctive and declaratory relief, and thus could not obtain review in the Court of Claims. The court, nonetheless, regrettably denied both parties a decision on the merits because of the lack of federal jurisdiction over the case:

The resolution we have reached is not pleasant. CMS has waited nearly three years for the resolution of its suit.... We must deny both parties a decision on the merits where at least one argument is substantial. But the alternative is to find that Congress cannot cut off jurisdiction over these issues while providing another Court, the Court of Claims, to hear the issues. That is a decision we cannot make....

The Fifth Circuit expressed doubt over the constitutionality of § 405(h), yet once again failed to decide the issue. Instead, the court alluded to the alternative of bringing a suit for mandamus to resolve "what [was] obviously an important issue to the private hospitals in this country." This result resembled the results in both South Windsor and Trinity. The plaintiff's only relief was the opportunity to renew its claim in another forum after having expended the time and money to seek review in the district court. In addition, the court was again excused from intimating any view as to the constitutionality of § 405(h) in the Medicare context.

V. Conclusion

At a time when the excessive power of administrative agencies is a growing concern, judicial review is an important control device, particularly as a means
of challenging the constitutionality of agency actions and regulations. The jurisdiction of the federal courts to review such constitutional claims, therefore, should not be unduly restricted. Conceding, however, that Congress has the power to limit jurisdiction to review agency decisions, clarity in drafting preclusion-of-review provisions such as § 405(h) would reduce the risk involved in choosing the wrong forum,70 as well as the need for indulging in "strained" determinations of congressional intent.71

In Trinity, the Seventh Circuit held that the 1970 version of § 405(h) precluded district court review under § 1331 of Trinity's constitutional claim. This case is important, however, not for what it decides, but for what it does not decide. By allowing Trinity to sue in the Court of Claims, the court excused itself from intimating any view as to the constitutionality of a congressional scheme that would bar all judicial review of valid constitutional objections originating in an administrative proceeding. The 1974 amendment to the Medicare Act, which expressly authorized judicial review, significantly reduced the likelihood of such a constitutional dilemma resurfacing in the Medicare provider reimbursement context. A similar problem may arise, however, as it has previously,72 from preclusion-of-review provisions in other administrative contexts. If the Seventh Circuit had specifically addressed the constitutional issue arising from § 405(h), it could have made a significant contribution toward initiating a resolution. As indicated by the more recent cases, however, the constitutional dilemma surrounding § 405(h) and similar preclusion-of-review provisions remains unresolved.

Bernadette Muller

70 L. JAFFE, JUDICIAL CONTROL OF ADMINISTRATIVE ACTION (1965); Jurisdiction to Review Federal Administrative Action: District Court or Court of Appeals, 88 HARV. L. REV. 980, 999 (1975).
71 Dr. John T. MacDonald Foundation v. Mathews, 554 F.2d 714, 718 (5th Cir. 1977).
I. Introduction

The purpose of the National Labor Relations Act is to prescribe the rights of both employees and employers and to provide orderly and peaceful procedures for preventing interference by one party with the legitimate rights of the other. In furtherance of this goal, Congress has declared it an unfair labor practice for an employer to refuse to bargain collectively with the representatives of his employees.

As early as 1936, the National Labor Relations Board recognized that an employer who claimed inability to afford a wage increase but who would neither prove his claim by providing financial statements nor permit independent verification of the claim was not engaging in good faith bargaining. To encourage such good faith bargaining, Section 8(a)(5) of the Act has been held to prescribe that an employer must furnish to the collective bargaining agent information relevant to the bargaining process.

In NLRB v. Custom Excavating, Inc., the United States Court of Appeals for the Seventh Circuit addressed the issue whether an employer is required to furnish to a union the names and addresses of customers for whom work was performed by union members.

II. Statement of the Facts

The controversy arose when Retzack, the union’s business representative, was visiting union jobsites for the purpose of checking compliance with a collective bargaining agreement. At that time, he noted that Thimke, a union member, was working on Saturday, September 13, 1975. Approximately one month later, Retzack contacted Grimm, the company’s president and informed him that the

* 575 F.2d 102 (7th Cir. 1978).
1 29 U.S.C. §§ 151-68 (1970) [hereinafter cited as NLRA or the Act].
2 See Fanning, The Obligation to Furnish Information During the Contract Term, 9 Ga. L. Rev. 375 (1975).
3 29 U.S.C. § 158(a) (1970) 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 159(a) of this title.”
4 Hereinafter referred to as NLRB or the Board.
5 Pioneer Pearl Button Co., 1 N.L.R.B. 837, 842-43 (1936).
8 575 F.2d 102 (7th Cir. 1978). The appeal in NLRB v. Custom Excavating, Inc., was originally decided by unreported order. The Seventh Circuit subsequently issued a published opinion.

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union had reason to believe that the company was not compensating its operating engineers properly and asked to inspect the company's payroll records. Grimm refused to comply with the request. Approximately three months later, after the union threatened to file a grievance, Grimm allowed Retzack to inspect the payroll records of the two operating engineers in the bargaining unit.

The records provided reflected no hours worked by Thimke on Saturday, September 13, 1975, and Retzack, proclaiming the records a "patent fraud," requested a complete record of all payroll dates with respect to the company's operating engineers for 1975. In addition, Retzack demanded a complete list of the customers for whom the company had done work involving the operation of construction equipment in order to resolve the perceived problem with the payroll records. The information was not forthcoming and the union filed an unfair labor practice charge with the NLRB.

At the ensuing hearing before an administrative law judge, Retzack testified that the union considered the requested information essential to prove the fraudulent nature of the payroll records. Moreover, the union introduced the testimony of two former employees which indicated that the company regularly maintained falsified records.

The company argued that such information was confidential and that its customers would be unable to provide the requested information, namely, dates and times when unit employees had worked. The administrative law judge rejected these arguments and concluded that the company had refused to bargain in good faith when it failed to furnish the union with the requested information.10

The NLRB affirmed the findings and conclusions of the administrative law judge and separately stated Conclusions of Law which the administrative law judge had inadvertently failed to set forth.11

The Seventh Circuit affirmed the decision of the Board holding that the NLRA required the disclosure of customer lists. The court modified the order of the Board, however, to require respondent to furnish to the union only the names of those customers for whom work was done by unit employees in 1975.12

III. NLRA Mandates Good Faith Bargaining

The NLRA is intended to encourage the peaceful settlement of labor disputes by collective bargaining.13 Section 8(a)(5) of the Act labels a refusal to bargain collectively an unfair labor practice and thereby illustrates the great importance which Congress has ascribed to the collective bargaining process in an effort to ensure industrial stability.14

Despite strong Congressional endorsement of the collective bargaining process, the NLRA is flawed by its overly broad definition of the term "collective

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9 575 F.2d at 104.
10 Id. at 105.
11 Id.
12 Id. at 108.
13 See Fanning, supra note 2.
14 Curtiss-Wright Corp., Wright Aero Div. v. NLRB, 347 F.2d 61, 68 (3rd Cir. 1965).
The Act fails to describe those actions or attitudes which constitute good faith bargaining and, therefore, merely provides broad guidelines used to define and interpret the specific duties which are imposed upon the parties engaged in collective bargaining. As a result, the NLRB must determine what constitutes “good faith” bargaining in each individual context.\textsuperscript{16}

A. Good Faith—A Factual Determination

There exists a wide spectrum of management actions, each of which may, under given circumstances, constitute an unfair labor practice. Whether a particular management action will be classified as such generally is determined by the factual context in which that action occurs.\textsuperscript{17} Refusal to furnish information requested by a union is one such action which might constitute an unfair labor practice.

The Supreme Court has concluded, therefore, that the NLRB has the right, after reviewing the surrounding circumstances, to consider the refusal to furnish information in determining whether the obligation of good faith bargaining has been met by the employer.\textsuperscript{18}

B. Information Requests

In appropriate circumstances, it is apparent why refusal to furnish needed information constitutes an unfair labor practice. The union is designated by a majority of employees in the unit as the exclusive bargaining representative and as such is charged with the responsibility of negotiating and administering the collective bargaining agreement. Without the disclosure of pertinent data, the union would be handicapped in negotiations with the employer and would be unable to properly perform its statutorily imposed duties. Since the mere meeting and conferring of the parties, without a prior exchange of relevant requested data does not facilitate effective collective bargaining, it does not meet the good faith bargaining requirement of Section 8(a)(5).\textsuperscript{19} Thus, the general obligation of the employer to furnish necessary and relevant information is a natural corollary to the duty to meet and confer in good faith.

\textsuperscript{15} The term “collective bargaining” is defined for purposes of the Act by 29 U.S.C. § 158(d) (1970), which provides in pertinent part:

For the purposes of this section, to bargain collectively is the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment, or the negotiation of an agreement, or any question arising thereunder, and the execution of a written contract incorporating any agreement reached if requested by either party, but such obligation does not compel either party to agree to a proposal or require the making of a concession.

\textsuperscript{16} See Fanning, supra note 2.

\textsuperscript{17} See, e.g., note 49 infra for a discussion of two instances in which management’s refusal to provide information may constitute an unfair labor practice.

\textsuperscript{18} NLRB v. Truitt Mfg. Co., 351 U.S. 149, 152 (1956) (employer claiming financial difficulties refused to provide information on financial standing and profits).

\textsuperscript{19} 347 F.2d at 68.
C. Qualifying the Duty to Furnish Information

Several qualifications restrict significantly the type and scope of the information to which the union is entitled. The NLRA's mandate of good faith bargaining dictates that the union must genuinely believe that the information requested is needed for collective bargaining purposes. Furthermore, requests for data need only be honored when the information sought is relevant and necessary to the union's duty to negotiate and administer collective bargaining agreements. As the Court in NLRB v. Truitt remarked, "[e]ach case must turn upon its particular facts. The inquiry must always be whether under the particular circumstances of the particular case the statutory obligation has been met."

Information of any description may be requested and received under appropriate circumstances. In its seminal decision, the Custom Excavating court has determined that customer lists may be an appropriate subject for a union's request for data. The inquiry must now focus on those factors which, when analyzed within a factual context, establish the propriety of the request.

IV. Relevance: The Critical Issue

A. Relevance and Necessity—A Single Criterion

In NLRB v. 'Acme Industrial Co., the Supreme Court prescribed a rule which required an employer to furnish requested information which is both relevant and necessary to the bargaining process. Although many court and NLRB decisions are framed in terms of this dual language, once relevance is found, typically, the information is found to be necessary as well. In fact, the terms "relevant" and "necessary" are synonymous because once information is construed as relevant, it is a fortiori necessary. Thus, the rule has been stated: "[T]he requested data is relevant and therefore reasonably necessary to a union's role as bargaining agent in the administration of a collective bargaining agreement, it is an unfair labor practice within the meaning of Section 8 (a) (5) of the Act to refuse to furnish the data."

Necessity, therefore, is not a separate and unique guideline which must be independently satisfied but rather is subsumed in the standard of relevance. Accordingly, regardless of what type of information is requested by a union, the critical inquiry is whether disclosure of that information is relevant to the union's collective bargaining responsibilities.

20 351 U.S. at 152. This comment examines a situation in which the request for information was made from a union to an employer. The requirement of good faith bargaining, however, is equally applicable to unions. It may be assumed that unions have a similar obligation to furnish relevant information upon request by an employer. See 29 U.S.C. § 158(b)(3) (1970). There appear to be no decisions, however, concerning the scope or nature of a union's duty to furnish information to an employer. See Di Fede, Employer Duty to Disclose Information in Collective Bargaining, 6 N.Y.L.F. 400 (1960).
21 385 U.S. at 437.
22 351 U.S. 149 (1956).
23 Id. at 153 (emphasis added).
26 347 F.2d at 68 (emphasis added).
B. Relevance in Custom Excavating

In *Custom Excavating*, the information requested was clearly relevant to the union’s pending grievance. For a period of approximately six months the union had sought payroll information from the employer. The data, eventually provided, was deliberately falsified and of no use to the union. Thus, the court properly concluded that it was “appropriate for the union to check with the company’s customers to determine whether the company was falsifying payroll records as contended in the January 8 grievance.” 27 The Seventh Circuit, however, apparently recognizing the existence of a single standard of “relevance and necessity,” treated the union’s request only in terms of need.

With its decision in *Custom Excavating*, the Seventh Circuit became the first court of appeals to sustain the right of a union to an employer’s customer lists. Since the weight of the evidence clearly established the relevancy of the information to the union’s pending grievance, the court, without distinguishing the nature of the information, endorsed prior holdings which found refusals to bargain in good faith when employers withheld relevant information. 28

C. Developing a Standard of Relevance

Although the relevancy of the request in *Custom Excavating* was evident, situations will arise in which “the thin red line between hard bargaining and refusal to bargain . . .” 29 will be difficult to delineate. This will be particularly true when the information requested, such as customer lists, has no apparent application to the union’s right to gather information pursuant to its collective bargaining responsibilities. Thus, although there is a need for a more definite standard of relevance, acknowledging that need is far easier than deriving the appropriate standard.

In *Acme Industrial Co.*, the Supreme Court concluded that the standard to be applied to a union’s request for information should be a liberal “discovery-type” determination of relevance. 30 Analogizing to a discovery standard suggested by Professor Moore, 31 the majority ordered the enforcement of an NLRB order when the Board had acted upon the probability that the desired information was relevant and that it would be of use to the union in carrying out its statutory duties and responsibilities. The Court seemed to indicate that broad

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27 575 F.2d at 106.
28 Id.
29 NLRB v. Dothan Eagle, Inc., 434 F.2d 93 (5th Cir. 1970). The court continued: “Some cases are so clear that we are led to one side or the other, but in the difficult case we must in many instances rely extensively on the subjective factual conclusions of the [administrative law judge] and the Board.” Id.
30 385 U.S. at 437.
31 Cf. 4 Moore’s Federal Practice § 26.16 [1] (2d ed. 1948). Professor Moore suggests the following:

[I]t must be borne in mind that the standard for determining relevancy at a discovery examination is not as well defined as at the trial. . . . Since the matters in dispute between the parties are not as well determined at discovery examinations as at the trial, courts of necessity must follow a more liberal standard as to relevance.

Id. at 1175-76.

“Examination as to relevant matters should be allowed whether or not the theory of the complaint is sound or the facts, if proved, would support the relief sought.” Id. at 1181.
discretion lies with the trial court in determining relevancy—provided the determination is based on factual circumstances. Thus, the Court enunciated a standard which infers an adjustable upper limit to the restrictions which may be imposed upon a union information request.¹²

When the information sought, however, is so "picayune" that failure to obtain it would not impede the union's effective representation of the employees, no requirement to furnish it exists.¹³ Thus, even under the liberal "discovery-type" standard, some information which might be useful to the union will not fall within the scope of Section 8(a)(5).

The task remains, however, to distinguish between hard bargaining and a refusal to bargain. The incident of a request for customer lists is illustrative of this dilemma.

D. Customer Lists

Customer lists, in most situations, are unlikely to be a useful tool for purposes of collective bargaining. The sole function of such nonfacially relevant information in the collective bargaining process would be to verify other data provided to the union by the employer or to provide information which the employer claims is not in his possession.

In Custom Excavating, the company argued that customer lists would not be useful to the union because the customers either did not have the desired data or would not talk to the union.¹⁴ As the court correctly explained, however, the ultimate utility of the information was not the issue.¹⁵ Rather, the issue was whether the requested data might prove useful to the union in the pending grievance procedure.

Recognizing that a union is always capable of requesting, in good faith, information for purposes of verifying previously received data, the union should be required to offer some additional justification for the demand. Considering the employer's demonstrated bad faith in Custom Excavating, consultation with the company's customers was the sole independent means of verifying the information furnished. Thus, the union's need for the customer list is legitimate when evaluated within the whole context of the dispute. Additionally, the union's representative in the hearing before the administrative law judge explained that

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¹² The Acme Industrial standard provides little guidance to the employer who is seeking to determine the relevancy of a union request for information. Thus, except in instances of clearly relevant collective bargaining information, an employer must resort to litigation in order to have his responsibilities defined.

¹³ American Standard, 203 N.L.R.B. 1132, 1133 (1973) (request for 9-year-old job descriptions). The Board further stated that "the alleged misconduct [refusal to furnish 9-year-old job descriptions] is of such obviously limited impact and significance that we ought not to find that it rises to the level of constituting a violation of our Act." Id.

¹⁴ 575 F.2d at 106.

¹⁵ Id. The court explained: [B]ecause of the need for verification, it is immaterial that the union might secure some overtime information from its members. While the Company attempted to show that some of its customers would be unwilling or unable to supply information to the union relevant to its grievance, under Acme Industrial Co., the union is at least entitled to attempt to bolster its case through the customers. Whether it will succeed or not is not an issue here.

Id.
the request was made in the light of the union's specific purpose of proving "the patently fraudulent nature of [the company's] payroll records."

In Fawcett Printing Corp., the union articulated a similar suspicion of fraud, namely, that the reasons advanced by the company for planned layoffs were spurious. The NLRB concluded that the information requested was relevant and ordered the company to furnish the requested customer information. Thus, customer lists are likely to be relevant when either the employer claims a lack of information or when the union can advance an "articulable suspicion" that the information provided by the employer is fraudulent or inaccurate.

Although declining to define a particular standard, at least two courts of appeal have addressed the issue of union requests for nonfacially relevant data.

In Prudential Insurance Co. of America v. NLRB, the union requested a list of the names of all employees in the bargaining unit regardless of membership in the union. Prudential refused to supply the names of those employees who were not union members. The union contended that the information was necessary for the union to locate and to communicate with these employees and that no other adequate means of communication were available. In sustaining the union's right to the names, the Second Circuit stated:

When a union requests information which is not ordinarily relevant to its performance as bargaining representative but which is alleged to have become so because of peculiar circumstances, the courts have quite properly required a special showing of pertinence before obliging the employer to perform.40

The need for a special showing of relevance was reiterated in San Diego Newspaper Guild v. NLRB.41 In Newspaper Guild, the union requested the names of nonunion employees who were being trained by the appellant to replace union employees in the event of a strike. The Ninth Circuit, following Prudential, noted that when the union requests unusual information, a special showing of relevance is required.42

Accordingly, a union must present specific reasons to justify its request for unusual information. A generalized assertion of need will not be sufficient. The requirement of stating an "articulable suspicion" merely prescribes a specialized form of the showing of relevance. The "articulable suspicion" standard strikes a balance between a standard of assumed relevance for all information requests and one which requires such an overwhelming proof of relevance that it effectively defeats the liberal "discovery-type" standard.43

36 575 F.2d at 105.
38 This "articulable suspicion" standard might be analogized to the standard required for a warrantless search. Cf. Terry v. Ohio, 392 U.S. 1 (1968).
40 Id. at 84.
41 548 F.2d 863 (9th Cir. 1977).
42 Id. at 867.
43 Id. at 869.
V. Harmonizing the Precedents

Three reported cases have arisen which specifically address the issue whether a union should be granted its request for an employer's customer lists. Only one of these, Custom Excavating, has progressed to the appellate level. The others, Fawcett Printing Corp. and American Needle & Novelty Co., were decisions of the National Labor Relations Board. The holdings of the Board in these two cases are apparently contradictory.

A. American Needle & Novelty Co.

In American Needle, the Board affirmed the administrative law judge's ruling that an employer is not obliged under the National Labor Relations Act to furnish customer lists upon request. The Board had previously concluded in Fawcett Printing Corp., that an employer was required to furnish such information. With these two NLRB decisions as precedent, Custom Excavating assumes a pivotal position. Although the Custom Excavating court disagreed without explanation with the Board's conclusion in American Needle, the two holdings, as well as that in Fawcett Printing Corp., can be reconciled. The critical question in analyzing the American Needle decision is, as previously discussed, relevance.

In American Needle, the union's request was made incident to a claim by the employer that for economic reasons it was unable to continue the operation of one of its plants and intended to close it. Although the claim of financial inability forced the employer to substantiate his claim by providing financial records to the union, it manifestly did not support a demand for customer lists by the union. Thus, the union, if it desired the data, was bound to make some effort to substantiate the request.

45 It is well established that the National Labor Relations Board's determination whether requested information is relevant in a particular case is given great weight by the reviewing court. This weight attaches to the Board's findings either because the determination is a finding of fact that is conclusive if supported by substantial evidence under Section 10(e) of the Act or because it is a mixed question of law and fact which is within the particular expertise of the Board. See, e.g., 548 F.2d at 867.

Although great weight is given to Board determinations, judicial review is not foreclosed. As the Supreme Court stated in Universal Camera Corp. v. NLRB, "[A] reviewing court is not barred from setting aside a Board decision when it cannot conscientiously find that the evidence supporting the decision is substantial, when viewed in the light that the record in its entirety furnishes, including the body of evidence opposed to the Board's view." 340 U.S. 474, 488 (1951).
46 206 N.L.R.B. at 545.
47 201 N.L.R.B. at 976.
48 206 N.L.R.B. at 540.
49 In addition to the rule raised in Custom Excavating, two other rules apply to requests for information by a union. First, when an employer in the course of negotiations cites financial inability as a reason for refusal to bargain, the burden is generally upon the employer to substantiate his claim by production of financial statements and records. See, e.g., 351 U.S. at 152. It does not necessarily follow, however, that employees are entitled to substantiating evidence. As noted previously, "[e]ach case must turn upon its particular facts. The inquiry must always be whether under the circumstances of the particular case the statutory obligation to bargain in good faith has been met." Id. at 153.

The second rule provides that when the union's request is for wage data information, such as payroll records, the data is presumptively relevant and the employer in the absence of rebuttal is required to furnish it. See, e.g., Boston Herald Trav. Corp. v. NLRB, 223 F.2d 58 (1st Cir. 1955).
showing of relevance. The union made no attempt, however, to demonstrate the relevance of the request. Absent such a showing, the Board’s conclusion that the employer should not be required to furnish the information was proper.

B. Fawcett Printing Corp.

In both Fawcett Printing Corp. and Custom Excavating, however, the requests for customer lists were made as a result of legitimate questions which arose about the information furnished by the employer. In Fawcett Printing Corp., the employer was in the process of laying off union workers, ostensibly in response to the company’s customers taking their business elsewhere because of a fear of an imminent strike. The employer refused to explain the relationship between the company and the Fawcett Publishing Company or to provide the union with information about contracts with other publishing companies. Consequently, the union did not believe the asserted reasons for the layoff and requested the customer lists. The employer refused to release the information and the union charged the employer with a violation of Section 8(a)(5).

At the ensuing hearing the union explained that the requested information was necessary in order for the union to establish the veracity of the employer’s claim that no work was being subcontracted. The administrative law judge, with subsequent affirmation by the Board, concluded that the requested information was relevant to the “not untenable theory that . . . the correspondence between Respondent and its customers regarding the removal of such work [from Respondent’s plant] might reveal who really decided on such removal.”

C. The Custom Excavating Rationale

In Custom Excavating, the request for the customer lists was made in a context in which the relevance of the information to the union was apparent. Indeed, before demanding the customer lists, the union representative had proclaimed the records provided to be a “patent fraud.” Moreover, the union’s evidence was presented to the administrative law judge virtually without rebuttal.

Thus, although the Seventh Circuit properly dismissed respondent’s reliance upon American Needle, the inference should not be drawn that the court feels that customer lists will always be the proper subjects of a union’s request for information. Such an inference would be unwarranted and clearly the court did not intend such a result. A careful reading of Custom Excavating demonstrates that the decision is largely founded on the facts of that particular case. Thus, a more enlightened interpretation of the court’s holding is that customer lists are proper subjects of a union’s request for information when an employer provides fraudulent or inaccurate data or claims that information requested is not in his possession.

50 201 N.L.R.B. at 975.
51 575 F.2d at 104.
VI. Defenses to an Action for Failure to Furnish Information

In its disposition of Custom Excavating, the Seventh Circuit dismissed, virtually without comment, the company’s assertions of harassment and confidentiality. The court decided correctly that the company may not avoid the union’s request for relevant information by the interposition of these defenses unless they have some bases in fact. Moreover, the company’s expressed fear of customer harassment and the need to shield its customers from such abuse is merely another way of asserting a need for secrecy. Thus, the company’s two defenses effectively assert only a need for record confidentiality.

A. Confidentiality Claims Are Closely Reviewed

The confidentiality of an employer’s records is a principle which has rarely found support in the courts. As the Sixth Circuit has declared, “[t]he requirement that the bargaining representative be furnished with relevant information necessary to carrying on its duties overcomes any claim of confidentiality in the absence of great likelihood of harm flowing from disclosure.” This is not to say, however, that a claim of confidentiality will never be honored, but rather that the standard applied to such a claim will be very demanding. In short, the union’s right to relevant information is superior to any right of the employer to withhold such information to preserve its secrecy except in the most extreme circumstances.

B. Employers’ Alternatives

Employers undoubtedly will decry the decision in Custom Excavating with assertions of potential secondary boycotts and other harassment against customers. The mandate to bargain in good faith, however, applies just as strongly to the union as it does to the employer. Thus, if an employer can substantiate past acts of harassment or probable future harassment if the union is provided customer lists, he may withhold the information pending assurances from the union that the data will not be misused. Moreover, harassment is strongly condemned by national labor policy and the courts have regularly upheld broad orders designated to prevent or counteract such activities. Further, violation of such orders or restrictions would be subject to the same sanctions as violations of any provision of a judicially enforced order.

VII. Conclusion

The holding of the Seventh Circuit in Custom Excavating was proper...
considering the relevance to the union of the customer lists in completing its investigation of falsified employer records. Given the bad faith of the employer, as evidenced by the delivery of doctored records, a ruling denying the lists to the union would have been incorrect.

The Seventh Circuit initially decided *Custom Excavating* by unreported order, but later published its opinion. One might infer from this action that the court was aware of the importance of the case and sought to avoid potential misinterpretation.

Initially, the *per curiam* opinion appears to grant the union a right to customer lists which is akin to the union's right to other forms of bargaining related information. Such an interpretation, however, misconstrues the court's opinion which, although flawless in its logic and application of the law, is marred by its failure to elaborate on the bases of the decision. Consequently, the opportunity to misapply this precedent still exists.

Generally, customer lists will be of little legitimate interest to unions in the execution of their collective bargaining duties. Moreover, information of this type is potentially damaging to an employer if it is utilized for such illegitimate purposes as harassment and secondary boycotts against customers. Although remedies are available to the employer for such violations of the union’s duty to bargain in good faith, they are of little value once the damage is incurred. Thus, it is imperative that the courts clearly explicate that customer lists generally are not relevant and that a union is not entitled to such information unless it is able to advance an “articulable suspicion” that the employer has acted in bad faith.

Two situations in which such a genuine need is likely to arise are (1) when the employer claims the information is not available to him, and (2) when the employer supplies fraudulent or inaccurate data. A generalized assertion, however, that the data presented is fraudulent or inaccurate, without the establishment of an “articulable suspicion” upon which to found the assertion, should not be sufficient to sustain the union’s request for customer list information. Moreover, since the situations, enumerated above, are not all inclusive, the courts should not summarily dismiss requests made in other factual settings. Rather, the courts should closely scrutinize the circumstances to determine if an “articulable suspicion” exists upon which the request for customer lists is based.

The Seventh Circuit’s failure to elaborate on its reasoning for enforcing the order of the NLRB in *Custom Excavating* should not be construed in a manner which would make customer lists generally available. Clearly this was not the intention of the court. The applicable rule is that customer lists must be furnished in the unusual circumstance in which the union advances an “articulable suspicion” that the employer, in exhibiting bad faith, has furnished falsified information or has refused to furnish requested information which is relevant to the union’s collective bargaining responsibilities. Thus, union entitlement to customer lists is the exception, not the rule.

Timothy J. Carey

59 *See, e.g.*, note 49 *supra*, for a discussion of two instances in which a union’s right to bargaining related information has generally been upheld.
In Harrison v. Chrysler Corporation, the Seventh Circuit confronted the issue of whether failure to exhaust intraunion remedies could be raised by an employer as a defense to an action brought by an employee under § 301(a) of the Labor Management Relations Act. The court's holding, to the extent it allows such a defense, constitutes a clear departure from the generally recognized principle that failure to exhaust intraunion remedies is a defense available only to the union.

Terrence J. Harrison inspected power steering units on an assembly line at a Chrysler electrical plant in Indianapolis, Indiana. On December 5, 1966, Harrison was discharged for allegedly falsifying a production count. Harrison denied the falsification and sought reinstatement and back pay by resorting to a grievance procedure established under the collective bargaining agreement between Chrysler and his union.

The union filed a grievance protesting the discharge, and shortly thereafter Harrison was offered reinstatement by the labor relations supervisor for Chrysler if he would admit that he falsified the production count and consent to a 30-day disciplinary layoff. Harrison rejected the offer. At about that time, the president of the local union privately told Chrysler's labor relations supervisor that he did not think Harrison was telling the truth.

The grievance was processed through the initial grievance procedure which consisted of four steps in which union and management representatives, at ascending levels of responsibility, attempted to resolve the employee's grievance. Under the collective bargaining agreement, if the participants in the last step of the grievance procedure could not resolve the dispute, the union could refer the grievance to an appeal board consisting of union officials, management executives and an impartial chairman. The appeal board would then consider the grievance in two stages. First, union and management representatives would attempt to settle. If they could not, the matter was to be resolved by a decision of the impartial chairman acting as arbiter. A decision of the appeal board would be final and binding on all parties. Harrison's grievance was processed

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* 558 F.2d 1273 (7th Cir. 1977).
1 558 F.2d 1273 (7th Cir. 1977).
3 558 F.2d at 1275.
4 Harrison was a member of the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America and its Local Union No. 1226. Id. at 1275 n.1.
5 Id. at 1276.
6 Id.
7 Id.
8 Id.
9 Id.
through the initial procedure and finally referred to the appeal board.

On July 10, 1969, the union and management representatives on the board issued a written disposition of the grievance under which Harrison was granted reinstatement with full seniority but was denied back pay. Harrison was informed of the board's decision in 1971 after he telephoned a representative of the union concerning the progress of his grievance. The representative advised Harrison of the decision and told him it was final. Harrison rejected the board's decision and subsequently brought this action against Chrysler under Section 301(a) asserting that the union had unfairly represented him in the grievance proceedings. The United States District Court for the Southern District of Indiana granted summary judgment for Chrysler on the ground that Harrison had failed to exhaust his intraunion remedies.

The Seventh Circuit reversed, concluding that an employer may raise the intraunion exhaustion defense under limited circumstances, but that it was unavailable in this case because Chrysler had failed to establish that any private remedy was available to Harrison to satisfy his claim for back pay.

Harrison's treatment of the intraunion exhaustion defense is novel in two respects. First, the facts of this case did not present circumstances under which the defense might be available to the employer. Consequently, the Seventh Circuit's determination of the issue was not necessary to decide the case. Second, those federal courts that have considered this question have held almost

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10 Id.
11 Harrison's assertion of unfair representation was based on the following: 1) the statement by the president of the local union, to Chrysler's labor relations supervisor, that he disbelieved Harrison; 2) the slow processing of his grievance which resulted in a 2½-year delay between filing and disposition; 3) the ultimate agreement of the union's representatives on the appeal board not to take the grievance to arbitration, but rather, to grant Harrison the same relief he had earlier rejected; and 4) the failure of the union to notify him of the appeal board's decision. Id. at 1277.
12 A union's constitution usually establishes certain intraunion appellate procedures designed to allow a member dissatisfied with the action taken by the union to challenge such action. The procedures in this case, as set forth in Article 32 of the 1968 Constitution and Article 33 of the 1970 Constitution are as follows:

Section 1. All subordinate bodies of the International Union, and members thereof, shall be entitled to the right of appeal.

Section 2. Any member of any Local Union or unit of an Amalgamated Local Union who wishes to challenge any action, decision or penalty of that body or of any official or representative of that body must, in all cases and procedures where no other time limit is specifically set forth by this Constitution, initiate the challenge before the appropriate body of such Local Union or unit within sixty (60) days of the time the challenger first becomes aware or reasonably should have become aware of the alleged action, decision, or penalty of that body.

Section 5. Any member feeling himself aggrieved by any action, decision or penalty of his subordinate body shall be entitled to appeal that action, decision or penalty to the International Executive Board only when it has been passed upon by the Local Union membership or delegate body, as the case may be; except where direct appeal to the International Executive Board from some action, decision or penalty of a body other than the Local Union membership or delegate body shall be specifically permitted by another Article of this Constitution.

Section 13. It shall be the duty of any member or subordinate body who feels aggrieved by any action, decision, or penalty imposed upon him or it, to exhaust his or its remedy and all appeals therefrom under the laws of this International Union prior to appealing to a civil court or governmental agency for redress. . . .

13 558 F.2d at 1279-80.
14 See text accompanying note 76 infra.
unanimously that the defense of failure to exhaust intraunion remedies is not available to the employer.\textsuperscript{15}

I. Federal Suits Under Collective Bargaining Agreements

Approximately 22.5 million workers are represented by unions and work under terms of collective bargaining agreements.\textsuperscript{16} These agreements were termed in \textit{Steelworkers v. Warrior \& Gulf Co.}\textsuperscript{17} an attempt to erect an entire system of industrial self-government.\textsuperscript{18} They cover the entire employment relationship and define the terms of workers' individual employment contracts, including certain employee rights regarding employee-employer disputes.\textsuperscript{19} Within this system of "industrial self-government" the union is designated as the exclusive bargaining representative of the employee in enforcing and protecting these rights. This authority to represent all members of the union is created under the Labor-Management Relations Act\textsuperscript{20} and includes a statutory duty to fairly represent all employees in collective bargaining.\textsuperscript{21}

A. Employee Suits Under § 301(a)

The Labor Management Relations Act of 1947 (Taft-Hartley Act)\textsuperscript{22} was designed to reduce industrial disputes and place employees in an equal position with unions in regard to bargaining and labor relations procedures.\textsuperscript{23} Section 301(a) of the act confers jurisdiction on the federal courts in cases involving contract violations: "Suits for violations of contracts between an employer and a labor organization representing employees may be brought in any district court of the United States without respect to the amount in controversy or regard to citizenship."\textsuperscript{24} The individual employee has the right to sue under § 301(a) on collective bargaining agreements negotiated by his union and employer on the rationale that he is a third-party beneficiary.\textsuperscript{25} Moreover, when an employee claims that the employer has violated the collective bargaining agreement and

\begin{itemize}
  \item \textsuperscript{15} See \textsuperscript{note 59} infra.
  \item \textsuperscript{16} U.S. \textit{NEWS} \& \textit{WORLD REPORT}, May 1, 1978, at 57.
  \item \textsuperscript{17} 363 U.S. 574 (1960).
  \item \textsuperscript{18} \textit{Id.} at 580.
  \item \textsuperscript{19} Marchione, \textit{A Case for Individual Rights Under Collective Agreements}, 28 \textit{LAB. L. J.} 738 (1976).
  \item \textsuperscript{20} The Labor Management Relations (Taft-Hartley) Act § 9(a), 29 U.S.C. § 159 (a) (1970), states in pertinent part that "representatives designated or selected for the purpose of collective bargaining by the majority of the employees in a unit appropriate for such purpose, shall be the exclusive representative of all the employees in such unit for the purpose of collective bargaining."
  \item \textsuperscript{21} \textit{Vaca v. Sipes}, 386 U.S. 171 (1967).
  \item \textsuperscript{23} \textit{Id.} at 580.
  \item \textsuperscript{24} \textit{Marchione, A Case for Individual Rights Under Collective Agreements}, 28 \textit{LAB. L. J.} 738 (1976).
  \item \textsuperscript{25} \textit{MacKay v. Loew's, Inc.}, 182 F.2d 170 (9th Cir. 1950). See also Annot., 18 A.L.R. 2d 348 (1951); 48 Am. \textit{JUR. 2d Labor} § 1298 (1970).
\end{itemize}
that his union has failed to represent him properly in the grievance procedure, the employee under § 301(a) may: 1) sue the employer for wrongful discharge; 2) sue his union for breach of the duty of fair representation; or 3) sue both of them jointly.

Within the context of Harrison, it is crucial to realize that although an employer may act in good faith in connection with the discipline of the employee and may follow the statutory bargaining procedure, he is not protected from an employee suit when the union has breached its duty of fair representation. As stated in Vaca v. Sipes,

It may be true that the employer in such a situation may have done nothing to prevent exhaustion of the exclusive contractual remedies to which he agreed in the collective bargaining agreement. But the employer has committed a wrongful discharge in breach of that agreement, a breach which could be remedied through the grievance process to the employee-plaintiff's benefit were it not for the union's breach of its statutory duty of fair representation to the employee.

Furthermore, in such cases in which the union's conduct has been found to constitute an unfair labor practice, the National Labor Relations Board has proclaimed the employer's conduct an unfair labor practice and has held the union and the employer jointly and severally liable for any back pay.

B. Exhaustion of Contractual Remedies Defense

1. Employee Suits Against the Employer

Generally, an employee who sues his employer for wrongful discharge under § 301(a) is bound by the terms of the collective bargaining agreement and, if the agreement establishes grievance and arbitration procedures as the exclusive means of enforcing contract rights, the employee must attempt to exhaust those procedures before he brings suit.

Collective bargaining contract remedies are separate and distinguishable from intraunion remedies. The former creates a duty upon the employer, union and employee to abide by the terms and remedies provided in the collective

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26 The union breaches the duty of fair representation when its conduct toward a member of the collective bargaining unit is arbitrary, discriminatory, or in bad faith. For a survey of the principles involved, see Vaca v. Sipes, 386 U.S. 171, 190 (1967); Jacobs, Fair Representation and Binding Arbitration, 28 LAB. L. J. 369 (1977); Note, The Union’s Duty of Fair Representation—Fact or Fiction, 60 MARQ. L. REV. 1116 (1977); Note, Individual Employee’s Rights Under the Collective Agreement: What Constitutes Fair Representation, 126 U. PA. L. REV. 251 (1977).
29 Id. at 185.
30 A union’s breach of the duty of fair representation has been held to constitute an unfair labor practice. See, e.g., Truck Drivers and Helpers, Local 568 v. NLRB, 379 F.2d 137 (D.C. Cir. 1967). See also 48 AM. JUR. 2d Labor § 771 (1970).
31 Vaca v. Sipes, 386 U.S. at 197 n.18.
32 Id. at 184.
bargaining agreement. The latter creates an obligation between the employee and the union only and is created by membership in the union. Intraunion remedies are a method for the resolution of employee-union conflicts and the employer is not a party to this contract.

The duty of the employee to exhaust contract remedies is grounded in congressional policy that resolution by a method agreed upon by the parties is the most desirable method for the settlement of grievance disputes. Allowing the employee to bypass available grievance procedures in favor of a lawsuit would deprive employer and union of the ability to establish a uniform and exclusive method of orderly settlement of employee grievances. In accordance with this policy, the Supreme Court has held that suits by employees who have bypassed contract grievance procedures must be dismissed by the district court.

2. Employee Suits Against the Union

A similar policy is found regarding suits by the employee against his union. It is well established that when there is no question as to the adequacy and mandatory nature of intraunion remedies, an exhaustion of those remedies is an indispensable prerequisite to the institution of an action against the union. Union membership establishes a contractual relationship between the union and employee vis-a-vis the union constitution. This relationship imposes an obligation upon the employee to exhaust intraunion remedies.

A general national policy exists against judicial interference in the internal affairs of a union until it has had at least some opportunity to resolve disputes concerning its own internal affairs. This federal policy of "staying the hand of judicial interference," and requiring exhaustion of internal remedies is based on the desire that such procedures, with the aid of persons experienced at resolving member-union conflicts, will result in speedy resolution of disputes without the delay inherent in judicial proceedings.

II. Relaxation of the Exhaustion of Contractual Remedies Doctrine

The Supreme Court has recently redefined the balance between national labor policy and individual employee rights within the scope of § 301(a) actions. In Vaca v. Sipes, the Supreme Court reiterated the basic premise that an employee must attempt to exhaust exclusive grievance and arbitration procedures.

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33 See text accompanying note 19 supra.
34 Labor Management Relations (Taft-Hartley) Act § 203(d), 29 U.S.C. § 173(d) (1970), states in pertinent part that "[f]inal adjustments by a method agreed upon by the parties is declared to be the desirable method for settlement of grievance disputes arising over the application or interpretation of an existing collective bargaining agreement. . . ."
36 Id.
37 See note 12 supra.
38 Newgent v. Modine Manufacturing Company, 495 F.2d 919, 927 (7th Cir. 1974).
39 Neal v. System Board of Adjustments (Missouri Pacific R.), 346 F.2d 722, 726 (8th Cir. 1965).
40 Ruzicka v. General Motors Corporation, 523 F.2d 306, 311 (6th Cir. 1975).
41 Id. at 312.
42 386 U.S. 171 (1967).
established by the collective bargaining agreement when the action against the employer is based upon a breach of that agreement. The Court acknowledged, however, that since these contractual remedies are fashioned and often controlled by the employer and union, they may prove, under certain circumstances, unsatisfactory or unworkable for the individual employee. The Court recognized that an employee should not be limited to the exclusive remedial procedures established by the contract when the conduct of the employer amounts to a repudiation of those contractual procedures. 43

Such a situation arises when the employee is prevented from exhausting his contractual remedies by the union's wrongful refusal to process his grievance. 44 Under these circumstances the employer is estopped from relying on the unexhausted contract procedures as a defense to the employee's § 301(a) action. 45 In effect, the wrongfully discharged employee can bring a § 301(a) action against the employer in the face of a defense based on the failure to exhaust contractual remedies provided the employee can prove a breach in the union's duty of fair representation. 46 The Court declared,

[W]e cannot believe that Congress, in conferring upon employers and unions the power to establish exclusive grievance procedures intended to confer upon unions such unlimited discretion to deprive injured employees of all remedies for breach of contract. Nor do we think that Congress intended to shield employers from the natural consequences of their breaches of their bargaining agreements in the enforcement of such agreements. 47

In Hines v. Anchor Motor Freight, Inc., 48 the Supreme Court expanded the Vaca rationale by holding that a "union's breach of duty relieves the employee of an expressed or implied requirement that disputes be settled through contractual procedures and, if it seriously undermines the integrity of the arbitral process, also removes the bar of finality provision of the contract." 49 The Court read § 301(a) as reflecting the interest of Congress in promoting "a higher degree of responsibility" among the parties to collective bargaining agreements to the aggrieved employee.

Vaca and Hines reflect judicial recognition of the necessity of balancing the dual interest presented under § 301(a) actions: 1) the strong national policy in settling labor disputes through the collective bargaining agreement, and 2) the need to afford the aggrieved employee a final resolution of his claim while protecting his rights. 50

As a practical matter, Vaca and Hines provide the employee with easier access to a federal forum by relieving him of the duty to exhaust collective bargaining remedies before bringing suit. In addition, they remove the finality

43 Id. at 185.
44 Id.
45 Id.
46 Id. at 186.
47 Id.
49 Id. at 567.
50 See 348 F.2d at 726. See also Note, Finality and Fair Representation: Grievance Arbitration Is Not Final if the Union Has Breached Its Duty of Fair Representation, 34 WASH. & LEE L. REV. 309 (1977).
of collective bargaining grievance resolutions, thereby resulting in the possibility
that the employer will be required to relitigate, in a federal court, the issue of the
wrongful discharge. The fact that the employer has acted in good faith in the
grievance procedure will not shield him from an action based on the union’s
unfair representation.

As a result of Vaca and Hines, an employer who has received a favorable
decision under the collective bargaining grievance procedures and who is faced
with an employee § 301(a) suit based on union misconduct cannot safely rely
on the finality of the decision arrived at under the grievance procedure, nor can
he rely on the exhaustion of contract remedies defense. Under these circum-
stances, employers sought to develop an alternate defense and, as a result, turned
to the intraunion exhaustion doctrine. This defense suggests that an employee
should not be allowed to sue an employer on a claim based on the breach of the
collective bargaining agreement when he has not completed the search for a
remedy within his own union.

Traditionally, however, the defense based on the employee’s failure to
exhaust intraunion remedies has, under the authority of Federal Courts of Ap-
peal, been available only to the union. The Seventh Circuit, therefore, found
itself attempting to shape the scope of § 301(a) actions by favoring the defense,
even absent authority sustaining an employer’s right to the defense.

III. Exhaustion of Intraunion Remedies as an Employer’s Defense

Both Federal District Courts and Circuit Courts of Appeal have had oc-
casion to address this defense. The conclusions reached by these courts, however,
have been conflicting.

A. Courts of Appeal

Circuit Courts of Appeal which have addressed the intraunion exhaustion
issue have held or stated that the defense is not available to the employer.51

Brady v. Transworld Airlines, Inc.,54 is one of the earliest cases to define the

51 Orphan v. Furnco Construction Corporation, 466 F.2d 795 (7th Cir. 1972).
52 See note 53 infra.
55 Id., at 102. The dispute referred to is the employee’s action against the employer for wrongful discharge. The employee was discharged for his alleged failure to pay back union dues.
In *Peterson v. Rath Packing Company*, a group of women brought a § 301(a) action against their employer for breach of the collective bargaining agreement and against their union for failure to represent them fairly. The employer asserted the employees' failure to exhaust intraunion remedies as a defense. The Eighth Circuit, in rejecting this defense, reasoned that "[t]he company cannot urge that the plaintiffs should have further appealed the grievance to the rank and file membership since there is no such requirement within the collective bargaining agreement. The question of exhaustion of internal union procedures is the union's concern, not the company's."  

The decisions denying the employer this defense are based on a recognition of the basic difference between contract and union remedies. The intraunion exhaustion requirement is predicated upon a contract between the employee and the union, and "[t]he employer cannot avail himself of the union's contractual defense." Moreover, the policy of avoiding judicial interference with the internal affairs of a union cannot be asserted by the employer since the policy protects only the interest of the union. It is upon these premises that courts of appeal have held or stated unanimously that the defense is not available to the employer. As stated by the D.C. Circuit in *Winter v. Local Union No 639, ETC.*, no court of appeals has held that the defense is available to the employer; the only court of appeals to suggest otherwise was the 7th Circuit in *Orphan v. Furnco*. Even under the *Orphan* dictum, there is no circuit court authority for making the defense of failure to exhaust union remedies available to the employer. . . .

**B. District Courts**

Even though an employer's use of the intraunion exhaustion defense has not found favor in the courts of appeal, several federal district courts have made the defense available to the employer.  

The most cogent rationale for allowing the defense is found in *Brookins v. Chrysler Corp.* This decision intimates that the availability of the exhaustion defense to the employer derives collaterally from *Vaca* and *Hines*. The *Brookins* court reasoned that requiring exhaustion might reveal the union's good faith

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56 461 F.2d 312 (8th Cir. 1972).
57 Id. at 315 (emphasis added). Under *Hines*, the employer could not avail himself of the defense even if intraunion exhaustion was required under the collective bargaining contract. The union's breach of duty relieved the employee of any requirement that disputes be settled through contractual procedures.
58 569 F.2d at 150.
59 See note 53 *supra*.
60 569 F.2d 146 (D.C. Cir. 1977).
61 Id. at 150.
64 Recall that these Supreme Court decisions hold that the employer cannot safely rely on the outcome of collective bargaining grievance procedures when the union has breached its duty of fair representation during the grievance process. See text accompanying note 50 *supra*. 
and thus render the contract action against the employer nugatory. The court stated:

By exhausting his internal remedies the employee may be able to eliminate the very wrong of which he complains, not merely obtain a remedy in another forum. If the union's wrongful act were reversed . . . the employee would no longer have a cause of action for breach of duty of fair representation and consequently would have no right under *Vaca* to sue his employer for breach of contract.

The court further indicated that this conclusion was consistent with national labor policy favoring arbitration.

In *Fleming v. Chrysler Corp.*, the district court adopted the *Brookins* rationale and concluded that requiring exhaustion of intraunion remedies would give the union a chance to rectify any alleged wrong and thereby prevent any breach of its duty of fair representation.

An inference to be drawn from these decisions is that the district courts were looking to promote the congressional policy of encouraging disputes to be settled through the grievance machinery to which the parties had agreed in the collective bargaining contract. It is primarily upon the *Brookins* rationale, augmented with an interest to further national labor policy, that the federal district courts have justified the employer's use of the defense.

**IV. Harrison on the Intraunion Exhaustion Defense**

The Seventh Circuit in *Harrison* drew from its earlier decision in *Orphan v. Furnco Construction Corp.*, a case in which an employee had brought a § 301(a) action against his employer for violation of a collective bargaining agreement. The *Orphan* court suggested, without deciding, that permitting the employer to raise the defense would facilitate the national labor policy favoring nonjudicial resolution of grievance disputes. The court, however, declined to extend the defense to the employer because it found that an intraunion appeal could not have resulted in any practicable remedy for the employee.

Using the foundation established in *Orphan*, the Seventh Circuit concluded in *Harrison* that a rule requiring intraunion exhaustion would directly and substantially benefit the employer by enabling him to rely on the integrity of the grievance procedure in all cases in which it has not been irretrievably spoiled by the union's unfair representation. The Seventh Circuit further established that the employee owes an obligation to the employer to exhaust available methods of reviving a stalled grievance procedure before abandoning that procedure and resorting to the courts for relief. The *Harrison* court found this obligation to be implied under a collective bargaining agreement which reposes in the union

65 381 F. Supp. at 568-69.
66 Id.
68 See note 62 *supra*.
69 466 F.2d 795 (7th Cir. 1972).
70 558 F.2d at 1278.
71 Id.
exclusive authority to represent the employee in contractual claims against the employer and which provides grievance machinery as the exclusive method of resolving those claims.\(^2\)

The court stated that no valid reason appeared for relieving the employee from the contractual requirement that he rely on the union for representation and the grievance procedure for relief, so long as the procedure remained viable and fair representation could be obtained.\(^3\)

_Harrison_ indicates that to successfully raise the defense, the employer would have to establish that: 1) an intraunion appeal could result in reversal of the union's refusal to press the grievance; 2) the grievance could be reinstated in accordance with the provisions of the collective bargaining agreement; and possibly, 3) resort to the intraunion appellate procedures would not be futile.\(^4\) If an employer can establish these elements, the district court would be required to dismiss the action.

**A. The Propriety of the Seventh Circuit's Discussion of the Defense**

In _Harrison_, after stating that an employer could use the intraunion defense under certain circumstances, the Seventh Circuit held the defense unavailable to Chrysler because an intraunion appeal could not have satisfied Harrison's claim for back pay.

In this regard, _Harrison_ is similar to _Orphan_. The latter case, however, refused to extend the defense to employers since the facts were not proper for its application. Yet in _Harrison_ the court expressly concluded that employers could use the defense notwithstanding the same lack of appropriate facts present in _Orphan_. Thus, the grant of the exhaustion defense appears to have been unnecessary to a resolution of the case. As stated by Chief Judge Fairchild in his concurring opinion,

> [b]ecause it is clear that the facts of this case do not fit the situation suggested by the employer's argument discussed in _Orphan_, . . . and really _dictum_ there as here, I prefer not to speculate as to whether there are any "limited circumstances" under which an employer might predicate a defense on the employee's failure to exhaust intraunion remedies.\(^5\)

The import of the _Harrison_ decision is found in its "dictum" recognizing the defense. It is essential, therefore, to isolate the reasons behind the court's discussion of the intraunion exhaustion issue.

The Seventh Circuit was possibly using _Harrison_ to further their interpretation of national labor policy that favors the submission of grievances to arbitration

\(^{72}\) *Id.*

\(^{73}\) *Id.* at 1278-79.

\(^{74}\) *Id.* at 1279. Although the Seventh Circuit does not make the third factor explicitly an element of the defense, the proposition that an employee is under no duty to exhaust intraunion remedies when it would be futile to do so is generally accepted by courts that have addressed the issue. See, e.g., Dorn v. Meyers Parking System, 395 F. Supp. 779 (E.D. Pa. 1975). See also 48 Am. Jur. 2d Labor § 334 (1970).

\(^{75}\) 558 F.2d at 1280 (emphasis added).
instead of the courts. The court stated that, "under certain circumstances an employee’s appeal within the union, after a union official’s bad faith refusal to push his grievance, might place the grievance procedure back on its proper course." Apparently the court was recognizing that it may be inequitable in some situations to allow an employee to sue his employer based on the union’s breach of its duty of fair representation when the employer has complied in good faith with all bargaining procedures.

Another possible explanation for the Seventh Circuit’s action may have been its concern with the recent proliferation of labor dispute cases in the federal courts. Many of the disputes that were once settled by arbitration are beginning to appear at an increasing rate on federal court dockets. This proliferation has given rise to understandable concern since it directly conflicts with the policy favoring nonjudicial disposition of grievance disputes.

B. The Implied Obligation Rationale

The Seventh Circuit rejected the rationale of district courts which have allowed the defense and adopted instead an “implied obligation” approach. The legal grounds upon which this implied obligation is based are, however, rather unclear. The duty to exhaust intraunion remedies is grounded upon a contractual relationship between the employee and his union. The great weight of authority recognizes that the employer, not being a party to the contract, has no standing to raise the defense. Yet the Harrison court found an implied obligation owed by the employee to the employer to exhaust available methods of reviving a stalled grievance procedure before abandoning that procedure and resorting to the courts for relief.

The “implied obligation,” created under the Seventh Circuit rationale by the collective bargaining contract, must be based upon the union contract with its employees. The court does not reveal clearly how this obligation, which is owed by the employee to his union for the benefit of the union and the employee, can be collaterally incorporated into the collective bargaining agreement and thereby entitle the employer to enforce it. Even assuming that the obligation could arise under the collective bargaining agreement, the Supreme Court in Hines held that no requirement exists to settle grievances under the contractual machinery when there is unfair union representation.

The Supreme Court decisions of Vaca and Hines preclude the employers’ use of the exhaustion of contract remedies defense when there is unfair union representation. The contractual defense is disallowed even though the employee owes a direct duty to the employer under the collective bargaining agreement to exhaust contract remedies before resorting to the courts. The Seventh Circuit

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77 558 F.2d at 1278.
78 See Adomeit, supra note 77, at 627.
79 558 F.2d at 1277.
80 See text accompanying note 71 supra.
81 See note 53 supra.
82 558 F.2d at 1278.
appears to disregard the *Vaca* and *Hines* authority, however, by allowing the employer to rely on an indirect duty which arises under the union constitution and is incorporated by implication into the collective bargaining agreement. Yet, if the employer is unable to rely on the direct duty, he should not be able to rely on an indirect duty created under an "implied obligation" rationale. By allowing the intraunion exhaustion defense when the collective bargaining defense is not available, *Harrison* violates the spirit, if not the letter, of *Vaca* and *Hines.*

Another possible interpretation of this "implied obligation" to exhaust is that the employer is placed in the position of a third-party beneficiary. To assume, however, that the employer is the intended beneficiary of a contract between the employee and the union is questionable. At most, the employer would seem to be an incidental beneficiary who attains no right to the contract benefits.

The intent of the *Harrison* decision is to deter aggrieved employees from resorting to the courts when intraunion appellate procedures could result in reviving the grievance procedure. Its practical effect, however, will depend on subsequent decisions applying the "limited circumstances" under which the defense may be raised. These "limited circumstances" appear to be quite narrow.

The Seventh Circuit indicates that the defense may be used only for the limited purposes of regaining fair representation and reviving the grievance procedure. The implication of this limited grant is best understood when viewed within the context that collective bargaining agreements generally provide that a settlement at any stage is final. As stated by Chrysler,

> [w]hile the initial panel recognizes the employer's right to raise the defense of exhaustion, nevertheless, it renders such defense almost useless by limiting it to situations where a stalled grievance procedure can be revived. The problem with the limited rule enunciated by the initial panel is that almost uniformly collective bargaining agreements provide that a settlement at any stage is final or that a grievance not processed from one step to the next within certain time limits is barred. Therefore, as a practical matter in almost every case in which an employee brings suit for breach of the collective bargaining agreement, it is already too late to revive or institute the grievance procedure unless the employer voluntarily waives his right to rely on the time limits barring further processing or on the final and binding nature of the settlement.

The *Harrison* court, in commenting on this very problem, stated "[t]he suggestion . . . that the union could have requested Chrysler to reopen the grievance proceeding . . . is patently frivolous. There is no basis for assuming that Chrysler willingly would have exposed itself to the very liability that it resists in this action." The Seventh Circuit, therefore, apparently recognized the limitation

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84 *See generally* Restatement of Contracts §§ 133, 147 (1932); Restatement (Second) of Contracts § 133 (1973).
85 558 F.2d at 1279.
86 Appellee's Brief for Rehearing at 8.
87 558 F.2d at 1279.
of its rationale and yet failed to define its scope or to provide guidelines for its implementation in future cases.

As a consequence of so limited and vague a rule, the employer is confronted with the choice of abandoning the defense or voluntarily resubmitting itself to the grievance machinery. In the final analysis, therefore, it seems unlikely that the Seventh Circuit's "implied obligation" theory will be followed by other circuits faced with the intraunion exhaustion issue. This conclusion results not only because the theory finds little support under established case law, but also because it is simply too limited to provide an effective means of promoting the national labor policy in favor of arbitration.

C. Alternatives

The district court's rationale finds stronger support under case law with respect to its use of *Vaca* in formulating a general grant of the defense. The proposition that there is no breach of the duty of fair representation until there is intraunion exhaustion, however, is flawed for several reasons. First, *Vaca* held that an employee must plead and prove unfair representation in order to sue the employer. The Court further held that this was established when the union's conduct was found to be arbitrary, discriminatory, or in bad faith. The Court did not hold, nor can it be inferred, that intraunion exhaustion was an element of proving bad faith. In fact, exhaustion of internal union remedies is not an element of the cause of action for breach of the duty of fair representation. Rather, it is a requirement based on strong federal policies favoring the quick resolution of such disputes without judicial interference. Second, the fictitious assertion that a wrong has not been committed until intraunion procedures are exhausted would result as a practical matter in allowing an injustice to go without a remedy.

*Dorn v. Meyers Parking System* rejects the district courts' rationale that the existence of an intraunion appellate procedure prevents a cognizable breach of the union's fair representation duty from occurring prior to the exhaustion of the appellate procedures. The *Dorn* court states that "that holding is analogous to the principle that where state officials violate state law by conduct also prohibited by the Federal Constitution if a state remedy exists, no unconstitutional state action has yet occurred. This holding has been firmly repudiated."

In applying national labor policy to § 301(a) actions, there must be a recognition that such policy also includes a strong interest in protecting individual employee rights as well as a desire to submit grievances to arbitration rather than

89 The suit against the employer would be dismissed because the employee failed to exhaust his internal remedies; yet since union constitutions almost uniformly provide that challenges to union actions not processed within certain time limits are barred, the employee would be effectively foreclosed from a hearing on his grievance. Cf., 569 F.2d at 153 n.1 (MacKinnon, J., dissenting) (exhaustion cannot be absolute prerequisite to suit).
91 Id. at 785 n.6.
For this reason, one possible solution to the basic controversy might be found in the nature of the claims asserted by the employee and employer.

The employee is basically aggrieved because his union has wrongfully refused to take his grievance to arbitration. The employer desires to resolve disputes through the arbitration procedures established under the collective bargaining agreement. Under these circumstances, an order by the court compelling arbitration, while retaining jurisdiction, would seem to provide the best remedy to the various interests asserted. The Vaca court indicated that this was a possible solution to the problem.

It is true that the employee’s action is based on the employer’s alleged breach of contract plus the union’s alleged wrongful failure to afford him his contractual remedy of arbitration. For this reason, an order compelling arbitration should be viewed as one of the available remedies when a breach of the union’s duty is proved.

By the use of this procedure, the grievance could be settled within the established collective bargaining machinery, considerable time and expense could be saved for both the employee and employer, and the greater expertise arbitrators possess in labor dispute cases could more easily resolve the controversy. Moreover, such a solution would take the interests of both the employee and employer into account. The employee is afforded a potentially speedier remedy and the employer is able to rely on the collective bargaining machinery upon which he and the union had bargained. Finally, it provides a resolution which is clearly in line with national labor policy.

V. Conclusion

The Seventh Circuit’s “implied obligation” to exhaust intrarunion remedies appears to be an attempt to establish, without precedent, a new principle of law in § 301(a) employee-employer disputes. Although it is evident that the Seventh Circuit’s primary concern in Harrison was facilitating the national labor policy favoring the resolution of labor disputes within the collective bargaining machinery, the limited scope and uncertainty of the decision will limit its practical impact on this goal. As a result, it seems unlikely that the “implied obligation” approach, as formulated by the Seventh Circuit, will find favor in the additional Federal Courts of Appeal.

92 See Marchione, supra note 19, at 740.
93 See, e.g., Ruzicka v. General Motors Corp., 523 F.2d 306, 315 (6th Cir. 1975); Marchione, supra note 19 at 745-46.
94 366 U.S. at 196.
95 It should be recognized that a rule compelling arbitration has its limitations. First, if the collective bargaining agreement does not provide for arbitration the rule may not be applicable. Second, compelled arbitration would serve no useful purpose if the circumstances of the employee-employer dispute have reached a level where arbitration could not provide a viable remedy to either party. For these reasons, a rule allowing for compelled arbitration would be best left to the trial court’s discretion.
A preferable approach to the problem is found in a procedure which allows the district court to compel arbitration, while retaining jurisdiction, until the controversy is settled. Beyond providing a method for resolving labor disputes within the collective bargaining machinery, an order compelling arbitration benefits both the employee and employer by allowing them to rely on the expertise possessed by arbitrators in these types of cases. Since such a procedure can result in a speedier resolution of the grievance while taking into account the interest of both parties, it seems likely to promote labor policy to a greater extent than would a grant of the exhaustion defense to the employer.

Alcides I. Avila

Hooker Chemicals & Plastics Corp. v. National Labor Relations Board*

I. Introduction

When considering lockouts or strikes as a means of introducing economic pressure during collective bargaining, special attention must be given to the conditions on collective bargaining imposed by Section 8(d) of the National Labor Relations Act (NLRA) of 1947.1 In addition to the general duty to bargain in good faith,2 the statute requires that the initiating party, the party desiring to modify the contract, must notify the opposing party of the desired contract change sixty days before the expiration of the current contract.3 Section 8(d) further requires that the initiating party give notice to federal and state mediation services thirty days after the first notice to the opposing party.4 Nonobservance of

* 573 F.2d 965 (7th Cir. 1978).
1 29 U.S.C. § 158(d) (1970) [hereinafter referred to as the Act].
2 Section 8(d) provides:
   (d) For the purposes of this section, to bargain collectively is the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment, or the negotiation of an agreement, or any question arising thereunder, and the execution of a written contract incorporating any agreement reached if requested by either party, but such obligation does not compel either party to agree to a proposal or require the making of a concession:
   Id.
3 Sections 8(d)(1) and (4) provide:
   Provided, That where there is in effect a collective-bargaining contract covering employees in an industry affecting commerce, the duty to bargain collectively shall also mean that no party to such contract shall terminate or modify such contract, unless the party desiring such termination or modification—
   (1) serves written notice upon the other party to the contract of the proposed termination or modification sixty days prior to the expiration date thereof, or in the event such contract contains no expiration date, sixty days prior to the time it is proposed to make such termination or modification—
   (4) continues in full force and effect, without resorting to strike or lock-out, all the terms and conditions of the existing contract for a period of sixty days after such notice is given or until the expiration date of such contract, whichever occurs later.
   The sixty-day period established in both § 8(d)(1) and § 8(d)(4) is commonly referred to as the sixty-day “cooling off” period. In NLRB v. Lion Oil Co., 352 U.S. 282 (1957), the Supreme Court clarified the definition of “expiration date” mentioned in § 8(d)(4) to include a date for modification of the contract as well as a termination date.
   If the initiating party serves notice less than sixty days before the expiration date, the full sixty days must still elapse. Until then, neither a strike nor a lockout can occur. [1978] 3 LABOR L. REP. (CCH) ¶ 5240. Untimely sixty-day notice, however, is not the subject of this comment.
4 Section 8(d)(3) provides:
   that no party to such contract shall terminate or modify such contract, unless the party desiring such termination or modification—
   (3) notifies the Federal Mediation and Conciliation Service within thirty days after such notice of the existence of a dispute, and simultaneously therewith notifies any State or Territorial agency established to mediate and conciliate
these requirements may render either a strike or a lockout unlawful.

Although charged with abiding by the statute, parties have, on occasion, failed to comply with its provisions and then afterwards attempted to justify their actions. As a result, ambiguities have arisen concerning the effect of giving untimely notice.\(^5\)

In *Hooker Chemicals & Plastics Corp. v. National Labor Relations Board*, the Seventh Circuit was confronted by a novel variation of noncompliance with the statute. The initiating party in *Hooker Chemicals*, the union, allegedly exploited its failure to give timely notice to the mediation services. The union sought to prevent the noninitiating party from imposing economic sanction at the expiration of the contract by forcing it to withhold the impositions of such sanctions until the end of the thirty-day period for mediation.

The Seventh Circuit concluded in *Hooker Chemicals* that, pursuant to Section 8(d)(3), the noninitiating party can bring economic pressure on the initiating party at the end of the contract or of the sixty-day "cooling off" period\(^6\) despite untimely notice by the initiating party to the mediation services. This comment will interpret the manner in which Section 8(d)(3) treats this unique but potentially recurring situation in collective bargaining. Such an analysis of Section 8(d)(3) demonstrates that the Seventh Circuit's interpretation of the statute is in harmony with congressional intent in rendering a just resolution for the parties involved.

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\(^5\) In *Mastro Plastics Corp. v. NLRB*, 350 U.S. 270 (1956), the Supreme Court held that a strike during the sixty-day "cooling off" period was lawful because it was held to protest the employer's unfair labor practice. *Procter & Gamble Independent Union of Port Ivory v. Procter & Gamble Mfg. Co.*, 312 F.2d 181 (2d Cir. 1962), held that untimely notice to the mediation services did not extend the period of the contract past its expiration date. In *United Elec., Radio, & Mach. Workers Local 1113 v. NLRB*, 223 F.2d 338 (D.C. Cir. 1955), a strike called within one hour of giving notice to the employer and with no notice given to the mediation services was held unlawful and thereby allowed the employer to lock out. Local 3, *United Packinghouse Workers of America v. NLRB*, 210 F.2d 325 (8th Cir. 1954), held that a strike which occurred several months before the end of the contract was unlawful. *International Union of Operating Eng'rs v. Dahlem Constr.*, 143 F.2d 470 (6th Cir. 1951), held that when untimely § 8(d) notice was given, the fact that thirty days had elapsed after notice and before the strike could not provide a defense in a breach of contract action. *Illinois State Employers v. NLRB*, 395 F. Supp. 1011 (1975), dealt with a situation similar to *Hooker Chemicals*. The union delayed filing notice to the mediation services and went on strike before the end of the thirty-day period. In *re Eisen*, 77 N.Y.S.2d 676 (1948), held that failure to give timely § 8(d) notice does not prolong the length of a contract. *Kaynard v. Bagel Bakers Council [1968] 37 Lab. Cas.* \(\$12,490\), presented a situation in which the employer and not the union was the initiating party and failed to give § 8(d)(3) notice.

\(^6\) According to § 8(d)(4), economic weapons can be used only after the latter of the two time periods have elapsed. *See* note 3 *supra*. 

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...disputes within the State or Territory where the dispute occurred, provided no agreement has been reached by that time. ...
II. Statement of the Case

Hooker Chemicals and the International Chemicals Workers Union operated under collective bargaining agreements, one of which was to expire on April 15, 1975. On January 27, 1975, the union gave notice of its desire to renegotiate those contracts and thereby initiated the sixty-day “cooling off” period. Despite intense bargaining, the parties were unable to reach an agreement by the middle of April. The union gave notice to the mediation services pursuant to Section 8(d)(3) on April 9. On April 15, the union informed Hooker Chemicals that it had rejected the management’s last offer. Although the union advised Hooker Chemicals that its members were willing to continue work, the management locked out its employees upon expiration of the current contract.\(^7\)

The noninitiating party, therefore, imposed a lockout after the end of both the contract and the sixty-day “cooling off” period but before the end of the thirty-day period for mediation. The union sought relief from the lockout by charging Hooker Chemicals with unfair labor practices before the National Labor Relations Board (NLRB). The NLRB held that by locking out its employees before the end of the thirty-day period for mediation, Hooker Chemicals had violated its duty to bargain collectively under Section 8(d) of the Act and thus had committed an unfair labor practice.\(^8\) The Board balanced the legitimate interests of the noninitiating party against the potential benefits of mandatory mediation and ruled in favor of mediation. The Board believed that such a result would best effect the congressional intent of eliminating substantial obstruction to the free flow of commerce by encouraging collective bargaining.

In light of Section 8(d)(3) and National Labor Relations Board v. Peoria Chapter of Painting & Decorating Contractors,\(^9\) Hooker Chemicals petitioned for review in the Seventh Circuit. The court granted the petition and denied the NLRB’s cross-application for the enforcement of their prior order that the use of economic weapons by the noninitiating party before the end of the thirty-day period for mediation was an unfair labor practice.

III. Section 8(d)(3) and Its Initial Evolution

In passing the NLRA, Congress discussed extensively its underlying policies.\(^10\) The prevailing objective of the Act is to preserve the “normal flow of commerce” by avoiding industrial strife.\(^11\) By prescribing “the legitimate rights of employers and employees”\(^12\) and by prescribing procedures for the peaceful

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\(^7\) The lockout continued from April 15, 1973, to June 9, 1973, when the parties reached a new two-year agreement. *Id.* at 967.


\(^9\) 500 F.2d 54 (7th Cir. 1974).


\(^11\) *Id.*

\(^12\) *Id.*
resolution of labor disputes, the threat of industrial strife is minimized. Essential to this concept is the preservation of the employee’s right to organize collectively.13

In interpreting the Act, the Supreme Court recognized a dual purpose regarding collective organization, namely "to substitute collective bargaining for economic warfare and to protect the right of employees to engage in concerted activity for their own benefit."14 To accomplish the first goal, Congress imposed a sixty-day period, during the first thirty days of which the parties must attempt to resolve the dispute themselves. Absent success, the party who first raised the issue of modification has the responsibility15 of notifying the mediation services that assistance is needed to resolve the dispute.16 The NLRB and the courts, therefore, have held that notification is mandatory17 and that it is an "integral part of the congressional scheme to achieve a higher degree of stability in collective bargaining."18

The Act should not be interpreted, however, so as to prohibit the use of economic weapons. Section 8(d)(4) specifically permits strikes or lockouts19 after the expiration of the contract or the sixty-day "cooling off" period, whichever occurs later. Thus, the policy considerations in Hooker Chemicals are contrasting. The value of requiring a thirty-day period within which to mediate conflicts with the right of the noninitiating party to use economic pressure at the end of the "cooling off" period. If the initiating party had fulfilled its obligations to

13 Id.
14 Mastro Plastics Corp. v. NLRB, 350 U.S. at 284. The Court also warned against adopting an interpretation which “would produce incongruous results.” Id. at 286.
15 When the noninitiating party might be prevented from using its economic weapons because the initiating party has either failed to give notice or given untimely notice, it has been suggested that the noninitiating party could preserve its right to use economic pressure at the end of the sixty-day period by inquiring whether the initiating party had given notice, and if it had not, to give notice itself. The NLRB in both Peoria Contractors, 204 N.L.R.B. at 346, and Hooker Chemicals, 224 N.L.R.B. at 1556, proposed this solution. A comment on Peoria Contractors proposes that both parties carry the burden of notifying the mediation services. Comment, Labor Law—The Lockout Loophole in 29 U.S.C. § 158(d)(3), 24 EMORY L. J. 495, 507-10 (1975) [hereinafter cited as Lockout Loophole]. The congressional regulation requiring the noninitiating party to notify the mediation services is well reasoned. The District of Columbia Circuit in United Furniture Workers v. NLRB, 336 F.2d 738 (D.C. Cir.) cert. denied, 379 U.S. 838 (1964), noted that if the burden of notification is not squarely placed on one party, there is a high probability that the public interest in the emollient intervention of the mediation services will fall between the two stools of contending parties. . . . It is a peril which can be avoided by assigning a fixed and definite responsibility for notifying the public agencies. Congress has made that assignment and, not surprisingly, it is to the party who started the process. Id. at 741.
16 The Seventh Circuit in Hooker Chemicals noted, however, that such a proposal could place the noninitiating party in a dilemma. If it does not inquire to determine whether notification has been given, it risks being delayed in using its economic sanctions. If it does inquire, it risks cooling the negotiation. 573 F.2d at 970.
17 The beneficial effects of mandatory notification were quickly recognized after the passage of the Act. "In the days before the 30-day notice was required, strikes frequently occurred before the . . . service had any knowledge that there was a dispute. Mr. Chaing (First Director of the FMCS) believes that in many instances the early intervention of conciliators has prevented a strike."2 Joint Comm. on Labor-Management Relations, Final Report, S. Rep. No. 986, 80th Cong., 2d Sess. 15 (1948).
19 Retail Clerks Local 1179, 109 N.L.R.B. at 759; Peoria Contractors, 204 N.L.R.B. at 346. 20 29 U.S.C. § 158(d)(4) (1970). In American Ship Bldg. v. NLRB, 380 U.S. 300 (1965), the Supreme Court held that the employer may lock out "in support of a legitimate bargaining position," and a lockout, therefore, was not "inconsistent with the right to bargain collectively." Id. at 310.
file proper notice pursuant to Section 8(d)(3), the use of such economic pressure would not be questioned.

In addition to Hooker Chemicals, Peoria Contractors is the only case which has addressed the effect of untimely Section 8(d)(3) notice on the noninitiating party. Thus, the NLRB's treatment of this form of untimely notice in both Peoria Contractors and Hooker Chemicals merits further analysis.

IV. The Board's Position Requiring Mediation

A. Prior Board Decisions

The Board first addressed the issue of untimely Section 8(d)(3) notice in Retail Clerks International Association Local 1179.20 The union, which desired to modify the contract, served proper sixty-day notice, but never served notice to the mediation services. The union went on strike almost four months after giving the first notice. Although the Trial Examiner held that the union committed an unfair labor practice by not notifying the mediation services, he also ruled that the mediation provisions were ancillary. Thus, violation of the mediation provisions alone did not render the strike unlawful.21

The Board ruled, however, that striking without first giving notice to the mediation services constituted an unfair labor practice. The Board noted that the Trial Examiner's ruling would "[permit] the very act which constituted the Respondent Union's misconduct to go unremedied,"22 and that "[t]here is nothing to indicate that Congress regarded the mandatory requirement [of Section 8(d)(3)] as less significant than any other of the mandatory provisions."23 The NLRB further stated that the mediation services "enhance the probability of a peaceful settlement,"24 and that such services are "an integral part of the scheme evolved by Congress for achieving a higher degree of stability in collective bargaining."25 Accordingly, the Board held that "Section 8(d), by its plain language and intent, made it unlawful for the Respondent Union to strike . . . without first serving notice [upon the mediation services] of its dispute. . . ."26

The sanctity of the thirty-day period was reaffirmed in Local 219, Retail Clerks International Association.27 In Local 219, Retail Clerks, the union gave notice to the mediation services over two months after Section 8(d)(1) notice had been given and struck ten days afterwards. In adopting the Trial Examiner's holding that a thirty-day period must exist within which to mediate, the Board apparently adopted an argument made by the General Counsel to the NLRB that "the spirit of the law has been violated by not permitting thirty days since the [services of the] Mediation Service [were] available or could be obtained."28

21 Id. at 768.
22 Id. at 758.
23 Id.
24 Id.
25 Id. at 759.
26 Id.
28 Id. at 278. The Board apparently presented this argument to the court in Local 219, Retail Clerks Int'l Ass'n v. NLRB, 265 F.2d at 819.
In finding that the Union had committed an unfair labor practice by striking without giving notice to the mediation services, the Board observed in Fort Smith Chair Co. that it has also been concluded that, where late notices under Section 8(d)(3) to the Mediation and Conciliation Service are filed, the waiting period must be extended to include a full 30 days after the filing of such notices in order to give mediation its intended statutory period in which to work.

The NLRB supported this analysis by relying on two Supreme Court decisions, National Labor Relations Board v. Lion Oil Co. and Mastro Plastics Corp. v. National Labor Relations Board. The NLRB referred to the dual purposes of the Act as interpreted by the Supreme Court in Mastro Plastics: "to protect concerted activities and to substitute collective bargaining for economic warfare." Thus, the Board's interpretation in Fort Smith Chair Co. in favor of mediation seems to follow Supreme Court precedent. Accordingly, the NLRB contended that the second thirty days of the "cooling off" period are tolled pending notice by the initiating party.

The Board in its Hooker Chemicals decision recognized that a posture of "continuing the current agreement and maintaining the parties' bargaining position" is thereby attained until mediation can be attempted.

B. The Board's Examination of Congressional Intent

In the initial NLRB opinions in Peoria Contractors and Hooker Chemicals, the Board also attempted to justify its position by examining the congressional intent behind Section 8(d)(3). The Board reiterated that "the 30 days is an integral part of the congressional scheme for achieving a higher degree of stability in collective bargaining." From this postulate the Board deduced that Congress did not intend to waive the thirty-day period. The Board further noted that the mediation services are "important contributor[s] to the 'probability of a peaceful settlement of the dispute.'"

Given these premises and the prevailing purpose of the statute, as clarified by the Supreme Court, to "substitute collective bargaining for economic war-

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30 Id. at 519.
33 Id. at 284.
34 Hooker Chemicals, 224 N.L.R.B. at 1538. Both Local 219, Retail Clerks and Fort Smith Chair Co. were affirmed by the District of Columbia Court of Appeals. In Peoria Contractors and Hooker Chemicals, the Board emphasized these affirmations to justify their conclusions.
35 204 N.L.R.B. at 346. To further support this proposition, the Board before the Seventh Circuit cites Senator Taft's explanation of 8(d) to Congress: We have provided in the revision of the collective bargaining procedure, in connection with the mediation process, that before the end of any contract . . . either party who wishes to open the contract may give 60 days' notice in order to afford time for free collective bargaining, and then for the intervention of the Mediation Service.
36 224 N.L.R.B. at 1536-38.
fare," the Board declared that the period for mediation "must be preserved in spite of the potential abuse of the statutory scheme." The Board admitted that such a ruling could place a burden on the parties by delaying the imposition of economic sanctions but dismissed this argument as placing only "minimal additional burdens on the parties." The Board summarized its conclusion in the form of a balancing test. The value of increased stability as promoted by a definite period of mediation outweighs the conflicting interests of mandatory notice and the right of the noninitiating party to resort to economic pressure at the end of the contract. Finally the Board suggested that if the noninitiating party really desired to use its economic sanctions at the end of the contract, it could send notice to the mediation services itself.

In some instances, however, penalizing the noninitiating party for the unlawful action of the opposing party is inequitable and, as a result, a potential for abusing the statutory scheme exists by endorsing the Board's position. Furthermore, the Hooker Chemicals circumstances and the cases relied upon by the Board are factually distinguishable. As will be shown further on in this comment, a closer scrutiny of the legislative history and prior judicial interpretation of Section 8(d) (3) reveals that the Board's reliance on its prior decisions and perceived congressional intent is not accurate. These reasons support the Seventh Circuit's conclusion that the initiating party's untimely Section 8(d) (3) notice should not hinder the noninitiating party in imposing economic sanctions upon the expiration of the contract.

V. Endorsing the Hooker Chemicals Result

A. Factual Differences in Precedent

Hooker Chemicals and Peoria Contractors can be distinguished on their facts from each of the cases relied upon by the NLRB as authority for concluding that the thirty-day notice requirement is immutable. In Retail Clerks, Local 1179, Local 219, Retail Clerks, and Fort Smith Chair Co., the party which had the legislative obligation to give notice failed to do so and then flaunted this evasion by striking the employer. In Peoria Contractors and Hooker Chemicals, however, the noninitiating party, which had no obligation to provide notice, locked out its employees at the end of the congressionally mandated sixty-day "cooling off" period. A district court perceived this fundamental difference when it held:

The actual decisions are not necessarily in conflict, however, because they all hold that a party giving a 30-day notice cannot terminate the contract legally until the 30 days have expired. The Seventh Circuit takes the additional step of holding that a party which does not initiate the procedure by a 60-day notice is not bound by the 30-day notice....
B. Prior Judicial Interpretation

In addition to distinguishable factual circumstances in the named precedent, enforcement of the Board’s position would lead to results inconsistent with prior interpretation of the Act. Examination of the District of Columbia Circuit’s opinion in Local 219, Retail Clerks reveals that although that court may have agreed with the Board’s result, the court disagreed with the Board’s reasoning and actually rejected the Board’s position that there must be a thirty-day period for mediation. The court framed the Board’s proposition as follows: “the spirit of Section 8(d)(3) is violated only when the Mediation Service or state agency does not have thirty days to intervene in the bargaining process.” After acknowledging the Board’s theory, however, the court reflected: “Although this interpretation may be consonant with the purpose of the section, it does not seem to give sufficient weight to the requirement of Section 8(d)(3) that notice to the Mediation Services must be given within thirty days of the sixty-day notice under Section 8(d)(1).” The D.C. Circuit finally rejected the Board’s theory by adopting the “more logical” interpretation of 8(d)(3) as making two demands. First, Section 8(d)(3) requires the initiating party to give proper notice within thirty days of the sixty-day notice period. Second, the Section requires a thirty-day waiting period before commencing a strike or a lockout by the initiating party.

Hooker Chemicals extended the D.C. Circuit’s interpretation by ruling that the noninitiating party is not penalized for the other party’s violation and may at its own discretion use its arsenal of legitimate economic sanctions.

In addition to the development above, several cases imply that the application of the Board’s position could result in extending the effectiveness of an expired contract. In Procter and Gamble Independent Union of Port Ivory v. Procter and Gamble Manufacturing Co., the Second Circuit ruled that the “appellee’s failure to give timely notice to federal and state agencies did not have the effect of extending the period of the expired contract.” By analogy if untimely notice does not extend the contract, then also untimely notice should not create a thirty-day-notice period which adds to the sixty-day period and thereby extends the effectiveness of the contract.

C. Congressional Intent and History

The Board’s proposition of tolling the second half of the sixty-day “cooling off” period to guarantee mediation is not in full accord with the statutory

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44 265 F.2d at 819.
45 Id. (emphasis added).
46 Id. (emphasis added). This second requirement does not apply to the noninitiating party. In United Furniture Workers the District of Columbia Circuit did not modify this position formed in Local 219, Retail Clerks. Instead, it viewed the case as applying those principles to the specific facts of the case, namely when the union does not give Section 8(d)(3) notice at all. 336 F.2d at 741.
47 See text accompanying note 34 supra.
48 312 F.2d at 189. For earlier holdings of this same principle see In re Eisen, 77 N.Y.S.2d at 679; United States Gypsum Co. 90 N.L.R.B. 964, 968 (1950); Int’l Harvester Co., 77 N.L.R.B. 242, 243 (1948).
language, purpose and history. Section 8(d)(3) specifies the time at which notice to the mediation service should be given. "[T]he party desiring ... termination or modification [of the contract shall] notif[y] the Federal Mediation and Conciliation Service within thirty days after such notice of the existence of a dispute. . . ."\textsuperscript{49} The language of the Act itself declares that the time to give notice under Section 8(d)(3) is not variable in that the thirty-day notice must fall within the 60-day-notice framework of Section 8(d)(1).

Section 8(d)(4) requires that "the [initiating] party . . . [continue] in full force and effect, without resorting to strike or lockout, all the terms and conditions of the existing contract for a period of sixty days after such notice is given. . . ."\textsuperscript{50} After the conclusion of the sixty-day period, there is no statutory mandate that economic sanctions be withheld any longer.

In analyzing Section 8(d)(3), the Peoria Contractors court commented:

The Section is clearly phrased in terms of a unitary sixty-day waiting period keyed to the notice provision in § 8(d)(1). . . . There is no provision in § 8(d)(4) for a bifurcated waiting period of thirty days following each of the two statutory notices when the notice to the mediators is untimely given.\textsuperscript{51}

The use of the phrase \textit{within thirty days} in Section 8(d)(3) and the phrase \textit{a period of sixty days after such notice is given} in Section 8(d)(4) is unambiguous. The language clearly indicates a congressional intent to have one "cooling off" period of sixty days rather than a divided period consisting of two thirty-day segments.

To support its premise of the prevailing importance of mediation, the Board cited an address by Senator Taft, which said that Congress provided a time for free collective bargaining and then for the intervention of the mediation services.\textsuperscript{52} It also cited the report of the Watch Dog Committee,\textsuperscript{53} which said that before passage of the act the services often never knew of disputes and that early intervention has often prevented strikes.\textsuperscript{54} These comments strongly support the value of mediation. The Seventh Circuit concluded, however, that these quotes are not decisive. In analyzing the Taft speech, the Hooker Chemicals court found that "[t]he statement is equally susceptible to an interpretation that Congress required the 8(d)(1) 60-day notice within which time the mediation services could intervene assuming they were timely notified."\textsuperscript{55} In dealing with the report of the Watch Dog Committee the court concluded that the "report is even less persuasive support for the Board's position than Senator Taft's statement. The only clear indication of legislative intent is to place the burden of obligation on the initiating party."\textsuperscript{56}

The legislative history of the Act offers persuasive evidence that Congress did not intend that notice to the mediation services must precede a strike or a

\textsuperscript{51} 500 F.2d at 57-58.
\textsuperscript{52} See note 35 supra.
\textsuperscript{53} See note 16 supra.
\textsuperscript{54} Hooker Chemicals Corp. v. NLRB, 573 F.2d at 968.
\textsuperscript{55} Id.
\textsuperscript{56} Id.
lockout. Two versions of the bill were introduced in Congress. The Senate version had substantially the same provisions as does the present Act. The House bill was more specific in that it required notification to the mediation services as a condition before any lockout or strike could occur. The House bill provided:

(11) The terms "bargain collectively" and "Collective bargaining" as applied to any dispute between an employer and his employees or their representative, means compliance with the following minimum requirements: . . .

(vi) the following requirements shall be applicable as a condition of authorizing, conducting or participating in, any lockout or strike in connection with the dispute:

(a) The collective bargaining representative shall notify the Administration of its desire to have a strike vote conducted in connection with the dispute.

Congress could have endorsed these requirements had it desired to impose upon the parties the duty to notify mediators before any strike or lockout could occur. The differences in the two bills were resolved by congressional conference, however, which rejected the House version. As Senator Taft explained: "[I]n adopting the language of the Senate bill, the conferes rejected a definition of collective bargaining which was contained in the House bill. . . ." Arguably, in rejecting the House proposal, Congress also rejected the mandatory mediation service notice feature prior to the utilization of economic weapons.

D. Chief Judge Fairchild's Dissent

Chief Judge Fairchild dissented from the Hooker Chemicals decision. He would reverse the Peoria Contractors ruling and enforce the NLRB's order. Fairchild postulates that Congress must have assumed that the sixty-day period will always include a thirty-day period for mediation and that this assumption was so prevalent that Congress never considered the issue. Thus, endorsing the Board's theory will further congressional intent. Chief Judge Fairchild adds that because the national interest, not just the parties' interest, is served by mediation, the mediation services should be given every possible opportunity to conciliate.

The response of the majority in Hooker Chemicals was that if mediation is so essential, Congress would have corrected the Peoria Contractors decision by amendment. In the four years since the Seventh Circuit decided Peoria Contractors, however, no such congressional action has been taken.

58 1 LEGISLATIVE HISTORY OF THE LABOR MANAGEMENT RELATIONS ACT, 1947 at 8, 114-16 (1948).
59 Id. at 36-38 (emphasis added).
60 93 Cong. Rec. 6444 (1947).
61 The record of the congressional debates is not decisive on Judge Fairchild's proposition. The Congress did consider the effect of failing to give proper sixty-day notice. See note 35 supra. Moreover, Congress was not totally assuming and inadvertent about the drafting of § 8(d)(3). When the committee accidentally failed to allow for the state mediation services, Senator Ives of New York proposed an amendment to correct this deficiency. 93 Cong. Rec. 5081 (1947). Such consideration and care make such an assumption seem unlikely, but the fact that it was not mentioned is some support for the judge's opinion.
62 573 F.2d at 970-71.
63 Id. at 969 n. 8.
E. The Noninitiating Party Unfairly Penalized

The NLRB's position of requiring thirty days for mediation unfairly penalizes the noninitiating party. In *Retail Clerks, Local 219*, even the petitioner admitted that "its untimely notice to the Service . . . was a violation of Section 8(d) (3) and hence an unfair labor practice under Section 8(b) (3)." Yet the Board's holding condones noncompliance, a noncompliance which unfairly penalizes the noninitiating party by forcing it to forego the rightful imposition of economic sanctions until the thirty-day period has passed. Therefore, to enforce the Board's ruling would create the inequitable situation in which "one party could flatly refuse to comply with [the statute] but at the same time demand for himself all the benefits of the Section." Under such circumstances the noninitiating party would not be able to use the legitimate economic leverage which otherwise would be available.

F. Potential Abuse

The Board's decision, in permitting one party to check the other's right, opens the statutory scheme to potential abuse, which, despite the Board's pleading otherwise, would actually frustrate the legislative purpose. In *Peoria Contractors*, the Seventh Circuit observed that the Board's bifurcating the sixty-day "cooling off" period into two periods of thirty days each "is in fact antithetical to the statutory scheme and would upset the delicate timing mechanism embodied in the Act." The Court further explained that the statute in allowing for only one sixty-day period for negotiation inserts the mediation services "at the optimum time for settlement." Thus, the Seventh Circuit concluded that if the Board's position were enforced, "[t]he probability of successful mediation occurring . . . is less apparent."

The Board's decision allows the union to restrict the management's options by effectively precluding the use of lockouts as a bargaining tool until the statutory thirty-day period expires. The Seventh Circuit concluded, however, that this result is unfair since the noninitiating party, which had bargained in good faith and could normally resort to a lockout after the expiration of the sixty-day period, would be at the mercy of the initiating party as to when it could lock out. The court perceived that by carefully manipulating the giving of notice, the initiating party

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64 265 F.2d at 816. See Procter & Gamble Union of Port Ivory v. Procter & Gamble Mfg. Co., 312 F.2d 181, 188-89 (1962); International Union of Operating Eng'rs v. Dahlem Constr., 143 F.2d at 473; In re Eisen, 88 N.Y.S.2d at 678. Kaynard v. Bagel Bakers Council [1968] 57 Lab. Cas. ¶ 12,499. Gorman in his treatise on labor law summarizes the law: "Failure to give timely notice to the mediation services is technically a violation of Section 8(d) (3). . . ." GORMAN, BASIC TEXT ON LABOR LAW, UNIONIZATION AND COLLECTIVE BARGAINING § 57 at 425 (1976). Yet, the Board "rarely addresses it as an unfair labor practice in isolation." Id. See also Lockout Loophole, supra note 15, at 498.

65 United Electrical, Radio, & Mach. Workers Local 1113 v. NLRB, 223 F.2d at 342.

66 Textile Workers v. NLRB, 227 F.2d 404, 410 (D.C. Cir. 1955). The court in this case further held that Congress did not limit "the use of economic pressure in support of lawful demands." Id.

67 500 F.2d at 58.

68 Id.

69 Id.
party could trap the noninitiating party into a more serious violation of the Act and then harvest the benefits of its strategy. The initiating party could also reserve its threat of untimely notification “to neutralize any pressure through strike or lockout which the other party might muster after sixty days to resolve the dispute quickly.”

In Hooker Chemicals the Seventh Circuit suggested that the threat of abuse materialized into reality. The union delayed filing notice so that it could coordinate bargaining at the three different plants thus placing unanticipated pressure on Hooker Chemicals and preventing timely intervention by the mediation services.

Regardless of the form, the threat of abuse is substantial. To allow such a risk, as the Board’s interpretation would, invites further strife when the Congress sought to prevent it. Thus, sanctioning an interpretation of Section 8(d)(3) which creates the possibility of abuse is not consistent with the goals of the Act.

The position of the Hooker Chemicals court provides strong incentive to the initiating party to file timely notice. Due to its dereliction in filing notice, the initiating party is temporarily stripped of its economic weapons, but the noninitiating party may, at its discretion, resort to economic sanctions. Thus, to prevent the noninitiating party from gaining this potential advantage, the initiating party will have greater incentive to file timely notice.

VI. Conclusion

The desire to avoid industrial strife through negotiation and, if necessary, mediation strongly supports the NLRB’s position of mandatory mediation. Yet the Hooker Chemicals result is more appropriate and desirable. The Seventh Circuit’s decision is more appropriate because it recognizes the factual differences between the Retail Clerks, Local 1179 series of cases and the Hooker Chemicals case. The Seventh Circuit’s decision also more closely follows congressional intent and prior judicial interpretation of the Acts. The Hooker Chemicals result is more desirable because it more fairly weighs the interests of the parties, and provides for a more just resolution in that the timely use of mediation is encouraged and the chance for abuse of the statutory scheme is diminished. This is accomplished by avoiding the disadvantage of unfairly foreclosing the noninitiating party’s right to economic sanctions because of the initiating party’s violation of the Act.

David F. Parchem

70 If management were to lock out before the expiration of the period for mediation, the union could bring suit for back wages. If the union were to strike before expiration, management could lawfully discharge the employees.
71 Peoria Contractors v. NLRB, 500 F.2d at 58.
72 573 F.2d at 969.
73 Id.

Hirk v. Agri-Research Council, Inc.\

I. Introduction

The classification of discretionary futures trading accounts is a problem1 that presently has the federal circuit courts of appeal in conflict. In particular, disagreement exists on the question whether discretionary accounts in commodities futures are securities2 within the meaning of the Securities Act of 1933 and the Securities Exchange Act of 1934 (Securities Acts).3 This disagreement has resulted in considerable confusion regarding the requisite elements of investment contracts4 and has fostered various interpretations of a common enterprise.

In Hirk v. Agri-Research Council, Inc.,5 the Seventh Circuit faced the issue whether a discretionary futures trading account could be protected by the fraud provisions of the Securities Acts.6 Relying on Milnarik v. M-S Commodities Inc.,7 an earlier Seventh Circuit opinion, the court held that a discretionary account is neither an investment contract8 nor a certificate of interest or participation in a profit-sharing agreement9 and therefore not a security within the meaning of the Securities Acts of 1933 and 1934. In so ruling, the Seventh Circuit expressly rejected the Fifth Circuit's contrary holding in SEC v. Continental Commodities Corp.10 The Seventh Circuit's decision in Hirk merits further analysis for several reasons. First, despite the court's claim to the contrary,11 the Hirk holding ignores the remedial purposes of the Securities Acts and promotes form over substance by focusing on the language of the agreement between the investor and broker rather than the economic realities of such an agreement. Second, the court over-

5 561 F.2d 96 (7th Cir. 1977).
6 The fraud provisions are codified in 15 U.S.C. §§ 77q, 78j(b), 78o(c) (1976); SEC rules 10b-5, 15c1-2 and 15c1-7; 17 C.F.R. §§ 240.10b-5, 240.15c1-2, & 240.15c1-7 (1977).
7 457 F.2d 274 (7th Cir. 1972).
8 561 F.2d at 99.
9 Id. at 102.
10 497 F.2d 516 (5th Cir. 1974).
11 Id. at 102. See text accompanying note 67 infra.

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looks the diverse nature of discretionary accounts and attempts to enunciate an inviolable rule of law. Finally, Hirk fails to give adequate emphasis to the legal context within which the decision was rendered.

II. Statement of the Case

William F. Hirk was induced to enter a trading agreement with the defendant, Agri-Research Council, Inc. (ARCO), by the two individually named defendants, John Burlington and Glenn Andersen. Pursuant to the agreement, Hirk deposited $10,000 in an account with Miller-Lane & Co., an ARCO futures commission merchant. A power of attorney was executed appointing Burlington as his agent and attorney-in-fact. Burlington utilized Hirk's money for margin deposits while conducting transactions in Hirk's account.¹²

Hirk's complaint alleged that defendants Burlington and Andersen, the president of ARCO, made numerous misrepresentations to him regarding the profitability of the enterprise, the acumen of their analysts, and certain investment information to be supplied to him. Hirk was also promised that his losses would not exceed $7,500 and at no time would his account have a balance of less than $2,500. Profit and loss statements of other accounts managed by the enterprise were shown to Hirk, implying that all were profitable.¹³

Despite the defendants' knowledge that Hirk was a novice in commodities trading, Hirk was not informed that he was engaging in a high risk venture. Due to the defendants' mismanagement of his account, Hirk lost his initial investment of $10,000 and incurred additional liabilities of $17,880.¹⁴

Hirk's complaint sought recovery of $27,880 in actual damages and $100,000 in exemplary or punitive damages. Count I of the original complaint asserted that the discretionary trading account executed with the defendants was either "an investment contract" or "a certificate of interest or participation in a profit-sharing agreement" and thus was a security within the Securities Act of 1933 and the Securities Exchange Act of 1934. The security status of the discretionary account required registration under Section 5 of the 1933 Act¹⁵ and compliance with the anti-fraud provisions of both Securities Acts.¹⁶ Hirk claimed that the defendants' violation of these provisions made them liable for his losses under Section 12 of the 1933 Act.¹⁷

On June 24, 1974, Count I of Hirk's complaint was dismissed on the ground that the agreement with the defendants was not an investment contract and therefore not a security under Section 2(1) of the 1933 Act and Section 3(a)(10) of the 1934 Act.¹⁸ The court required a finding of a "common enterprise" before an investment contract could exist. This element was found to be lacking despite Hirk's claim of overlapping investment services and the similarity of concomitant

¹² Id. at 98.
¹³ Id.
¹⁴ Id. at 98-99.
¹⁶ See note 6 supra.
¹⁸ See note 4 supra.
transactions conducted in the various discretionary trading accounts managed by the defendants.¹⁹

To overcome the common enterprise requirement, Hirk amended his complaint to allege that the defendants treated all the discretionary trading accounts in substantially the same manner and therefore he shared pro rata with the other accounts "as if" all the funds had been commingled. Further, he averred that the defendants employed his monies to cover ARCO's operating expenses and to pay for additional advertising necessary to attract new investors. Amended Count I was dismissed on the grounds that Hirk's new allegations failed to establish the requisite commonality and were directly contrary to the terms of the agreement.²⁰ On appeal, the Seventh Circuit affirmed the dismissal of amended Count I.

III. The Conflicting State of the Law

SEC v. Howey²¹ is the landmark case defining the term "investment contract." In Howey, the Supreme Court defined an investment contract as a "contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party."²² The Court held that an offering of units of a citrus grove development coupled with a contract for cultivating, marketing and remitting the net proceeds to the investor was an offering of an investment contract within the purview of the Securities Act of 1933.²³

The conflict in Hirk regarding the requisite elements of an investment contract arose from this definition. Generally, a four-part test is utilized in applying the Howey investment contract definition:²⁴ a person must (1) invest money (2) in a common enterprise (3) with the expectation of profits (4) solely from the efforts of the promoter or a third party. The second element, a common enterprise, has presented difficult questions of interpretation. Each interpretation depends upon which promoter-investor relationship is considered to have fulfilled the requisite degree of commonality.²⁵

A. The De-emphasis of a Common Enterprise—The Liberal Interpretation

The Howey test has received two basic judicial interpretations. The first, or liberal interpretation, originated in Maheu v. Reynolds & Co.,²⁶ in which

¹⁹ 561 F.2d at 99.
²⁰ Id. Hirk's amended complaint included three pendent claims based on violations of the Illinois Blue Sky Law, common law misrepresentation, and breach of a fiduciary duty. The pendent claims were dismissed without prejudice. 561 F.2d at 98 n.1.
²¹ 328 U.S. 293 (1946).
²² Id. at 298-99. At a later point the Court states that "the test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." Id. at 301.
²³ Id.
²⁵ Whether a common enterprise need be found at all has been challenged given the facts of Howey. See Bonnett, supra note 1.
Howey was found to require either a common enterprise or an expectation of profits derived solely from the efforts of others. The Maheu court stated that an agreement could be classified as a security despite the absence of a pooling arrangement or a common enterprise. Professor Loss’ treatise on securities regulation was cited in support of this contention. Loss states that “a pooling arrangement among investors helps, but it is not essential.” He proposes that in deciding whether an investment contract exists, “the line is drawn, . . . where neither the element of a common enterprise nor the element of reliance on the efforts of another is present.”

In rejecting the argument that security status was lacking, the court read Loss to propose that reliance on the skills of the broker would suffice for the absence of a common enterprise. The stipulated facts of Howey were asserted as support for this conclusion. The court’s analysis, therefore, focuses on the broker’s control of the account and the investor’s dependence on the broker’s skill in the generation of profits. The greater the broker’s skill and client’s dependence, the more likely a security will be found notwithstanding the absence of a formal finding of a common enterprise.

The liberal interpretation of a common enterprise was expanded in SEC v. Glenn Turner Enterprises. In Turner, the Ninth Circuit defined a common enterprise as “one in which the fortunes of the investor are interwoven with and dependent upon the efforts and success of those seeking the investment of third parties.” This approach emphasizes the dependence element found in Maheu and in addition, recognizes the common interest of the broker and investor as satisfying the commonality element. This type of commonality has been referred to as “vertical commonality.” The Turner court stated that in deciding whether an investment contract exists, a more “realistic” test should be employed, namely, “whether the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.”

282 F. Supp. at 429 (quoting 151 F.2d at 715-16 n.5). See note 25 supra for writers supporting this view.

27 Id. at 429.
28 Id.
29 1 L. Loss, Securities Regulation 489 (2d ed. 1961) [hereinafter cited as Loss].
30 Id.
31 282 F. Supp. at 429 (citing Loss at 491).
32 The facts stipulated to in Howey were that [a]ll sales (made by defendants) have been an out-right sale of a definitely identified tract of land. In no instance has there been a sale of a right to share with others in the profits of land held in common with the defendant Companies or others. . . . In the care of each grove, as in the yield of fruit, the cost of the care and the proceeds of the fruit may be, and are, definitely and distinctly accounted for with respect to the specific property owned by the individual.
34 474 F.2d 476 (9th Cir.), cert. denied, 414 U.S. 821 (1973).
35 Id. at 482 n.7.
36 Id.
37 Discretionary Accounts, supra note 1, at 401 n.1; Bromberg § 434.
38 474 F.2d at 482.
39 Turner involved a scheme to sell self-improvement courses. 474 F.2d at 476.
The Fifth Circuit extended the vertical commonality concept in the context of discretionary accounts in SEC v. Continental Commodities Corp. The court in that case adopted the Ninth Circuit's definition of a common enterprise and held that an investment contract existed when the broker's payment was based solely on commissions and did not depend on the profitability of the account. Continental Commodities has been interpreted to hold that no pooling element need be found when trading in the account lies within the broker's discretion.

Continental Commodities is unique because the relevant discretionary account was created to purchase options on commodities futures contracts as opposed to the contracts themselves. In these circumstances, if a customer elects to exercise his option, the broker must then secure the futures contract. The substantial cost of such contracts may necessitate the pooling of funds from the various discretionary accounts held by the broker. A transaction of this type should thereby satisfy the common enterprise element. Thus, accounts dealing with futures options are more susceptible to a finding of a common enterprise.

One commentator has suggested that the Continental Commodities result and its reliance on Turner can be justified solely by the conduct of the broker. In Continental Commodities the broker's conduct was similar to that of a promoter since discretionary accounts were solicited. The usual discretionary account involves the situation in which the investor seeks the services of the broker. Thus, solicitation of investor monies might stimulate the finding of a security.

The Fifth Circuit, however, did not sustain its decision on that basis. Instead, the court opted to avoid a "litmus application of the Howey test" and elected to reject the necessity of a pooling of investor funds. The court stated: "the critical factor is not the similitude or coincidence of investor input, but rather the uniformity of impact of the promoter's efforts." The court also rejected the notion that investor remuneration on a pro rata basis is necessary: "The fact that an investor's return is independent of that of other investors in the scheme is not decisive. Rather, the requisite commonality is evidenced by the fact that the fortunes of all investors are inextricably tied to the efficacy of the [broker]."

The cases endorsing the liberal interpretation reveal a commitment to enforce the remedial purpose of the Securities Acts. A premium is placed on protecting the investor while the increased burdens of registration are placed on the broker. This goal is accomplished by applying an expansive definition of

40 497 F.2d 516 (5th Cir. 1974).
41 Id. at 522.
42 See Discretionary Accounts, supra note 1, at 409 n.45 and accompanying text.
43 497 F.2d at 518.
45 Discretionary Accounts, supra note 1, at 409 n.46.
46 497 F.2d 521-22.
47 Id. at 522 (quoting SEC v. Koscot Interplanetary Inc., 497 F.2d 473, 478 (5th Cir. 1974)).
48 Id. (quoting 497 F.2d at 479).
a common enterprise so as to extend the scope of the investment contract theory of security status. The contrary approach demands a literal reading of Howey and narrow view of a common enterprise.

B. Fidelity to Howey—The Necessity of a Common Enterprise

The second approach to the Howey test requires a rigid application of the four criteria, particularly the common enterprise element. The benchmark case for this interpretation, as well as for the proposition that discretionary futures accounts are not securities due to the absence of a common enterprise, is Milnarik v. M-S Commodities, Inc. In Milnarik, the discretionary account agreement called for the broker’s compensation to come solely from commissions generated by his trading in the account. Thus, the broker’s interest in the agreement was not dependent upon the profitability of his transactions and no commingling of funds with other discretionary futures accounts occurred.

Under these circumstances, the Seventh Circuit held that the agreement was not an investment contract and therefore not a security within the purview of the Securities Act of 1933. The court stated that “judicial analysis of the question whether particular investment contracts are ‘securities’ within the statutory definition have repeatedly stressed the significance of finding a common enterprise.” Although the plaintiffs alleged that the defendant broker had entered into similar agreements with other investors the court found that “the success or failure of those other contracts had no direct impact on the profitability of plaintiffs’ contract.” Thus, the Milnarik court concluded that the various customers were merely represented by a “common agent” and were “not joint participants in the same investment enterprise.”

Milnarik apparently requires the presence of a pooling of monies of various investors so as to evince a common interest in the investment. Pooling of investor monies has been described as “horizontal commonality.” Professor Bromberg describes this form of commonality as “requiring that [investors] share profits and losses, or at least that one investor’s success or failure have an impact on other investors.”

The Third Circuit endorsed the Milnarik approach in Wasnowic v. Chicago Board of Trade. In Wasnowic, a securities fraud complaint filed by a corporate investor in a discretionary commodity futures account was dismissed for want of a common enterprise. The district court found a common enterprise to be lacking (1) in the corporation’s relationship with its shareholders and (2) despite the actual commingling of funds of the various investors in violation of their agreements with the broker. The district court asserted that “[w]hether an ‘investment’ contract exists depends, like any other contract, upon the original conditions under which the contract was entered into.”

50 457 F.2d 274 (7th Cir. 1972).
51 Id. at 275.
52 Id. at 276.
53 Id.
54 Id.
55 BROMBERG § 433.
56 Id.
intention of the parties." The court rejected the theory that a common enter-
prise could be established by the unilateral act of one party to the agreement.

The Seventh Circuit considered Hirk cognizant of the conflicting interpreta-
tions of the Howey test. The liberal interpretation as enunciated by the Fifth Circuit in Continental Commodities accepts "vertical commonality" as the equivalent of a common enterprise. The alternative approach is the Seventh Circuit's own ruling in Milnarik which demands the existence of "horizontal commonality" before the common enterprise criteria is satisfied. Thus, the question in Hirk was whether the Seventh Circuit would elect to endorse its earlier decision in Milnarik or adopt the less rigid test of Continental Com-
modities.

IV. The Seventh Circuit's Resolution of Hirk

On appeal, Hirk presented three alternate arguments to counter the Milnarik precedent. First, he suggested that the Seventh Circuit reexamine its holding in Milnarik that a common enterprise requires both "multiple investors and a pooling of their funds" and instead elect to adopt the Fifth Circuit's contrary view in Continental Commodities. Second, Hirk called for a reexamination of the pooling requirement enunciated in Milnarik "in terms of the remedial purpose of the [Securities] Acts, the legislative directives of flexibility, and the emphasis on substance over form." Finally, as an alternative to finding security status premised on an investment contract, Hirk claimed the existence of a security on the basis of a "certificate of interest or participation in a profit-sharing agree-
ment."

A. Reexamination of Milnarik in Light of Continental Commodities

The Hirk court resolved the pooling issue by focusing on the Fifth Circuit's express rejection of the need for a pooling arrangement or pro rata sharing of profits as well as its consistency with Milnarik. Noting that Milnarik did not directly address the pooling requirement, the court sought to ascertain whether that requirement was subsumed in Judge Steven's opinion. The answer was found in footnote seven of Milnarik. The court cites footnote seven as holding that Howey requires an investment pool. In writing the Milnarik decision, Judge Stevens utilized footnote seven to draw attention to the fact that in Howey the investors in the citrus tracts were not entitled to specific fruit. The land developer was only accountable to in-
dividual investors for an allocation of net profits based upon a survey conducted at the time of picking. As a result, all the fruit was pooled by the developer and sold under its own name. The Milnarik court felt that the relative importance

58 352 F. Supp. at 1070.
59 561 F.2d at 100.
60 Id. at 101-02.
61 Id. at 102.
62 Id. at 100.
63 457 F.2d at 279 n.7.
64 Id.
of commonality was reflected by the Supreme Court’s statement that “[t]he investors provide the capital and share in the earnings and profits; the promoters manage, control, and operate the enterprise.” In essence, the Seventh Circuit held that footnote seven conclusively required a pooling of investor funds. Thus, Hirk’s first argument fell with the court’s rejection of Continental Commodities.

B. Reexamination of Milnarik in Light of the Remedial Purpose of the Securities Acts

Hirk’s contention that the Seventh Circuit reexamine Milnarik in light of the remedial purpose of the Securities Acts and reach a conclusion consistent with the flexible standards asserted by the Supreme Court in Tcherepnin v. Knight was also rejected. The court stated that Milnarik was decided by a court cognizant of these guidelines and therefore the decision was consistent with both the letter and spirit of the law.

C. The Absence of a Certificate of Interest or Profit-Sharing Agreement

The argument that the discretionary futures agreement entered into with ARCO was a certificate of interest or profit-sharing agreement, and thus a security, was dismissed on the same basis as the investment contract theory, namely, a lack of commonality. The court held that the commonality requirement was identical to that necessary for an investment contract as defined by Milnarik. This assertion was made despite the presence of a 75%-25% profit-sharing clause in Hirk’s agreement with ARCO and its literal inclusion in the securities definition as found in the Securities Acts. Hirk cited Professor Loss’ statement that “the classic example of [such an agreement] is a contract whereby the buyer furnished the funds and the seller the skill for speculating in the stock or commodity markets under an arrangement to split any profits.” The court averred that the cases cited by Loss made no real distinction between investment contracts and profit-sharing agreements and noted that each investment scheme was characterized by widespread public participation. Thus, the court found the commonality element to be firmly entrenched in the definition of a profit-sharing agreement.

V. An Analysis of the Seventh Circuit’s Finding

Hirk is a classic example of judicial myopia—the application of the rule of stare decisis when dissimilar facts mandate a more responsive analysis. The Hirk facts are readily distinguishable from those in Milnarik in that no profit-sharing
agreement existed in *Milnarik*. Also, a critical analysis of the facts of *Howey* lends credence to the de-emphasis of the commonality requirement as found in the circuits following the liberal interpretation of the *Howey* test. Despite the factual distinctions of *Milnarik* and *Howey* the Seventh Circuit was apparently determined to establish an inviolable rule of law; discretionary accounts are not securities.

The facts in *Howey* support the view that the common enterprise element must be applied loosely. The investors in the Howey Company citrus tree scheme paid varying prices for their plots depending on the age of the trees. Prices ranged from $675 to $1000 per acre. Every purchaser entered into a separate contract for a distinct tract of land. Supplementing the sale contracts were service and management contracts. These provided for the development of the land and the harvesting and sale of the fruit at the discretion of the Service Company. The company in turn received a management fee plus expenses for labor and materials employed in developing the particular tract of land. The total cost of care for an individual tract of land was “definitely and distinctly accounted for with respect to the specific property owned by the individual.” Although the yields of the individual tracts of land were pooled for marketing, the individual investor’s profits were determined by the amount of produce actually generated by his tract and at no time was there a sale of a right to share in the profits of land commonly held.

Given these facts, it is obvious that the investment scheme in *Howey* was substantially unitary in nature. Each tract had “a success or failure rate without regard to the others.” The return on any given tract was dependent upon the unique costs and yield it produced. The pooling of total yields for marketing purposes is merely reflective of the fungible nature of the commodity and a uniform market price. Thus, the so-called pooling element, to which the Seventh Circuit attached such importance in *Hirk*, is of little importance to the return on a single tract of land. The success or failure of one tract would have little direct impact on the profitability of the other tracts. Individual tracts among the 2,500 acres of citrus groves would have varying costs and yields depending upon the extent of disease or insect infestation, terrain conditions, soil fertility, tree replacements, and general maintenance. Therefore, the definition of a common enterprise articulated in *Turner*, and later followed in *Continental Commodities*, is more descriptive of the factual setting in *Howey*: “whether the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.” The *Howey* facts indicate that those circuits endorsing the liberal interpretation

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73 151 F.2d at 716 n.5.
74 *Id*.
75 *Id*.
76 *Id*.
77 561 F.2d at 101. This is the language used by Seventh Circuit to describe the discretionary account in *Hirk*.
78 This was the test for a common enterprise applied in *Milnarik*. See note 53 supra.
79 60 F. Supp. at 411.
80 474 F.2d at 482 n.7.
81 497 F.2d at 522.
of the common enterprise element are more responsive to the Supreme Court's analysis. Thus, the Seventh Circuit's narrow definition of an investment contract is difficult to comprehend based on the Howey factual setting. The requirement of multiple investor input with interdependence of profit and losses is simply not presented by the Howey scheme. Concluding that Howey demands an investment pool as the Seventh Circuit first did in Milnarik, and did subsequently in Hirk, results in an interpretation unsubstantiated by the Howey facts.

By opting for a narrow interpretation of the common enterprise element, the Seventh Circuit was also endorsing form over substance. The Supreme Court, however, has clearly encouraged a contrary approach. In Howey the Supreme Court noted that "form was disregarded for substance and emphasis was placed upon economic reality" in state court decisions dealing with the scope of the term investment contract. The Court later averred that the Securities Acts require a broad definition of the term "security": "[the definition] embodies a flexible rather than a static principle, one that is capable of adaption to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." This elastic approach was reasserted by the Court in Tcherepnin v. Knight. Noting the remedial nature of the Securities Acts, the Court in Tcherepnin expressed an obligation to follow the expansive guidelines established in Howey.

Notwithstanding the Supreme Court's encouragement to employ a flexible definition of a security, the Seventh Circuit excluded a discretionary futures account from its purview. Such exclusion was accomplished by concentrating on the unitary nature of the agreement, namely, an investor and a broker came to terms.

The approach of the Hirk court is formalistic because it focuses on the contractual relationship between the parties rather than the economic realities involved. The investor is "pooling" his resources with the broker in every sense of the term. Resources are commingled to generate profits for both. The investor supplies the funds while the broker provides the business acumen. The two interests are interwoven into a single "common enterprise." Any definition of a common enterprise which would exclude such a relationship can only be characterized as demanding form while sacrificing substance. Thus, a literal reading of the investment agreement should not preclude consideration of the economic realities of the situation.

The Seventh Circuit's decision in Hirk also ignores the diverse nature of the discretionary account and the differences between the agreements posed by Hirk and Milnarik. Generally, discretionary accounts take one of three forms:

1. The investor places his money with a broker, permitting the broker to invest it at his discretion. The broker is paid on a commission basis. The broker has similar accounts with other investors, but each is handled on an individual basis with the broker trading only for that account.

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82 328 U.S. at 298.
83 Id. at 299.
84 389 U.S. at 336.
85 Id.
(2) The account is opened giving the broker authority to enter into transactions at his discretion. The broker is compensated from the profits generated by his trading skill or the broker may invest his own funds.

(3) Several investors pool their money and have it invested at the broker's discretion or the broker combines the funds of several accounts and invests for the benefit of all.\textsuperscript{86}

The structure of these three arrangements reveals that the degree of commonality present in a given discretionary account can vary greatly. The first type of agreement presents the strongest case for not finding a common enterprise. The interests of the broker and the investor are completely segregated.\textsuperscript{87}

The second and third types are representative of the vertical and horizontal commonality distinction. The vertical commonality of the second type of discretionary account is representative of the agreement in \textit{Hirk}. The interests of the investor and broker were interwoven by a 75%-25% profit-sharing agreement. This provision makes the \textit{Hirk} agreement readily distinguishable from \textit{Milnarik} in which the broker was paid on a commission basis regardless of the profitability of the account.\textsuperscript{88} Hence, vertical commonality was absent in \textit{Milnarik} although present in \textit{Hirk}.

The \textit{Milnarik} decision also rejected the notion of a common enterprise despite the fact that the discretionary account in question was a seven-person joint account,\textsuperscript{89} which is representative of the third type of arrangement. Multiple investors in such a single scheme is referred to as horizontal commonality. This difference in the method of the broker's compensation makes it clear that the \textit{Hirk} agreement is not analogous to the \textit{Milnarik} contract, which itself presents an element of common enterprise distinct from that found in \textit{Hirk}, namely horizontal commonality.

Despite the lack of similarity between the discretionary accounts in \textit{Hirk} and \textit{Milnarik}, the Seventh Circuit held the \textit{Milnarik} decision to be controlling. By so ruling, the court ignored the distinction between vertical and horizontal commonality. Implicit in both the \textit{Milnarik} and \textit{Hirk} decisions is the necessity of horizontal commonality before the common enterprise element can be satisfied. Not only is this position inconsistent with the Supreme Court's decision in \textit{Howey}, but it also fails to acknowledge the varied forms of discretionary accounts. By relying on \textit{Milnarik} to render void the claim of security status in \textit{Hirk}, the Seventh Circuit rejected the possibility of vertical commonality satisfying the common enterprise requirement. Such a generalized approach to the commonality element results in a single conclusion: discretionary futures accounts are not securities. Such a result denies the investor who relies on the broker's invest-


\textsuperscript{87} The SEC made such a recommendation when the broker offered the account without solicitation, all accounts were segregated, independent investment decisions were made, and the broker and investor did not share profits. See E.F. Hutton and Co., SEC Div. Corp. Fin. 94-95 Letter (Aug. 8, 1972), [1972-1973 Transfer Binder] \textit{FED. SEC. L. REP.} (CCH) ¶ 79,007.

\textsuperscript{88} 457 F.2d at 275.

\textsuperscript{89} 320 F. Supp. 1149 (N.D. Ill. 1970).
ment skills, and who shares his profits with the broker, the protection of the Securities Acts. Yet Howey clearly demonstrates that either vertical or horizontal commonality is sufficient to insure classification as a security.\textsuperscript{90}

The context in which Hirk was decided also merits further analysis. In Hirk, the Seventh Circuit was reviewing the dismissal of a complaint and therefore was compelled to accept all allegations asserted in the complaint as true.\textsuperscript{91} The court, therefore, accepted as valid the claim that ARCO "treated all of the discretionary accounts in substantially the same manner and consequently that he shared pro rata with the other accounts ‘as if’ all the funds had been commingled."\textsuperscript{92}

Despite these allegations, the court ignored the presence of a common enterprise "especially in light of plaintiff’s claim that such treatment was in direct contravention of defendant’s representations and plaintiff’s expectations."\textsuperscript{93} Thus, the court was willing to permit ARCO to escape the purview of the Securities Acts by intentionally violating the agreement with Hirk and perpetuating the fraud it had allegedly committed.

Such a conclusion continues to emphasize form over substance and ignores the economic realities inherent in the Hirk circumstances. If ARCO treated all the discretionary accounts in the same manner and Hirk was actually sharing pro rata in the profits, then ARCO was essentially managing a mutual fund. Hirk was alleging in essence that ARCO was dealing in investment contracts collectively for the various accounts and then allocating profits and losses on the basis of investment amounts. By ruling that the absence of authorization of this conduct in the investment agreement will preclude it as the basis of a common enterprise, the Seventh Circuit enables the broker to control whether a common enterprise will be found. An uninformed investor is not likely to require a broker to state explicitly the manner in which he will conduct his business. That the account is discretionary serves as an indication that the investor acknowledges naivete in commodities dealings.

In resolving Hirk the Seventh Circuit was obviously cognizant of Howey and later Supreme Court decisions suggesting an expansive definition of a security. Thus, one must speculate as to the court’s motive in applying a restrictive definition. To some extent the court may have been inspired by judicial expediency. Although a broad interpretation would extend the protection of the Securities Acts, other factors require consideration. By extending security status to discretionary accounts dealing with commodities futures, the court would be infringing on the commodities market, an area subject to an independent regulatory scheme and enforcement agency. The resulting overlap in regulations and statutory remedies would add further complication to the already complex regulatory scheme of the commodities market. Increased costs of registration and compliance with the Securities Acts also militate against the

\textsuperscript{90} Vertical commonality is evidenced in Howey by the management-service contracts, which place discretion in the Service Company in the management of the citrus tracts. 328 U.S. at 299-300.

\textsuperscript{91} 561 F.2d at 98 n.5, (citing Cruz v. Beto, 405 U.S. 319 (1972)).

\textsuperscript{92} 561 F.2d at 99.

\textsuperscript{93} Id.
extension of the Securities Acts. Thus, the segregation of the securities and commodities markets reduces duplication of statutory remedies and assists in eliminating the unnecessary costs of overregulation.

Notwithstanding the merits of these policy considerations, the Seventh Circuit predicated the Hirk decision on the Howey criteria and subsequent decisions. Critical analysis of Howey renders suspect the conclusion that the unitary nature of a discretionary account precludes security status. Also, the claim of adequate remedies under the Commodity Exchange Act of 1936 fails to focus on the basis of the security claim. Security status is alleged in the discretionary account, not the commodities futures contracts. The nature of the agreement between the broker and investor is averred to be an investment contract. Therefore, the object of the investment, whether citrus groves or commodities futures contracts, is not of importance. The court's attention should be directed to the investor giving the broker money with the broker making the investment decisions. The Seventh Circuit's implicit view to the contrary evinces a results orientation, which does have practical justification, but is inconsistent with existing case law.

In summary, economic reality should be the court's concern in the search for a common enterprise. The relevant inquiry should be to determine the manner in which the broker manages the discretionary account, both individually and in relation to other accounts. By asserting the allegations of uniform treatment of accounts and pro rata sharing of profits, Hirk was attempting to uncover an investment scheme that was masquerading as an individualized opportunity, but was in reality a common venture. These allegations should be sufficient to establish a cause of action. The allegations still must be proven before recovery under the Securities Acts will be allowed.

VI. Conclusion

The Seventh Circuit's decisions in Milnarik and Hirk reveal a commitment to deny security status to discretionary accounts. By following its earlier decision in Milnarik, the Seventh Circuit failed to focus on the precise terms of the Hirk agreement and instead sought to enunciate an inviolable rule of law, discretionary futures trading accounts are not securities. This blanket approach to the issue fails to recognize that discretionary accounts are not indistinct, but present varying degrees of commonality.

The Seventh Circuit's denial of security status to the Hirk agreement based on the unitary nature of the account is also without merit. The Supreme Court found the existence of an investment contract in Howey, which presented an investment scheme more unitary than that found in Hirk. Investor profits and losses in Howey were not interdependent, but segregated by the terms of the investment agreement.

The decision in Hirk may be explained in part by a desire to keep the commodities laws and securities laws distinct. Although the elimination of the

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94 In Hirk, the Seventh Circuit reversed a district court dismissal of a cause of action under the Commodity Exchange Act of 1936. 561 F.2d at 103-04.
overlap in statutory remedies might foster judicial expediency, this decision is ultimately one for the legislature and not the courts. An aggrieved investor who has satisfied the Howey criteria should not be denied the protection of the Securities Acts by the application of an overly restrictive definition of a "common enterprise." Employment of such a test tends only to obfuscate the definition of an investment contract and adds more confusion to an area of law plagued by uncertainty.

Although discretionary futures accounts may be drawn so as to escape securities status, Hirk did not present such a case. The Hirk agreement conforms to any reasonable application of the Howey criteria. The exclusion of the Hirk account from the purview of the Securities Acts contradicts the remedial purpose of the Acts. It also runs contrary to the express instructions of the Supreme Court which suggest an expansive definition of a "security."

Given the division of the circuits on this issue, Supreme Court resolution is necessary. Until this is accomplished, both brokers and investors in the various circuits are subject to inequitable treatment under federal law. Absent final resolution, the federal courts should follow those guidelines already established by the Supreme Court and focus on the precise terms of the agreement in question and not attempt to establish immutable rules of law. Unless this course is pursued, further inconsistencies and distortions of the Securities Acts are certain to follow.

Glenn A. Clark

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Many of the decisions in the various circuits are those of the district courts. Therefore, realignment is possible. Both the D.C. Circuit and Ninth Circuit have expressed the possibility of granting discretionary accounts security status if presented with the proper fact situation.
Securities Regulation—Limited Partnership Capital Contributions Constitute Separate "Purchases" for a Rule 10b-5 Action.

Goodman v. Epstein*

I. Introduction

In Goodman v. Epstein, the Seventh Circuit was confronted with the question whether each capital contribution made by limited partners in response to a call from general partners, pursuant to a partnership agreement, constituted a separate “purchase” of a security for the purposes of an action for fraud brought under § 10(b) of the Securities Exchange Act of 1934 and Securities and Exchange Commission (SEC) rule 10b-5. Although the partnership agreement did not provide an express option to the limited partners to refuse to contribute capital on the general partners’ call, the Seventh Circuit said the agreement contemplated a “continuing relationship” between them and concluded that “the contribution by each Limited Partner in response to the call constituted a separate ‘purchase’ of a security and, therefore, any material representations or omissions at that time were ‘in connection with the purchase or sale’ of a security, as required by § 10(b) and Rule 10b-5.” By this decision, the Seventh Circuit departed from analogous case law and expanded the definition of “purchase” within the context of the federal antifraud provisions.

II. Statement of the Case

A. The Agreement

Plaintiffs in Goodman brought an action seeking compensation for damages suffered in connection with a limited partnership land development scheme that went awry. In October of 1971, Lee A. Freeman, an experienced real estate investor and attorney, contacted L. W. Douglas, an experienced real estate develop-

* 582 F.2d 388 (7th Cir. 1978).
1 Section 10 of the Securities Exchange Act of 1934 reads in part:
   It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
   (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.
2 Rule 10b-5 states, in part:
   It shall be unlawful for any person, directly or indirectly . . . (a) to employ any device, scheme, or artifice to defraud, (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person in connection with the purchase or sale of any security.
3 582 F.2d at 414.
er and Sidney Epstein to inform them that he wanted to obtain a substantial equity interest in a real estate development project Douglas was proposing. Subsequently, Freeman became the moving force in setting up the financing for the project. In June of 1972, the real estate development project was formalized into the D-E Limited Partnership Agreement. Freeman and seven others\(^4\) signed as limited partners while Douglas, Epstein, and two others\(^5\) signed as general partners.

The purpose of the partnership, as expressed in the agreement, was "residential development" of a 108-acre tract of vacant land (Westmont Project).\(^6\) To finance the venture the limited partners contractually obligated themselves in the agreement and subsequent amendments\(^7\) to furnish total capital of $3 million.\(^8\) Moreover, it can be assumed that this contractual agreement did not contain any alternatives to contribution by the limited partners because the defendants in support of their case, and the court in making its decision, went to great lengths to show that the limited partners did have a "legal option" to contribution. However, in the exhaustive list of these possible alternative courses of action available to the limited partners,\(^9\) neither the limited partners nor the court made mention of any alternative provided for in the agreement.

Early on, the Westmont Project encountered significant problems, including: formal denial of a sewage permit by the Illinois Environmental Protection Agency, denial of local government approval because of undersized pipes of an adjacent developer, and the removal of Douglas\(^10\) as a general partner. Failure

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\(^4\) Jerry E. Poncher, a sometimes client of Freeman, originally assumed forty percent of the equity interest. In July of 1972 David L. and Mollie E. Goodman purchased twenty-five percent of Poncher's interest. The percentage division of the remaining interest was not set out in the opinion although it was stated that Freeman had tentatively agreed in 1971 to take or place at least sixty percent of the equity. Lee A. Freeman, Jr., Freeman's son and law partner, was the only other limited partner mentioned in the opinion.

\(^5\) Raymond Epstein and Melvin M. Kupperman were the remaining original general partners. Messrs. Epstein and Kupperman were architects, engineers and developers for the project.

\(^6\) The project as originally planned consisted of three phases, the first of which was the construction of some 480 rental units on approximately thirteen acres of the 108-acre tract. The limited partners' $3 million obligation concerned only phase one.

\(^7\) The first amendment, the only one pertinent here, was signed at the same time as the agreement. Shortly after the execution of the agreement (and its amendment), a certificate of limited partnership was signed and filed pursuant to Illinois state law.

\(^8\) Although the court stated the $3 million was not collected "up front" but was to be contributed upon requests from the general partners from "time to time," this does not imply that the limited partners were not committed for the entire amount. Nothing in the agreement would have prohibited the general partners from requesting the lump sum up front; in fact, one of the plaintiffs believed that the total amount was due upon signing the agreement.

Under certain circumstances, the limited partner could be called upon to contribute in excess of $3 million. 582 F.2d at 412-13, 391 n. 8.

\(^9\) See note 58 infra and accompanying text.

\(^10\) Douglas' removal resulted primarily from his performance on another project. One of the terms of Douglas' withdrawal, which was negotiated by Freeman, was the release of any claim arising from his acts as general partner. To effect this release a second amendment to the partnership agreement was executed that read:

The Limited Partners and each of them do hereby release and forever discharge Raymond Epstein, Sidney Epstein and/or Melvin M. Kupperman from any and all claims, debts, liabilities, payments, obligations, actions and causes of action of every nature, character and description which the Limited Partners or each of them hold as of the date of actual execution of this Second Amendment or have ever held against Raymond Epstein, Sidney Epstein and/or Melvin M. Kupperman arising out of or in any way connected with the partnership.

582 F.2d at 394 (quoting from the Second Amendment to the partnership agreement).
of the Westmont Project, as originally planned, was conceded in March of 1973 when the developers, faced with these and other difficulties, requested return of the money the partnership had paid to obtain the necessary building permits.

During the period described above, the limited partners responded on several occasions to capital calls. Another call came on June 6, 1974, requesting money for payment of interest and taxes. At the district court trial below, a dispute arose concerning whether the limited partner plaintiffs had knowledge of the serious difficulties encountered by the general partner defendants. The trial, however, resulted in a general verdict; hence, there was no finding of fact resolving the dispute. The final months of the Westmont venture involved accounting and disbursement of funds as both the limited and general partners "jockey[ed] for position in the lawsuit which was then looming ever more ominously over the horizon."

B. The Litigation

Suit was filed on February 23, 1976, by the limited partners who alleged violations of § 10(b) of the Securities Exchange Act of 1934 and SEC rule 10b-5 (Count I), common law fraud (Count II), and breach of fiduciary obligation (Count III), and sought $1,061,500 in damages. The jury returned a general verdict in favor of the defendant general partners on all three counts.

On appeal, the plaintiff limited partners raised seven errors on the part of the trial judge (4 pertaining to instructions and 3 involving his conduct at trial). Six of the seven errors were found insufficient to require a reversal but, one, the trial judge's instruction stating that "each subsequent capital contribution made pursuant to such an agreement does not constitute a purchase of a security," was found to be an incorrect statement of the law. The Seventh Circuit held that this instruction amounted to a peremptory direction in favor of the defendants on Count I and therefore it reversed and remanded to the district court for a new trial on Count I.

C. The Issue

A prerequisite to a cause of action under § 10(b) is that there must have

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11 See note 6 supra.
12 582 F.2d at 394.
13 The plaintiffs in the action were David L. Goodman, Mollie E. Goodman, Lee A. Freeman, and Lee A. Freeman, Jr. The $1,061,500 figure represented fifty percent of the total investment of the limited partners, the owners of the other fifty percent interest electing not to sue.
14 The four errors alleged pertaining to instructions concerned: (1) the trial court's instructions dealing with the validity of the release of the general partners which accompanied Douglas' removal as a general partner; (2) the trial court's instruction on the means of knowledge and the due diligence defense; (3) the trial court's instruction on whether a limited partnership interest constitutes a security; (4) the trial court's instruction stating when a "purchase" occurs.
15 At oral argument, it was determined that all of plaintiffs' objections related only to Count I, thus judgment was affirmed as to Count II and Count III. The Seventh Circuit said that such an instruction amounted to a peremptory direction because if the only purchase or sale of a security occurred at the execution of the limited partnership agreement in 1972, then this claim, filed in February of 1976, would be barred by the three-year statute of limitation absent additional proof of fraudulent concealment.
been a purchase or sale of securities. Although there has been an enormous number of decisions concerning § 10(b) and rule 10b-5, there is limited authority on when a purchase or sale takes place.\textsuperscript{16} The issue in Goodman was whether each capital contribution made by the limited partners in response to a call from general partners, pursuant to a partnership agreement that did not provide any express options to contribution, constituted a separate “purchase” of a security under § 10(b) and rule 10b-5.

The limited partners, who cited no specific authority, contended that the original “commitment” to the limited partnership was not the final “investment decision” to be made in the venture; rather, each capital contribution was a separate “investment decision” and therefore each contribution was a separate “purchase” of securities. The general partners, on the other hand, relying primarily on the “commitment doctrine” enunciated by the Second Circuit in \textcopyright Radiation Dynamics, Inc. v. Goldmuntz,\textsuperscript{17} advanced the position that the limited partners became “committed” on the date of execution of the limited partnership agreement. Therefore, any duty on the part of the general partners arising under the federal securities laws to furnish information to the limited partners ceased at that time.

III. “Purchase or Sale” Under § 10(b) and Rule 10b-5

A. Statutes

The starting point in the construction of a statute is the language itself,\textsuperscript{18} even though history has demonstrated that cases construing the terms of the statute in context often turn out to be the most valuable source. This is essential because the scope of the antifraud rule 10b-5 cannot exceed the power granted the Securities and Exchange Commission by Congress under § 10(b).\textsuperscript{19} Although “the interdependence of the various sections of the securities laws is certainly a relevant factor in any interpretation of the language Congress has chosen,”\textsuperscript{20} “the meaning of particular phrases must be determined in context.”\textsuperscript{21} Moreover, “Congress itself has cautioned that the same words may take on a different coloration in different sections of the securities laws; both the 1933 and the 1934 Acts preface their lists of general definitions with the phrase ‘unless the context otherwise requires.’”\textsuperscript{22}

The statutory definitions in and of themselves lend little guidance in specific

\textsuperscript{16} See 5 A. Jacobs, \textit{The Impact of Rule 10b-5}, § 38.02(d) (1978).
\textsuperscript{17} 464 F.2d 876 (2d Cir. 1972).
\textsuperscript{19} 430 U.S. at 472-73; 425 U. S. at 212-14.
\textsuperscript{20} 425 U.S. at 206 (quoting SEC v. National Securities, Inc., 393 U.S. 453, 466 (1969)).
\textsuperscript{21} 393 U.S. at 466.
\textsuperscript{22} \textit{Id.} Section 3 of the 1934 Act provides:
(a) When used in this title, unless the context otherwise requires—
(13) The terms “buy” and “purchase” each include any contract to buy, purchase, or otherwise acquire.
(14) The terms “sale” and “sell” each include any contract to sell or otherwise dispose of.
factual situations; therefore, courts have generally looked to the purposes behind federal securities laws in their attempt to define the reach or limits of the securities acts' terms and phrases. Consequently, in the past, statutory terms and phrases have generally been broadly construed and have not been limited to their common law meanings. In particular, the Seventh Circuit has previously commented with respect to the 1934 Act's definitions of "purchase" and "sale":

[The] broad language [in the Exchange Act's definitions] indicates an intention by Congress that the words "purchase" and "sale" are not limited to transactions ordinarily governed by the commercial law of sales. The purpose is evidently to make control of securities transactions reasonably complete and effective to accomplish the purposes of the legislation.

The Seventh Circuit again in Goodman relied on this general history of expansive reading of the terms of the federal antifraud provisions when it made its determination to include each capital contribution within the meaning of "purchase."

However, "reading the Rule flexibly does not relieve . . . the obligation to define the limits of liability imposed by the Rule and to adhere to common sense." Indeed, recent Supreme Court decisions have sharply reversed the former trend of expansive reading and have given narrow interpretations to the terms of rule 10b-5 and other antifraud provisions.

B. The "Commitment" and "Investment Decision" Doctrines

Closely related to the question of what constitutes a "purchase" or a "sale" under § 10(b) and rule 10b-5 is the question of when the "purchase" or "sale" takes place, an issue on which there is limited authority. The time of the

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23 The Supreme Court in Hochfelder described the purposes behind the Acts as follows:

The Securities Act of 1933 (1933 Act), 48 Stat. 74, as amended, 15 U.S.C. § 77a et seq., was designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of honesty and fair dealing. See H.R. Rep. No. 85, 73d Cong., 1st Sess., 1-5 (1933). The 1934 Act was intended principally to protect investors against manipulation of stock prices through regulation of transactions upon securities exchanges and in over-the-counter markets, and to impose regular reporting requirements on companies whose stock is listed on national securities exchanges. See S. Rep. No. 792, 73d Cong., 2d Sess., 1-5 (1934).

24 See 393 U.S. at 466-67.
25 For general discussion of what is a "purchase or sale" and a list of authorities see generally Annot., 4 A.L.R. Fed. 1048, 1054 (1970) and 5 A. JACOBS, supra note 16, at § 38.02[a].
27 582 F.2d at 410.
29 See Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977) (where the Court opined that "artifice to defraud" and "fraud or deceit" in rule 10b-5 mean something more than breach of fiduciary duty). Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) (where the Court held specifically that "scienter—intent to deceive, manipulate, or defraud" must be alleged for a private 10b-5 action. 425 U.S. at 193). Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) (here the Court upheld a rule developed by the Second Circuit several years earlier and limited standing under rule 10b-5 to actual purchasers or sellers of securities).
30 See note 16 supra.
purchase or sale is crucial because in an action under rule 10b-5 the alleged misconduct must take place "in connection with a purchase or sale." To be "in connection with a purchase or sale," the misrepresentation or omission must be prior to or contemporaneous with the purchase or sale. Moreover, the need for setting a specific time for the sale or purchase becomes obvious when a person is faced with the question whether the claim is barred by the statute of limitations.

A general rule states that the time of purchase or sale is when the parties have become irrevocably committed to the consummation of the transaction. Referred to as the "commitment doctrine," the rule was recently enunciated by the Second Circuit in Radiation Dynamics and appears to be firmly established in the law. The rationale for using the moment of commitment as the critical point at which a "purchase" takes place derives from the purpose behind the federal antifraud provisions, that is, "[t]o substitute a philosophy of full disclosure for the philosophy of caveat emptor" in purchases or sales of securities. Once the parties decide to irrevocably commit themselves to a sale or purchase there is no reason to require further disclosures since the disclosure could have no effect on that decision.

In Radiation Dynamics, plaintiff Radiation Dynamics, Inc. (RD), in need of working capital, sold stock in another company, Technical Research Group, Inc. (TRG). RD, subsequently, discovered that TRG was involved in a merger with Control Data Corporation. As a result of the merger, the stock which RD sold for $299,000 to the defendants was resold, within two and a half months, by the defendants at an enhanced value of $690,270.

The evidence indicated that Cohen, an officer from RD, contacted Goldmuntz, the chief executive of TRG, in late May of 1964, to determine whether RD's share of TRG could be marketed. Goldmuntz indicated to Cohen a possible buyer of the stock who later proved uninterested. During this same period TRG became involved in merger discussions with another corporation which

31 For text of the rule see note 2 supra.
33 There is no general federal statute of limitations and no provision in § 10 of the Securities Exchange Act of 1934. Therefore, the appropriate act of limitation in the forum state controls. In Illinois, the forum state of Goodman, the action must be brought within three years of the purchase or sale of a security. Hupp v. Gray, 500 F.2d 993, 996 (7th Cir. 1974); ILL. REV. STAT. ch. 121½, § 137.13D (1975).
34 464 F.2d 876. Radiation Dynamics is not the first case in which the Second Circuit has articulated the "commitment" doctrine. In SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969), the court found that liability for insider trading violations under rule 10b-5 attaches at the time of commitment to buy or sell rather than the time of the transaction's ultimate execution.
38 Goldmuntz also introduced Cohen to one Fisher who subsequently arranged for the purchase of 3,000 shares of TRG stock. This sale was closed on August 8, 1964. These purchasers were also named as defendants.
were abandoned in the early stages. Determined to sell, Cohen recontacted Goldmuntz on June 24, at which time they made a binding oral contract under which Goldmuntz agreed to purchase 500 TRG shares, subsequently increased to 700 shares. The sale was actually completed on August 17. In the period between June 24 and August 17, TRG continued to seek a merger and on July 24, serious discussions were held with Control Data Corporation. Negotiations continued throughout August and then on September 23, the parties made a public statement that they had reached an agreement to merge. This merger agreement was finally signed on November 12, 1964.

RD, in an attempt to recover some of the lost profits, argued that Goldmuntz and the other defendants had violated § 10(b) and rule 10b(5) by not disclosing TRG's merger plans. A special verdict was returned in favor of the defendants upon a finding that the defendants did not possess "material information as to a reasonably possible . . . merger with Control Data" when RD, on June 24, made its respective "commitments" to sell its TRG stock. On appeal, RD argued against the trial judge's instruction that made the date of sale for disclosure purposes the date at which RD became "committed" to sell. RD contended that the date of the consummation of the transaction, August 8, was the actual date of the "sale." Affirming, the Second Circuit held that the trial judge correctly instructed the jury when he stated that the time of a "purchase or sale" of securities within the meaning of Rule 10b-5 is to be determined as the time when the parties to the transaction are committed to one another. A party does not, within the intendment of Rule 10b-5, use material inside information unfairly when he fulfills contractual commitments which were incurred by him previous to his acquisition of that information, for, as Judge Pollack instructed the jury, the Rule imposes "no obligation to pull back from a commitment previously made by the buyer and accepted by the seller because of after acquired knowledge." The goal of fundamental fairness in the securities marketplace is achieved by such a determination. . . . "Commitment" is a simple and direct way of designating the point at which, in the classical contractual sense, there was a meeting of the minds of the parties; it marks the point at which the parties obligated themselves to perform what they had agreed to perform even if the formal performance of their agreement is to be after a lapse of time. . . .

Decisions prior to Radiation Dynamics place emphasis on the options and investment decisions available to the complaining parties in lieu of performance under a purchase or sale agreement when determining whether the acts or omissions of the defendants were "in connection with the purchases or sale of any security."

In SEC v. North American Finance Co., the SEC brought an action to enjoin the defendant from engaging in acts and practices constituting violations of both securities acts. The defendant corporation had used subscriptions for

39 See note 38 supra.
40 464 F.2d at 884 n. 8.
41 582 F.2d at 412 (quoting from 464 F.2d at 891) (emphasis deleted).
 selling its stock. After subscribing to purchase stock, the subscribers had the option at a later time to either purchase the stock or cancel the subscription option, thus freeing themselves of further obligation. Recognizing that this option was available to the plaintiffs and therefore required the subscribers to make an investment decision, the court granted the injunction and held “that the sale is not consummated until the full subscription price has been received by the issuer and all shares subject to the subscription have been issued and delivered to the subscriber.”

In another stock subscription case, United States v. Kormel, Inc., the court found that representations made to induce investors to continue payment under the stock subscription were made “in the offer or sale” of the stock within the meaning of the securities act. The court showed its concern with the options available to the plaintiff when it stated:

*It is not persuasive to suggest that the subscribers, in making additional payments under the subscription contracts, would be doing only what they were already legally bound to do. In view of the injunction action brought by the SEC which resulted in the entry of a permanent injunction, by consent, against the defendants, it is at least likely that the contracts were voidable. Further, the contracts contained a provision for forfeiture of payments already made if the full subscription price were not paid, rather than an express promise to pay the full sum and from this viewpoint, were in the nature of conditional unilateral contracts rather than bilateral contracts.*

Thus, in both these subscription cases, where the courts found a sale at the time of payment, there was a contractual alternative available to both of the contributing parties.

In a Second Circuit case, Fershtman v. Schectman, the limited partners brought an action under the antifraud provisions of the federal securities legislation and rule 10b-5 for concealment or misrepresentation in the termination of a limited partnership. The court held: “if the defendants were legally entitled to terminate the partnership on March 31, 1968, in their sole discretion, it would make no difference what they represented or concealed, even if we assume in plaintiff’s favor that this transaction constituted a sale.” Thus, here again, when determining if there is a requirement to disclose, a court placed emphasis on whether the complaining party had an option remaining under the agreement.

Cases after Radiation Dynamics have followed the “commitment doctrine” rationale and have cited the case approvingly. In Sundstrand Corp. v. Sun Chemical Corp., the plaintiff had an option to purchase $6.7 million worth of stock for which it paid $334,785 on January 9. The final payment and exchange of shares was to come between February 9 and April 19. After the

43 Id. at 202.
45 Id. at 278.
46 Id. (emphasis added).
47 450 F.2d 1357 (2d Cir. 1971), cert. denied, 405 U.S. 1066 (1972).
48 Id. at 1360 (emphasis added) (citations omitted). For a discussion on the duty to correct and on how long correction is necessary, see 2 A. Bromberg, Securities Law: Fraud, § 6.11 (540-543) (1977).
49 553 F.2d 1033 (7th Cir.), cert. denied, 434 U.S. 875 (1977).
initial payment but prior to further payment, the purchaser discovered material information that made further purchases undesirable. On erroneous advice from counsel that it was committed to full payment, the remaining $6,360,915 was paid by Sundstrand on February 2. In a subsequent § 10(b) action, the Seventh Circuit found liability but limited damages to only the first payment on January 9 because it discovered from its own study of the record that Sundstrand was not obligated under its contract with Sun Chemical to purchase the stock. The court determined that the option actually gave Sundstrand the right but not the duty to proceed with the purchase. The Seventh Circuit reasoned, then, that Sundstrand had a legal and contractually valid alternative to the second payment, even if Sundstrand’s counsel was not aware of it. Because plaintiffs knew of the adverse information prior to payment, they were not injured by its nondisclosure. The important point is that the Seventh Circuit saw that the legal alternative to payment which constitutes a separate "sale" was based upon the contract itself.

Ingenito v. Bermec Corp., explains that the key to determining whether a transaction is a purchase or sale hinges on whether or not there is an investment decision to be made. Ingenito arose out of a cattle investment operation. The defendant was in the business of selling breeding cattle and maintaining them for the purchasers. The investors made periodic payments to the seller under maintenance contracts to pay for the upkeep of the cattle. The district court, "while not free from doubt," held that each payment under the maintenance contracts constituted a "sale" under § 10(b). The court relied on what it expressed as an impressive analogy to SEC rule 136, which deals with assessable stock. The maintenance payments, the court analogized, could be viewed as charges which, like assessments, the purchasers were not obligated to pay because the maintenance contracts were cancellable by the investor prior to the due date of any payment. The court, to avoid resting solely on the analogy to rule 136, discussed two similar cases involving periodic payments. The court stated:

The crux of those decisions, as we read them, is that plaintiffs' right to continue purchasing the installments on their contracts, or to cancel at their

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50 Id. at 1049-51.
52 Id. at 1182-83.
53 id.
54 Rule 136, promulgated under the Securities Act of 1933 provides, in pertinent part:
   (a) An "offer," "offer to sell" or "offer for sale" of securities shall be deemed to be made to the holders of assessable stock of a corporation when such corporation shall give notice of an assessment to the holders of such assessable stock. A "sale" shall be deemed to occur when a stockholder shall pay or agree to pay all or any part of such an assessment.
   (c) The term "assessable stock" means stock which is subject to resale by the issuer pursuant to statute or otherwise in the event of a failure of the holder of such stock to pay any assessment levied thereon.
55 The cases discussed were SEC v. North Am. Fin. (see note 42 supra and accompanying text) and Gross v. Independence Shares Corp., 36 F. Supp. 541 (E.D. Pa. 1941) (which held that each monthly payment under a "contract certificate" cancellable at any time by the investor was a purchase of an interest in a security within the meaning of § 2(3) of the Securities Act of 1933).
option, amounted to a series of investment decisions to purchase (with a corresponding increase in their equity in the issuer) and, accordingly, a series of sales by the issuer. The contracts were executory, or open, and in practical effect they involved the same sort of investment choice as, for example, the decision to purchase monthly 100 shares of General Motors stock (or, more true to life, one share per month).  

The Ingenito court, however, viewed promissory note payments in a different light. The purchasers of cattle investment contracts received certificates of ownership of their cattle at the time of the original transaction in exchange for promissory notes which called for installment payments. The court found that

[i]nsofar as the animals taken alone represented a § 2(3) "interest in a security," the interest was purchased at the time of the initial sale and the rights and obligations of the parties were fixed at the time of the making of the note. Each payment represented not the creation or assumption of new obligations, but the fulfillment of those previously created. There is a substantial economic and legal difference between the note payments and the maintenance payments. Each payment on a maintenance contract represented a fresh decision to further invest in Black Watch; the herdowner "bought" something each month which he did not own before which, by virtue of the cancellation clause, he was not obligated to buy. The same is not true of the note payments.

Thus, on close examination of the cases leading up to Goodman, the courts support the proposition that the time of purchase or sale of a security is that time at which the parties have become irrevocably obligated to the consummation of the transaction. Cases such as North American Finance, Kormel and Ingenito, which find periodic payments pursuant to a contractual agreement to be separate purchases or sales, rely on the fact that the plaintiffs in each of these cases had a contractual option to performance and, therefore, had a remaining "investment decision" at each payment. In other words, the plaintiffs in these cases were not committed to making the periodic payments.

IV. "Purchase or Sale" in Goodman v. Epstein

Distinguishing Goodman from the situation in Radiation Dynamics, the Seventh Circuit in Goodman seized on the available "legal alternative" to performance under the agreement, not available to the plaintiff in Radiation Dynamics. This alternative required the investors in Goodman to make an "investment decision" each time they made a capital contribution.

The Seventh Circuit emphasized that the contract between the parties in Radiation Dynamics contemplated no continuing relationship and that the seller in that case was bound to perform whether or not he acquired the information regarding merger. In contrast, the court viewed the partners in Goodman as having contemplated a continued relationship requiring an investment decision to be made by the limited partners as to their "legal alternatives" each time a
capital call was made. As stated by the court, the “legal alternatives” were:

A limited partner could (claim the investors): (1) comply with the
call; (2) abandon the project; (3) sell his limited partnership interest;
(4) if he had any information tending to demonstrate fraud by the General
Partners, refuse to contribute the called-for capital and defend against
the General Partners' suit (if, indeed, one was brought) on the basis of
breach of the Limited Partnership Agreement by the General Partners;
(5) file for a declaratory judgment ending his obligations to the Limited
Partnership; or (6) file an action to dissolve the partnership and seek a
return of prior contributions. 58

The Seventh Circuit, citing Sundstrand, emphasized that Goodman was not
the first time it found the critical fact to be whether an “investment decision”
remained to be made by a party from whom information was withheld. The
Goodman court, reading its earlier opinion, stated: “... Sundstrand could have
avoided the final payment—(the court) determined that Sundstrand had had a
legal alternative which it could have exercised.” 59

The test selected, and properly so, by the Seventh Circuit in Goodman to
determine the time of “commitment” was whether an “investment decision”
could be made each time there was a capital call. The absence of a remaining
“investment decision” would signal “commitment.” The criterion used by the
Seventh Circuit to determine if an “investment decision” remained was whether
the limited partners had a “legal alternative which [they] could have exercised.” 60
The absence of an available “legal alternative” would signal that no “investment
decision” remained.

The Goodman court placed great weight upon the fact that the limited
partners, like the plaintiffs in Sundstrand, had a legal alternative to performance.
However, even though the Seventh Circuit chose to draw an analogy between
options available 61 to the limited partners in Goodman and the contractual stock
option available to the plaintiff in Sundstrand, they are in fact very dissimilar.

It is apparent that the choice to exercise the right given the purchasing party
in Sundstrand through the stock option involved an “investment decision.” To
say, however, that the limited partners in Goodman had “legal alternatives”
similar to the contractual option in Sundstrand stretches the facts of both cases.

The partners in Goodman became committed to the limited partnership
when they all signed the agreement in late June of 1972. From that time
forward, the limited partners had obligated themselves to furnish at least $3
million in capital which could have been called for at any time. 62 It was prior
to the signing of this agreement, which did not provide a contractual alternative
to contribution when capital was called for, that the limited partners should have
evaluated the risks and merits of their prospective investments and determined
their ability to bear the total investment risk. It was also at this time, prior to the

58 582 F.2d at 398.
59 Id. at 413, 414.
60 Id. (emphasis deleted).
61 See text accompanying note 58 supra.
62 See note 8 supra.
execution of the agreement, that the potential investors should have been provided with the same information that would be required on a securities registration statement.\textsuperscript{63}

None of the "legal alternatives"\textsuperscript{64} which the limited partners listed to support their theory that an "investment decision" remained to be made at each capital call, the theory adopted by the Seventh Circuit,\textsuperscript{65} were provided for in the agreement. The list of "legal alternatives," when analyzed, provides basically for three possible paths of action on the part of the limited partners when faced with a capital call. First, a limited partner could comply with each capital call; second, he could sell his limited partnership interest; or third, the limited partner could seek judicial relief from the agreement while at the same time subjecting himself to a possible lawsuit for breach of the partnership agreement.

Thus, the first way a limited partner could have reacted to a capital call was to respond to it. This was the only way to assure fulfillment of the contractual commitment. The second alternative available, sale of the limited partnership interest, was more academic than real. Although the partnership agreement provided that "[t]he transferee shall be a limited partner to the extent of the partnership interest transferred or encumbered," there might be some question whether these transferees would hold limited partnership status.\textsuperscript{66}

The court, analyzing the third alleged alternative, judicial relief, placed emphasis upon the limited partners' awareness "of their ability to bring about dissolution of the partnership if it could not be operated profitably, Ill. Rev. Stat. ch. 106½ § 32(1) (c)...."\textsuperscript{67} The ability of a party to bring suit in lieu of performance under a contract, however, is not unique to this situation, and it is not accurate to say that seeking a judicial remedy is an option within the scope of an "investment decision." The conclusion to be drawn from this type of analysis is that every case involving a delay in performance following contractual commitment would present the "legal option" of litigation in lieu of performance.

By holding each capital contribution to be a separate "purchase" the Seventh Circuit also introduced some practical problems. The court did not clarify whether it intended each contribution to be a "purchase" for the purposes of the Securities Act of 1933 or whether it intended to extend this rather broad interpretation for § 10(b) and rule 10b-5 purposes only. This uncertainty exists because the court put substantial weight on its analogy to assessable stock. The time of sale of such stock is provided for in SEC rule 136(a), a rule promulgated under the 1933 Act. If each contribution is a separate "purchase" for purposes

\textsuperscript{64} See text accompanying note 58 supra.
\textsuperscript{65} 582 F.2d at 414.
\textsuperscript{66} Id. at 392 n. 10.
\textsuperscript{67} Id. at 413. The Illinois statute provides, in pertinent part:

(1) On application by or for a partner the court shall decree a dissolution whenever:

(c) A partner has been guilty of such conduct as tends to affect prejudicially the carrying on of the business,

(d) A partner wilfully or persistently commits a breach of the partnership or agreement, or otherwise so conducts himself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him,

(e) The business of the partnership can only be carried on at a loss,

(f) Other circumstances render a dissolution equitable.

\textit{ILL. REV. STAT. ch. 106½ § 32 (1975).}
of the 1933 Act, then the issuers would have to establish a "private offerings" exemption under § 4(2) of the 1933 Act to avoid registering the security. Further, if the limited partnership interests did not qualify as a "private offering" and had to be registered pursuant to § 5 of the 1933 Act, it follows that at each contribution a new filing would have to be made with the SEC, a burden that could prove to be quite expensive.

The Seventh Circuit, to buttress its argument, referred to two of its prior decisions in which the availability of a "legal alternative" was a deciding factor. In Wright v. Heizer Corp., the court held that the power of shareholders under state law to veto an amendment to a corporate charter was a sufficient choice to establish the fact that the shareholders had relied on material omissions prior to their approval of the amendments. There is a crucial difference between the shareholders' option to veto certain amendments in Wright, and the limited partners' "legal alternative" of seeking judicial relief in Goodman. The right to veto gave the shareholders in Wright a free choice; however, the limited partners in Goodman would subject themselves to substantial risk of being sued for breach of contract if they attempted to seek judicial relief from compliance with a capital call.

In the second case, Daniel v. International Brotherhood of Teamsters, the court found that the ability to vote down a pension plan or withhold services from the local fund was a sufficient "legal alternative" to render compulsory contributions to the pension fund a "purchase or sale." Thus, in both Wright and Daniel, the rights of the investors lay within their contracts. In Goodman, however, the limited partners did not have the contractual right not to comply with capital calls.

Finally, to support its conclusion, the court spoke of SEC rule 136 as lending support to its holding. The analogy, although having some surface appeal, stands on weak footings. The weakness of the analogy to the irrevocable obligation of the limited partners in Goodman becomes evident by reading one of the court's own sentences, which states: "The stockholder is, of course, 'committed' to meet the assessment call; but his option to return the stock [pursuant to Rule 136(c)] to the issuer in lieu of meeting the assessment requires an investment decision on his part." Thus, the purchaser of assessable stock is only "committed" to decide whether or not he will meet the assessment, unlike the limited partners in Goodman who were not afforded an option similar to that available under rule 136(c).

V. Conclusion

The Seventh Circuit has made a rather liberal extension of the concept of

68 560 F.2d 236 (7th Cir. 1977), cert. denied, 434 U.S. 1066 (1978).
69 Id. at 250.
70 561 F.2d 1223 (7th Cir. 1977), cert. granted, 434 U.S. 1061 (1978).
71 Id. at 1243. It should be noted, however, that the Supreme Court, which has been recently limiting the reach of the federal antifraud provisions, has granted certiorari to this case. See note 70 supra.
72 For text of rule see note 54 supra.
73 582 F.2d 414.
“purchase or sale” on the theory that § 10(b) and rule 10b-5 are to have broad and liberal applicability. Although courts in the past have given broad protection under these antifraud provisions, a binding limited partnership agreement to contribute capital should be treated as possessing a great degree of finality. The goal of securities regulation, as stated previously by the Seventh Circuit in *Sundstrand*, is “to achieve fundamental fairness in the marketplace.” But the scope of the securities laws is not infinite. Section 10(b) and rule 10b-5 cover fraud in connection with “purchases” or “sales” of securities, they do not, and were not designed to, reach all instances of fraud.

To have held that each capital contribution was not a separate “purchase,” and therefore not each time trigger the protection of § 10(b), would not deprive the limited partners of all possibility for protection and recovery. The limited partners could, and in fact did, seek relief by bringing an action for common law fraud or breach of fiduciary obligation, causes of action on which the general partners prevailed in *Goodman*. Moreover, additional proof of fraudulent concealment would have equitably tolled the running of the statute of limitations with respect to any § 10(b) cause of action arising at the time of execution of the partnership agreement.

The Seventh Circuit in *Goodman* should have concluded that the trial judge’s instruction stating “[that] each subsequent capital contribution made pursuant to such an agreement does not constitute a purchase of a security” was a correct statement of the law given these facts. The only “purchase” of a security should have been found to have taken place at the time that the agreement was signed. After the signing, the limited partners did not have the freedom to make any more “investment decisions” within the plain meaning of the words; holding otherwise deviates from earlier case law. The limited partners’ claim under Count I, therefore, should have been barred by the three-year statute of limitations. To have so held would have been in line with the current Supreme Court trend to give a narrow reading to the terms and phrases of the federal anti-fraud provisions and would have given greater finality to contractual commitment.

*Thomas P. Powers*

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74 553 F.2d at 1050.
75 582 F.2d 390.
76 See note 29 *supra.*

First Wisconsin Mtg. Trust v. First-Wisconsin Corp.*

In exercising its broad discretionary power to supervise the conduct of attorneys appearing before it, the Seventh Circuit in *First Wisconsin Mtg. Trust v. First Wisconsin Corp.* considered the novel question whether counsel who have been disqualified for prior simultaneous representation of both parties to a controversy may properly turn over to substitute counsel their work product generated prior to the order for disqualification. The Seventh Circuit concluded that absent a showing of a "reasonable possibility" that confidential information would be passed through the work product, access to the work of former counsel by new counsel should not be denied. In reaching this conclusion the court rejected the position adopted by the dissent that once an attorney is disqualified it should be presumed that the work product is tainted with confidential information.

The Seventh Circuit was confronted with a difficult issue of first impression. The few relevant decisions to consider presdisqualification work product gave little analysis or guidance. In view of these facts, it is not surprising that the Seventh Circuit was strongly divided on the proper outcome of *First Wisconsin*. The court attempted to devise a holding that would have the least detrimental practical impact on the administration of justice and the parties involved. As a result, the majority failed to adequately consider the issue, and a vociferous dissent legitimately criticized the holding as ignoring the ethical considerations relevant to the decision. This comment will consider the two divergent approaches given in *First Wisconsin* in light of the ethical principles involved in granting access to predisqualification work product.

Plaintiff in *First Wisconsin* is a real estate investment trust ("Trust") established in 1971 under the sponsorship of defendant First Wisconsin Corporation. Plaintiff Trust was jointly involved in various investments with and advised by two subsidiaries of First Wisconsin Corporation, both also named as defendants.

The law firm of Foley & Lardner served as general counsel to the Trust, First Wisconsin Corporation and its subsidiaries from 1971 until September, 1974, when it withdrew as counsel for the Trust following a dispute concerning problem loans. Trust hired special counsel in February, 1974, and filed suit in

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1 Fred Weber, Inc. v. Shell Oil Co., 566 F.2d 602, 605 (8th Cir. 1977); Schloetter v. Railoc of Indiana, Inc., 546 F.2d 706, 710 (7th Cir. 1976); Hull v. Celanese Corp., 513 F.2d 568, 571 (2d Cir. 1975).
2 The term "work product" was used throughout the litigation to refer to the written work prepared by the attorneys for defendant. No. 77-1786, slip op. at 2 n.1. Hickman v. Taylor, 329 U.S. 495 (1947), developed extensive rules concerning work product in the context of discovery. Hickman is to be distinguished from *First Wisconsin* in which plaintiff is attempting to prevent turnover of the work product from defendants' former attorneys to their new counsel.
3 No. 77-1786, slip op. at 16, 31.
4 See text accompanying note 22 infra.
March, 1975, claiming that defendants had violated certain sections of the federal securities laws and regulations. After commencing the action, Trust refused to consent to the continued representation of defendants by Foley & Lardner, and moved on August 4, 1975, to disqualify defense counsel. The motion was granted 15 months later on November 16, 1976. Following disqualification of their attorneys, defendants, through substitute counsel, moved for authorization to request access to the work product generated by Foley & Lardner prior to disqualification. The defendants requested the "written work product, consisting essentially of summaries of loan files relating to more than 300 complex transactions, and an explanation limited to an identification of the documents reviewed." This work product, prepared in anticipation of litigation by 15 attorneys throughout 1974 and early 1975, was the result of "routine lawyer work of a type which any competent lawyer . . . could accomplish. . . ." The motion for access to the work product was denied, and defendants appealed. After an initial determination by the Seventh Circuit that it had jurisdiction to consider the appeal, a divided three-judge panel affirmed the district court order. A rehearing en banc was granted and the decision of the panel was reversed.

I. First Wisconsin Majority

For a clear perspective of the impact of First Wisconsin, it is necessary to note that the disqualification of Foley & Lardner was not questioned by the Seventh Circuit because the issue was not properly before it. In its limited examination of the propriety of allowing access to the work product of former counsel, the First Wisconsin majority began by emphasizing the routine nature of the work product in question. Relying on this routine nature of the work, the six-judge majority unquestioningly accepted "the defendants' assertion that the preparation of the loan file summaries was not aided by any confidential infor-

5 Plaintiff's complaint alleged failure to disclose material information relating to plaintiff's investments and breach of contractual and fiduciary duties by defendants. No. 77-1786, slip op. at 32 (dissent).
7 Substitute counsel initially filed a notice of appeal of the disqualification order and requested a pretrial conference to discuss defendants' access to the work product generated by Foley & Lardner prior to disqualification. The appeal was dismissed voluntarily by defendants after the district court declined to hold the pretrial conference on grounds that it had been deprived of jurisdiction due to filing of the notice of appeal. No. 77-1786, slip op. at 5-4.
8 Id. at 5.
9 Id.
12 571 F.2d 390 (7th Cir. 1978).
13 See note 7 supra.
14 The majority opinion was supported by Fairchild, C.J., and Swygert, Pell, Tone, Bauer, and Wood, J.J.
information acquired by the Foley lawyers through their prior relationship with Trust."

Once it had concluded that no confidential information was involved, the court began a piecemeal justification for reversal. The court dwelled primarily on the undesirable results which would occur if it was presumed that the work product was tainted with confidential information once an attorney is disqualified.

It would destroy the work done by disqualified counsel, irrespective of any fault on the part of the party for whom the work was done;

It would do this regardless of whether the work destroyed involved the use of any confidential information obtained from the complaining party;

It would foreclose trial courts from any exercise of discretion in determining what effect an order of disqualification should have upon the parties to litigation, for it creates a per se rule whose effect is automatic and unqualified once an order of disqualification is entered, regardless of the circumstances giving rise to the disqualification and regardless of the extent to which the complaining party may have caused the work in question to be done;

It would seriously impede the administration of justice, because the rationale of the decision applies to all work done by disqualified counsel, and for all practical purposes it would impose a moratorium upon trial preparation for such period of time as it might take to rule upon a motion for disqualification;

It would do a major injustice to the clients of disqualified counsel, causing them to pay a second time for the same work;

It would encourage the public in its dissatisfaction with the expense and delay involved in the administration of the judicial system;

It would provide no benefit to the complaining party other than the satisfaction of imposing an unnecessary financial burden on its opponent;

It would in no way discipline disqualified counsel whose actions have been the cause of the disqualification order.

Only in an addendum to their decision did the Seventh Circuit majority finally offer some guidance to the district courts who are charged with determining whether the work product reflects confidential information. The court adopted the general test offered by the dissent of "whether there exists a reasonable possibility of confidential information being used in the formation of, or being passed to substitute counsel through, the work product in question." The burden of proof would be on the movant to indicate whether such a possibility exists. To protect any confidential information contained in the work product, the court could proceed on an in camera basis if necessary. In defense of its conclusion that no confidential information was reflected in the Foley work, the court cited plaintiff's concession that no confidential information in the evidential sense had been used.

Throughout the majority opinion, the court made no specific reference to

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15 No. 77-1786, slip op. at 5.
16 Id. at 14-15.
17 Id. at 16. While the dissent offered this general test, it applied it by use of a presumption that the work product reflected confidential information. Id. at 26, 31.
18 Id. at 17.
the ABA Code of Professional Responsibility (CPR). The opinion, however, was not completely devoid of sensitivity to the need for high professional standards of conduct. In applying the reasonable possibility test, the court urged an *ad hoc* determination of whether there is “taint of confidentiality or other improper advantage gained from the dual representation.” Yet, without explanation, the *First Wisconsin* majority never allowed plaintiff the opportunity to demonstrate “other improper advantage” which might occur from turnover of the Foley work. Plaintiff Trust realized that it had not been allowed to apply the *First Wisconsin* test, and brought a Petition for Rehearing En Banc and Modification of the Mandate, requesting the court to remand to the district court for findings of fact concerning the actual existence of other impropriety. The petition was denied without comment by the Seventh Circuit.

II. *First Wisconsin* Dissent

The three-judge dissent recognized the serious flaw in the majority holding: reversal was not in compliance with the *ad hoc* appraisal urged by the majority. The holding was also challenged as unworkable because of the time and judicial resources required for *ad hoc* appraisal, the absence of adequate guidance to lower courts, and most importantly, the reversal of the burden of proof. The majority view was attacked as being ethnically improper. Support for this contention was derived from the CPR.

Canon 4 states, “A Lawyer Should Preserve the Confidences and Secrets of a Client.” The dissent concluded that this command applies with equal force to both the work product of an attorney and the person himself. This is true because the work possesses the potential for being the vehicle used to reveal confidential information obtained prior to disqualification. It is, however, in the application of Canon 4 to the work product that the tension between the majority and dissent views becomes apparent. The dissent urged that Canon 4 be applied to work product in the same manner that it is applied to disqualification: once it is demonstrated that a former attorney-client relationship existed between counsel and the complainant, and that there was a substantial relationship between the former and current representations, it should be presumed that confidential information is reflected in the work product. In defense of this presumption, the dissent stated that the rule would not be a *per se* denial of the work product. For example, if the work product was generated prior to the hiring of a new attorney who at one time had represented the opponent in a matter substantially related to the current suit, it would be obvious that there would be no possibility that the work reflected confidential information. However, such exceptions would be rare, and the practical effect of the dissent approach would be a *per se* exclusion of the work product.

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19 *Id.* at 16 (emphasis in original).
21 The dissenting opinion was supported by Castle, Senior J., and Cummings and Sprecher, J.J.
22 *See* note 27 infra.
23 No. 77-1786, slip op. at 30.
The dissent further supported use of a presumption by its analysis of the facts of *First Wisconsin*. Without any deliberate impropriety, it is possible, claimed the dissent, for the work product to include special emphasis of certain loan transactions. Such emphasis might not be apparent to an outsider, such as a judge in an *in camera* inspection, who is under time pressure and unable to examine carefully minute details of the work product.

The dissent did not rest its case with Canon 4. Rather, it turned to the generic command of Canon 9 that, "A Lawyer Should Avoid Even the Appearance of Professional Impropriety." It is possible that not only the attorney himself, but also the attorney's work product, might give an appearance of impropriety. The dissent concluded that such an appearance was cast by use of the work product in *First Wisconsin* because the average person would not distinguish between the work product and the attorney, and the consequent loss of public trust would outweigh any harm which might come to the defendants.24

Responding point by point to the majority's list of practical effects that would occur with use of a presumption that confidential information was reflected in the work, the dissent claimed that: there is some indication of fault on the part of defendants in their urging Foley to continue work despite knowledge of possible conflict; the proper test is the possibility of confidences being used or revealed; no *per se* rules are advocated; the extent to which plaintiff caused creation of the work product is a matter for the district court to judge; the moratorium argument is unpersuasive because defendants were aware of the possibility of loss of the work product; expediency should not override ethical standards; defendants' hardship does not outweigh plaintiff's detriment in having to litigate against secret materials; and the dissent position encourages the public to fully confide in their attorneys.25

III. Application of Canons 4 and 9 to *First Wisconsin*

It is obvious that proper conduct should be encouraged, even at the sacrifice of smooth administration of justice. When unsure about what constitutes proper conduct, courts should resolve all doubts in favor of more careful enforcement of ethical rules.26 This maxim is a helpful guide, but it does not indicate at what point doubts become so relatively unimportant that the application of these ethical rules will be more harmful to the litigants than it will be beneficial to the legal community. Courts can only instinctively grope for the answer. The ethical canons of the CPR, however, provide a proper starting point.

A. Canon 4

1. Application to Disqualification

Canon 4 is commonly applied to disqualification through use of the "substantial relationship test."27 Under this test, once an attorney-client relationship...
between counsel and the adverse party is shown to have existed, the attorney will be disqualified if the current suit involves matters substantially related to the issues of the prior representation. Most courts hold that no breach of confidence need be demonstrated to justify disqualification, and they will presume that confidential information was revealed to the attorney. The reason advanced for this presumption is that requiring a former client to prove that confidential information was involved in the attorney-client relationship creates a danger of disclosure of the very confidences sought to be protected. Because disqualification and the question of access to predisqualification work product are so closely linked, the issue raised by Canon 4 is whether, in its application, the presumption that confidential information was involved in the former attorney-client relationship should also be used to presume that confidential information taints the work product.

2. Application to Work Product and First Wisconsin

The scope of the protection of Canon 4 clearly is broader than the First Wisconsin majority recognized. Although grounded in the attorney-client relationship, the Canon includes more than the attorney-client evidentiary privilege:

"Confidence" refers to information protected by the attorney-client privilege under applicable law, and "secret" refers to other information gained in the professional relationship that the client has requested be held inviolate or the disclosure of which would be embarrassing or would likely to be detrimental to the client.

The acknowledgement by plaintiff Trust that no confidential information in the evidentiary sense had been used was a limited concession. Because Foley & Lardner had represented plaintiff and defendant jointly before suit was filed, there were no "confidences" given to the attorneys which were not simultaneously given to defendants.

The majority hinted that secrets might be a factor in denying work product to new counsel by holding that courts should look for "taint of confidentiality or other improper advantage." However, no specific mention of secrets was made. This failure to adequately consider possible secrets is an indication that,


32 No. 77-1786, slip op. at 17.

at least in *First Wisconsin*, the court thought secrets not to be worthy of stringent protection. This view is not without some logical support. Examples given by the dissent of possible secrets included knowledge by Foley & Lardner's attorneys of the Trust's reaction to certain loans, and possible unconscious emphasis on certain transactions in the loan file summaries. However, even if Foley & Lardner had withdrawn as attorney for both parties at the first sign of conflict, defendants could have indicated these *secrets* to their new counsel because, just as with *confidences*, this information was also available to the defendants.

However, the mere fact that both the confidences and secrets of plaintiff Trust were also known to defendants does not solve any ethical problem raised in *First Wisconsin*. The CPR, ethical canon 4-4, states that the ethical obligation of a lawyer to guard the confidences and secrets of his client, "unlike the evidentiary privilege, exists without regard to the nature or source of the information or the fact that others share the knowledge." This canon would not have prevented Foley & Lardner from making all information known to both plaintiff and defendant *during* the joint representation. However, the Canon appears to apply where the attorney has withdrawn from joint representation. Therefore, despite availability of the information during the period of joint representation, the test of whether there exists a reasonable possibility of confidences and secrets being reflected in the work product still applies. The availability of the information is a factor to be considered when determining propriety of work product turnover, for a balancing of potential harm to the parties is not foreclosed in the Canon 4 analysis. The *First Wisconsin* court should have remanded the case to allow plaintiff the opportunity to demonstrate possible confidences and secrets.

B. Canon 9

1. Application to Disqualification

Canon 9 admonishes an attorney to avoid even the appearance of professional impropriety. It is now clear that counsel may be disqualified solely on these grounds. This "appearance of evil" doctrine is designed to effectuate the goal of maintaining public confidence in the legal system. Laypersons and lawyers alike acknowledge that confidence in both the law and lawyers may be eroded by conduct which appears improper although it may be of borderline propriety. For this reason, courts often state that an attorney's conduct "should not be weighed with hairsplitting nicety." It is possible that even if Canon 4 is not threatened by the work product turnover, the work could give such an appear-

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34 No. 77-1786, slip op. at 37 n.15.
ance of impropriety that denial would be justified. This issue can be decided only by looking to the facts of *First Wisconsin*.

2. Application to Work Product and *First Wisconsin*

As noted by the three-judge panel before *en banc* reversal, the essence of an attorney's representation is his or her "mental impressions, conclusions, opinions or legal theories." The court continued, "[t]o say that a lawyer's physical presence gives the appearance of impropriety while the use of his work product does not is to immerse oneself in the same 'hair-splitting niceties' which properly have been condemned in the enforcement of ethical standards."

Yet, the work product remains one step removed from the actual presence of the attorney. It may capsulize one particular point or issue without the full reflection or explanation possible when the attorney is present and actively representing the client. Whether this distinction is sufficient to erase an appearance of impropriety depends on how the public sees the work product. In *First Wisconsin*, neither pleadings nor answers to interrogatories were questioned by the court as appearing improper to the general public. If these documents, an acknowledged and highly visible work product, do not give an appearance of impropriety, it is difficult to justify a presumption that all other types of work will give such an appearance.

The *First Wisconsin* dissent proposed a balancing test, stating that "we must ask whether reasonable members of the public would view access to predisqualification work product as being improper, and, if so, whether the benefit of permitting such access outweighs the harm to the public trust." In order to incorporate the public scrutiny spirit of Canon 9 into this test, it is also necessary to consider how the public would view the economic and strategic impact of denial of work product on the parties. A per se denial of access to the work product could "encourage the public in its dissatisfaction with the expense and delay involved in the administration of the judicial system." The public could easily interpret such a rule as being merely another tactic on the part of the legal community to create more work for themselves. Protection of the values inherent in Canon 9 requires a broad reading of the balancing test, with consideration of both the work product and the previous representation. This flexible rule would preserve the high value placed on the appearance of proper conduct without damage from overzealous ethical fervor. Canon 9, like Canon 4, requires discretion on the part of the trial court judge, for no rule of certitude could accomplish the purpose of Canon 9—to maintain confidence in the legal system.

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38 571 F.2d at 397 (quoting 329 U.S. at 508, 511).
39 Id.
40 Pleadings and other documents were discussed by the dissent in reference to Canon 4. The dissent distinguished such documents from the general work product because of their public access. Id. at 30-31 n.8. Ease of inspection would not appear to mitigate the appearance of impropriety under Canon 9, should it exist.
41 Id. at 38.
42 Id. at 15.
43 At least one court has acknowledged the practical detrimental effect of overcompensating for the deteriorating public image. 370 F. Supp. at 591. See Note, Ethical Considerations When an Attorney Opposes a Former Client: The Need for a Realistic Appraisal of Canon 9, 52 CHI.-KENT L. REV. 525 (1975).
IV. Impact of First Wisconsin

A. Burden of Proof

Although the First Wisconsin majority gave an incomplete analysis of the issue, its holding provides adequate protection to confidences and secrets under the instant facts. A shift in the burden of proof to require the movant to demonstrate a reasonable possibility that confidences and secrets are involved in the work product is a workable device only by careful application. The First Wisconsin opinion can be interpreted to say that once the disqualification order has been entered, the court will examine the record to determine if there is an independent basis for an inference that confidential information had been used in preparation of the work product. If such an inference can be drawn from the facts, new counsel may attempt rebuttal. Only if rebuttal is successful must the former client establish a reasonable possibility that confidential information was used. Disclosure of the actual confidences and secrets is not required where the inference from the record is not rebutted. Where disclosure is required, in camera proceedings will protect the material discussed. Through a strict application of the reasonable possibility test, the necessity of in camera review would be infrequent, thereby alleviating the fear expressed by the dissent that such a review would be unworkable because it requires excessive amounts of judicial time.

B. Cooperation of the Courts

It is apparent from the dearth of cases on point that litigants have seldom questioned whether the work product should be turned over to substitute counsel. Now that litigants are aware that work product may be denied if the

44 Courts should not follow the example given by the Seventh Circuit in First Wisconsin. See text accompanying note 20 supra.

45 No. 77-1786, slip op. at 7. The court stated:

No doubt it will frequently be that the lawyer who is unfortunate enough to become involved in the Goodwin Sands of simultaneously representing clients whose interests either are or thereafter come into conflict, and who ceases representation of one of the clients, will find that the work performed during the period subject to disqualification will have aspects of confidentiality or other unfair detriment to the former client arising from the very fact of the knowledge and acquaintance acquired during the period of the prior representation. This does not mean, however, that this is always the situation, or even that it is frequently so.

46 Id. (emphasis added).

47 Id. at 16.

48 Id.

49 Only three cases cited by the litigants directly considered the question of access to predisqualification work product, and none of them had any difficulty in justifying work product turnover. IBM Corp. v. Levin, 579 F.2d 271 (3rd Cir. 1978) ; E. F. Hutton & Co. v. Brown, 305 F. Supp. 371; Allied Rlty. of St. Paul, Inc. v. Exch. Nat. Bank of Chic., 408 F.2d 1099 (8th Cir. 1969), cert. denied sub nom., Abramson v. Exch. Nat. Bank of Chic., 396 U.S. 823 (1969). IBM involved simultaneous representation of both plaintiff and defendant in unrelated matters, a violation of Canon 5. There was no question of confidential information being involved, and the court held that disqualification was sufficient “vindication of the integrity of the bar.” In Hutton counsel for plaintiff was disqualified in a suit by a corporation against a
attorney is disqualified for a Canon 4 violation, courts must be increasingly aware that motions for disqualification and subsequent work product denial may be used as a trial tactic. For example, the movant may submit excessive discovery requests to his or her opponent which properly could be postponed until the motion for disqualification is acted upon. Without some control by the court, the moving party may encourage this artificial buildup of the work product to the detriment of the nonmoving party should the work product be denied.

Inherent delays in the legal system compound the problem, as evidenced by the 15-month delay between submission of the motion to disqualify in First Wisconsin and the disqualification order by the court. Courts should attempt to give a prompt response to a motion to disqualify, in order to minimize lost time should access to the work product be denied. Harmful effects from the First Wisconsin holding will be avoided only through full cooperation from the courts.

V. Conclusion

The Seventh Circuit in First Wisconsin formulated a correct standard for determining the propriety of predisqualification work product turnover by examining the facts of the case to determine whether there existed a reasonable possibility of confidential information being passed through the work product. The court analyzed the work product independently from the initial disqualification, and did not assume that confidential information was reflected in the Foley & Lardner work. As a consequence, the First Wisconsin decision has shifted the burden of proof to require the party opposing the transfer of work product to demonstrate a possible taint of the work product.

However, in arriving at its conclusion, the court, despite the objection of the dissent, failed to give sufficient weight and thought to Canons 4 and 9. Future courts should note that the Seventh Circuit in First Wisconsin was confronted with an issue of first impression, that it gave an incomplete analysis of the issue, that it did not apply its own standards to the facts of the case, and that the decision was countered by a strong and rational dissent. These factors give First Wisconsin dubious precedential value unless courts are willing to give First Wisconsin a restrictive reading.

First Wisconsin, however, does give warning that courts should be sensitive to the use of motions for disqualification and subsequent denial of work product as simply a trial tactic. Only a sensitive administration of the holding will afford litigants the protection they are due. Courts will be guided correctly if they pause to question whether Canons 4 and 9, so carefully propounded by the American Bar, will be supported by denial of the work product.

Judith A. McMorrow

former vice-president because the firm had represented the vice-president at SEC hearings concerning the matters substantially related to the current suit. Hutton relied on the absence of an attorney-client relationship and the fact that the vice-president knew that any information revealed to the attorneys would be given to the corporation. Disqualification was upheld but the attorney work product was turned over to new counsel for plaintiff. Hutton was distinguished by the dissent as involving factual statements rather than legal analysis of the facts. No. 77-1786, slip op. at 26 n.4. In Allied a former government attorney who had been involved in a related criminal suit against defendants was disqualified from representing plaintiff. The work product, including pleadings, was not excluded. Allied was distinguished by the First Wisconsin dissent as involving material which had already been made public. Id.
Disqualification of Counsel—Attorney-Client Relationship Can Develop Absent the Requirements Needed for the Establishment of an Agency Relationship—Traditional Imputation of Knowledge Rule Applies Regardless of Size or Geographic Scope of Law Firm.


I. Introduction

The basis of all disqualification motions is an alleged ethical transgression. Such motions normally raise three questions: (1) did a violation actually occur? (2) what type of transgression was it? and (3) was the type of violation found of such magnitude that the need to preserve ethical standards outweighs an individual's freedom to choose his own counsel?

Each of these questions arose in Westinghouse Electric Corp. v. Kerr-McGee Corp. Although a seemingly obvious ethical transgression had occurred, the characterization of the violation was dependent on whether an attorney-client relationship existed between the moving parties and the law firm they sought to disqualify. The Seventh Circuit, therefore, had to determine what factors must exist for the development of an attorney-client relationship and whether such a relationship was established here. Once this determination was made, the court could consider whether the violation mandated affirmation of the disqualification motion. An analysis of the Seventh Circuit's reasoning on these questions, with strict attention paid to the underlying facts of the case, forms the basis of this comment.

II. Statement of Facts

Westinghouse is an appeal of the district court's denial of a disqualification motion made by four named defendants.¹ To fully understand this complex case, some historical background is required. On September 8, 1975, Westinghouse, a major producer of nuclear reactors, notified a number of utility companies that it would not fulfill existing uranium supply contracts. Because the price of uranium had increased substantially, Westinghouse claimed that the contracts had become commercially impracticable under § 2-615 of the Uniform Commercial Code,²

¹ The four named defendants referred to are Gulf Oil Corp. (Gulf), Kerr-McGee Corp. (Kerr-McGee), Getty Oil Corp. (Getty) and Noranda Mines Limited (Noranda). Gulf Minerals Canada Limited is also a defendant, but for convenience is included within Gulf. See generally 580 F.2d at 1312.

² Noranda's motion for disqualification stems from a claimed conflict of interest different in fact from those alleged by the oil companies. See generally 580 F.2d at 1312. The issues raised by Noranda are not addressed in this comment.

The Uniform Commercial Code § 2-615 states in relevant part:

(a) Delay in delivery or non-delivery in whole or in part by the seller . . . is
thus excusing Westinghouse from performance. In response, all of the utility companies filed breach of contract actions against Westinghouse in various courts. Ancillary to its defense of the above contract actions, Westinghouse filed an antitrust action on October 15, 1976, against 12 foreign and 17 domestic corporations involved in various aspects of the uranium industry. In this complaint, Westinghouse claimed that the defendants had conspired to increase uranium prices. Throughout all phases of this litigation, Westinghouse retained the law firm of Kirkland & Ellis as lead counsel.

Beginning slightly before the alleged breach by Westinghouse and continuing throughout the time of the antitrust litigation, the American Petroleum Institute (API), of which the three principal Westinghouse defendants were dues-paying members, was engaged in an extensive lobbying effort in opposition to legislative proposals seeking to break up oil companies both vertically and horizontally. One facet of this lobbying effort was the creation of a legal task force to conduct studies and legal research "into the implications of divesture and the adequacy of existing laws to keep the industry competitive." One of the recommendations of this task force was that a law firm be retained to conduct an overall review of the subject. On February 25, 1976, Kirkland was retained for this purpose.

In a letter sent from API to Kirkland on May 4, 1976, Kirkland was told that its work should include the preparation of possible testimony, analyzing the probable legal consequences and antitrust considerations of the proposed legislation. As part of the study, we [API] will arrange for interviews by your firm with a cross section of industry personnel. Your firm will, of course, act as an independent expert counsel and hold any company information learned through these interviews in strict confidence, not to be disclosed to any other company, or even to API, except in aggregated or such other form as will preclude identifying the source company with its data.

not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.


4 580 F.2d at 1313. Thirteen suits initiated in various courts have been consolidated for trial in the Federal District Court of Virginia at Richmond under MDL Docket No. 235. Id.

5 Included as defendants in this antitrust action were Gulf, Kerr-McGee, and Getty, the three principal defendants in the case addressed here. Westinghouse Elec. Corp. v. Rio Algom Ltd., 448 F. Supp. 1284 (N.D. Ill. 1978).

6 448 F. Supp. at 1288.

7 Kirkland & Ellis is a two-city law firm with offices in Chicago and Washington, D.C. During the time period in question the Washington office used the name Kirkland, Ellis & Rowe. Kirkland "Chicago" employs approximately 130 attorneys and Kirkland "Washington" employs an additional 40 attorneys. 448 F. Supp. at 1288-89.

8 These defendants are Gulf, Kerr-McGee, and Getty. 580 F.2d at 1314.

9 448 F. Supp. at 1291.

10 Id. Kirkland, Ellis & Rowe was actually retained by American Petroleum Institute (API). Throughout the time in question, Chicago-based attorneys were responsible for the Westinghouse litigation while Washington-based attorneys worked on the API report. Id. at 1305. See generally note 7 supra.

11 580 F.2d at 1313 (emphasis added).
In the weeks that followed, API developed channels through which Kirkland could obtain the confidential information it needed to complete the report.12 Through these channels Kirkland successfully obtained a great deal of information which was publicly unavailable. Kirkland’s final report to API contained 230 pages of text and 82 pages of exhibits. Uranium references appeared throughout the report, and uranium was the primary subject of approximately 25 pages of text and 11 pages of exhibits. The report concluded that “the energy industries, both individually and collectively, are competitive today and are likely to remain so.”13 This final report was released on October 15, 1976, the same day as the Westinghouse antitrust litigation was filed.

A comparison of Kirkland’s API report and the antitrust complaint it filed for Westinghouse reveals a basic conflict. Although Kirkland’s report for API stated that the energy industry in general and the uranium industry in particular were extremely competitive and were likely to remain so for the foreseeable future, Kirkland’s complaint for Westinghouse claimed a complete lack of competition in the uranium industry and hinted at possible collusion among energy producers. In essence, simultaneously inconsistent positions were taken by Kirkland—a contention even Kirkland did not attempt to rebut.14

Kerr-McGee, Getty, and Gulf sought disqualification of Kirkland as counsel in the Westinghouse antitrust action because of Kirkland’s relationship with them and with API in preparation of the antidiversification report.15 The oil companies’ principal assertion was that during the course of Kirkland’s preparation of the API report, they had given confidential industry and market data to Kirkland attorneys. Relying on The American Bar Association Code of Professional Responsibility Canon 4, which requires a lawyer to preserve the confidences and secrets of his client,16 Canon 5, which dictates that an attorney must exercise independent judgment on behalf of his client,17 and Canon 9, which seeks to deter even the appearance of attorney impropriety,18 the oil companies claimed that the simultaneous representation of both API and Westinghouse “create[d] a sub-

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12 See generally 580 F.2d at 1314-16. API sent questionnaires to 59 member-companies directing the recipient to return the answers to Kirkland. In a cover letter accompanying the questionnaire, API explained the need for the requested information and noted that “Kirkland, Ellis & Rowe is acting as an independent special counsel for API, and will hold company information disclosed in strict confidence, not to be disclosed to any other company or even API...” 580 F.2d at 1313-14 (emphasis in the original).

14 Id.

15 Other disqualification motions were presented at the district court level. One involved Noranda, discussed in note 1 supra. Another was made by twelve other corporate defendants to the Westinghouse antitrust action. Their argument centered on the possibility that Gulf, Kerr-McGee, and Getty might be dropped from the case. They claimed this would be prejudicial to their positions. See generally 448 F. Supp. at 1289.

16 ABA Code of Professional Responsibility, Canon 4: “A lawyer should preserve the confidences and secrets of a client.”

17 ABA Code of Professional Responsibility, Canon 5: “A lawyer should exercise independent professional judgment on behalf of a client.”

18 ABA Code of Professional Responsibility, Canon 9: “A lawyer should avoid even the appearance of professional impropriety.”
stantial conflict of interest, a potential for disclosure of confidential information, and the appearance of impropriety.” Because of these violations, the oil companies moved to disqualify the entire Kirkland firm or, in the alternative, to dismiss the oil companies from the antitrust suit. The district court denied the motion to disqualify the firm and the oil companies appealed to the Seventh Circuit.

III. Disqualification as a Remedy for Canon 4 and Canon 5 Violations

A. The Agency Test

The first issue to be determined in Westinghouse was whether an attorney-client relationship had developed between Kirkland and the oil companies. Stressing that such a relationship was one of agency, the district court initially looked for any explicit evidence of an agency relationship. Finding none, the court then searched for any conduct between Kirkland and the oil companies which would imply such a relationship. Again the search was futile. Finally, the court looked for evidence of what it considered to be the three fundamental characteristics of an agency relationship. These characteristics are (1) the power of the agent to affect the legal relations of the principal, (2) the fiduciary relationship existing between the agent and the principal in which the agent works on behalf of and primarily for the benefit of the principal, and (3) the principal's right of control over the acts of the agent. The court held that evidence of these characteristics was insufficient to establish an attorney-client relationship. In addition, the court held that any beliefs the oil companies may have had regarding the existence of such a relationship were irrelevant since agency is a concept dependent upon the manifest conduct of the parties and not their intentions or beliefs. As no agency relationship existed, Canons 4 and 5, which apply solely under the umbrella of such a relationship, accorded no relief to the defendant oil companies.

In reversing the district court, the Seventh Circuit held that the court erred in its “narrow, formal agency approach to determining the attorney-client relation. . . .” The Seventh Circuit, however, promulgated no hard and fast rules to determine when an attorney-client relationship comes into existence. The court did hold that “to apply only the agency tests is too narrow an approach for determining whether a lawyer's fiduciary obligation had arisen.”

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19 448 F. Supp. at 1289.
20 Id. at 1305.
21 Id. at 1300-01.
22 Id. at 1303.
24 The Seventh Circuit reversed the district court's holding that Kirkland could continue as counsel for Westinghouse in the antitrust action regardless of the defendants. The court, however, gave Westinghouse the alternative of dismissing Gulf, Kerr-McGee, and Getty as defendants in the antitrust action in lieu of discharging Kirkland. As Westinghouse had obtained substitute counsel by the time this decision was rendered, it chose to discharge Kirkland. 580 F.2d at 1322.
25 Id. at 1318.
26 Id.
specifically outlined various situations in which an implied attorney-client relationship or fiduciary obligation on the lawyer’s part was found despite the absence of all the characteristics required by the district court’s agency tests. Alluding to the defendants’ reasonable belief that a confidential relationship between themselves and Kirkland had developed, the court held that such a relationship existed, at least for purposes of applying Canons 4 and 5.27

The district court’s holding that “an attorney-client relationship is one of agency to which the general rules of agency apply” and therefore “arises only when the parties have given their consent, either express or implied, to its formation” is not well-supported. Although the district court’s application of an agency theory to the attorney-client relationship has been applied by other courts, no federal court has used an agency principle to allow an attorney to escape what would otherwise be an obligation to his client. A reading of the relevant cases indicates that the agency principle normally has been applied in the attorney-client context either to bind a client to, or relieve him from, actions of his attorney in much the same way that agency principles have been applied when the agent was a layman. Although the attorney-client relationship may possess many of the same traits as an agent-principal relationship, the absence of these traits, either in whole or in part, is not a per se indication that no attorney-client relationship exists.

The one case cited by the district court as support for the agency test approach to the determination of an attorney-client relationship, Committee on Professional Ethics & Griev. v. Johnson, is not conclusive. Johnson, which was a disbarment proceeding, involved an attorney who allegedly was guilty of unethical conduct relating to land dealings. The district court had suspended the

27 Id. at 1321. The Seventh Circuit never actually stated that an attorney-client relationship between Kirkland and the oil companies had developed. Its decision appears to be solely on the applicability of the Canons. Since the court did not refute the district court’s ruling that Canons 4 and 5 are irrelevant in the absence of an attorney-client relationship, however, it can be inferred that the Seventh Circuit found such a relationship existed.
28 448 F. Supp. at 1300.
29 Id.
30 See, e.g., Brinkley v. Farmers Elevator Mut. Ins. Co., 485 F.2d 1283, 1286 (10th Cir. 1973); Blakely v. American Employers’ Ins. Co., 424 F.2d 728, 734 (5th Cir. 1970); Hensley v. United States, 281 F.2d 605, 607 (D.C. Cir. 1960); Rothman v. Wilson, 121 F.2d 1000, 1006 (9th Cir. 1941).

In Brinkley, the agency test was used to deny any liability of an insurance company for injuries received by the plaintiff in an automobile accident with a car driven by an attorney who was returning home after defending the insurance company at a trial some distance from the attorney’s residence. In Blakely, the agency theory was applied to attribute to the client (in this instance, an insurance company) the mistakes made by the client’s attorney while working for the client. In Hensley, a criminal case, an agency theory was utilized to hold the defendant’s waiver of a jury trial valid, even though the waiver in fact had been made by the defendant’s attorney. Finally, in Rothman, the agency theory was applied to allow a layman to recover profits, which were made by the attorney’s acquisition of interests antagonistic to those of the client, from the attorney.

31 One possible exception is Committee on Professional Ethics & Griev. v. Johnson, 447 F.2d 169 (3rd Cir. 1971). For reasons discussed in the text accompanying note 33 infra, the application of the agency principle by federal courts in cases with similar facts may fairly be held as nonexistent.
32 See note 30 supra. In none of these cases was the agency theory utilized to allow the attorney to escape obligations owed to his client.
33 447 F.2d 169 (3rd Cir. 1971).
defendant attorney on two or three separate grounds. Only one of the grounds directly involved a disputed attorney-client relationship. On appeal, the Third Circuit reversed the suspension and remanded the case because of a due process violation. The statement in Johnson, on which the district court in Westinghouse relied, that "[a]n attorney-client relationship is one of agency and arises only when the parties have given their consent, either express or implied, to its formation," thus becomes mere dicta. Further, any comparison between the factual situation in Johnson and that in Westinghouse is pallid by the varying degrees of contact between the attorney and client.

Conversely, the Seventh Circuit's views that an "attorney is held to obligations to the client which go far beyond those of an agent and beyond the principles of agency," and that "attorney-client" fiduciary relationships can develop without the presence of any of the traditional characteristics of an agency relationship, are well supported. Many situations exist in which an implied professional relationship is present despite the lack of any express attorney-client relationship. For example, a professional relationship can arise when a prospective client engages in preliminary consultations with an attorney or when co-defendants and their attorneys exchange information in a criminal case. An attorney-client relationship can also exist when an insurer retains an attorney, and the insured cooperates with the attorney; the attorney may not thereafter represent a third party suing the insured. The fundamental characteristics of an agency relationship required by the district court exist in none of these situations; still, professional relationships governed by the ABA Code of Professional Responsibility can be found.

B. Justification for the Disqualification

Once the existence of a fiduciary relationship between Kirkland and the oil companies was established, the entire ABA Code of Professional Responsibility became applicable. The direct application of Canon 4 and Canon 5 was then decisive on the issue of Kirkland's disqualification.

Canon 4 is designed to preserve a client's trust in his lawyer. In Interna-

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34 Id. at 171. The Third Circuit was unable to determine the number of grounds on which the district court's memorandum decision was based.
35 Id. at 174. The Third Circuit held that the failure to give adequate notice of the charges to the defendant-attorney constituted a blatant due process violation. Id. The issue of agency as it applied to an attorney-client relationship was, therefore, irrelevant to the holding of Johnson.
36 447 F.2d at 174.
37 580 F.2d at 1317.
38 "Both the fiduciary relationship existing between lawyer and client and the proper functioning of the legal system require the preservation by the lawyer of confidences and secrets of one who has employed or sought to employ him." ABA CODE OF PROFESSIONAL RESPONSIBILITY, Canon 4, EC 4-1 (emphasis added). See also Taylor v. Sheldon, 172 Ohio St. 118, 173 N.E.2d 892 (Ohio Sup. Ct. 1961).
41 See note 27 supra.
42 Canon 4 clearly states that an attorney must protect more than the information received from a client which is protected by the attorney-client privilege. Secrets of the client must also be protected. Secrets refer to "other information gained in the professional relationship that the client has requested be held inviolate or the disclosure of which would be embarrassing or
tional Electronics Corp. v. Flanzer, the Second Circuit held that one seeking to employ Canon 4 for disqualification must show not only the presence of an attorney-client relationship, but also a substantial relation between the subject matter of the previous dealings and the current litigation. The party seeking the disqualification need not prove an actual breach of confidence since access to confidential information raises an irrebuttable presumption of disclosure. Since Kirkland did not debate that a substantial relationship between the API report and the Westinghouse antitrust litigation did exist, the International test was met. The Canon 4 violation, premised on the presumption of disclosure, thus permitted the disqualification of Kirkland.

Canon 5 deals with an attorney’s exercise of independent professional judgment. The Canon specifically precludes simultaneous representation of conflicting interests. By representing both Westinghouse and the oil companies, however, Kirkland did simultaneously represent conflicting interests: Kirkland formulated the antitrust complaint for Westinghouse contending collusion in the uranium industry and at the same time prepared a report for the oil companies stating that this same uranium industry was highly competitive and was likely to remain so for the foreseeable future. Because of these conflicting interests, Kirkland violated Canon 5 thus justifying the firm’s disqualification by the Seventh Circuit.

IV. Disqualification as a Remedy for Canon 9 Violation

The failure of the district court to find an attorney-client relationship between Kirkland and the oil companies did not dispose completely of the disqualification motion. Because the oil companies also based their motion on a Canon 9 violation by Kirkland, and because Canon 9 applies “to the entire spectrum of lawyer conduct,” the presence of an attorney-client relationship was not a prerequisite to finding a Canon 9 violation on Kirkland’s part or upholding the disqualification motion.

The district court found evidence of a Canon 9 violation, but was reluctant to disqualify on the basis of Canon 9 itself. Noting that a Canon 9 disqualification usually rests on an infraction of the Canon’s disciplinary rules, the district court found that Kirkland’s apparent impropriety did not violate any Canon 9 disciplinary rules. Rather, the conduct was on the perimeters of ethical transgressions. In these gray areas, the court believed that “a mechanical application

would likely to be detrimental to the client.” ABA Code of Professional Responsibility, Canon 4, DR 4-101 (A). Except in rare cases, an attorney may not reveal these secrets, use them for the advantage of himself, or that of a third party. The same, of course, holds true for confidences. ABA Code of Professional Responsibility, Canon 4, DR 4-101 (B) (1), (2), (3).

43 527 F.2d 1288 (2d Cir. 1975).
44 Id. at 1291. See also American Can Co. v. Citrus Feed Co., 436 F.2d 1125, 1128 (5th Cir. 1971).
45 See In Re Yarn Processing Patent Validity Litigation, 530 F.2d 83, 89 (5th Cir. 1976).
46 See ABA Code of Professional Responsibility, Canon 5, EC 5-14.
47 566 F.2d at 609.
48 448 F. Supp. at 1304.
49 See ABA Code of Professional Responsibility, Canon 9, DR 9-101, DR 9-102. Many courts have been hesitant to use Canon 9 as a tool for disqualification when no such violations have been found. See, e.g., International Electronics Corp. v. Flanzer, 527 F.2d 1288, 1295 (2d Cir. 1975).
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of Canon 9 is to be avoided. . . ." To give pragmatic content to the canon, the
court suggested that "an attorney should be disqualified under Canon 9 only
when 'there is a reasonable possibility of improper professional conduct. . . .'" The
district court therefore examined the conduct of the Kirkland firm to
determine whether it had been improper.

The primary basis for the oil companies' charges of impropriety was the
presumed disclosure of confidential information gathered by Kirkland's Wash-
ington attorneys preparing the API report to Kirkland's Chicago attorneys han-
dling the Westinghouse antitrust litigation. Although imputation of knowledge
between members of the same law firm has been the traditional rule, the district
court noted that "recent decisions [had] occasionally rejected this rigid approach,
in recognition of the changing realities of modern legal practice," and refused
to apply the traditional rule. Once this rule was discarded, most of the ap-
parent impropriety involving Kirkland vanished.

Like the district court, the Seventh Circuit found Canon 9 applicable in
this situation. Unlike the district court, however, the court of appeals believed
that this Canon was a basis for disqualification. Steadfastly adhering to the
traditional rule that actual knowledge of one or more lawyers in a firm is to be
imputed to every member of that firm, the Seventh Circuit gave no judicial
weight to the possibility that Kirkland attorneys working for API had been
completely insulated from Kirkland attorneys handling the Westinghouse case.

Acknowledging the district court's test that "'a reasonable possibility of improper
professional conduct' must exist before an attorney could be disqualified under
Canon 9, the Seventh Circuit found that "there exists a very reasonable possibility
of improper professional conduct despite all efforts to segregate the two sizeable
groups of lawyers." The Kirkland firm was thus disqualified under Canon 9 as
well as under Canons 4 and 5.

The Seventh Circuit was not obligated to address the issue of disqualification
which may result from a "technical" Canon 9 violation or a Canon 9 violation
premised on the imputation of knowledge rule. The district court was forced to
examine this issue because it found no attorney-client relationship. At the ap-
pellate level, however, a determination of the Canon 9 issue was unnecessary
because the Seventh Circuit had already held that an attorney-client relationship
existed between Kirkland and the oil companies, that Canons 4 and 5 had been
violated, and that these violations warranted Kirkland's disqualification.

The Seventh Circuit's discussion relating to imputation of knowledge was
particularly unnecessary. As noted previously, Kirkland is one of the nation's

50 448 F. Supp. at 1304.
51 Id. (citing 537 F.2d at 813 n.12).
52 Id.
53 Id. at 1305.
54 580 F.2d at 1321. In the district court, Kirkland maintained that their Chicago at-
torneys working for Westinghouse and their Washington attorneys working for API had been
sufficiently insulated from each other. 448 F. Supp. at 1305. Whether Kirkland continued
to maintain this position before the Seventh Circuit is unclear. See 580 F.2d at 1321 n.28.
In any event, complete isolation was not achieved. See text accompanying note 59 infra.
55 448 F. Supp. at 1304 (citing 537 F.2d at 813 n.12).
56 580 F.2d at 1321.
57 See notes 7 and 10 supra.
largest law firms with offices in Chicago and Washington, D.C. In *Westinghouse*, the Chicago-based staff handled the antitrust litigation and the Washington office handled the API matter. In theory, the two teams were completely segregated. There was, however, one crack in the "Chinese wall." This break, evidenced by the showing that one Kirkland attorney assigned to the Westinghouse litigation also admittedly prepared a legal memorandum for API, was crucial. Since an actual breach had been proven, the court did not have to rule on the imputation of knowledge issue. Overall, by commenting on the issues raised by the Canon 9 allegation, the Seventh Circuit evidently deemed it necessary to rectify errors in the district court's application of Canon 9.

**A. The "Technical" Violation: Appearance of Impropriety**

The modern case law on the issue of Canon 9 disqualification appears to support the district court's view. Courts which have used transgressions of this Canon as a basis of disqualification have typically done so only when one of the disciplinary rules of Canon 9 has been violated. To allow disqualification simply on the appearance of impropriety opens the door for potential abuse as a court can easily find the appearance of impropriety in many everyday attorney actions. The Seventh Circuit's application of Canon 9 did not follow these precedents. Kirkland violated no Canon 9 disciplinary rules, yet one of the reasons the firm was disqualified was the appearance of impropriety in some of its actions. Such use of the canon gives the practicing attorney little guidance. With no guidelines or boundaries set, he or she may tread into truly proper areas, and only later be informed that the journey was unethical because some steps appeared improper. Although hindsight may clearly show that one's actions took on the appearance of impropriety, whether foresight can give as accurate a view is questionable. As disqualification is detrimental to both the so-designated unethical attorney and the innocent client, "non-particular" Canon 9 disqualification should rarely, if ever, occur. Further, if a court believes such a disqualification is warranted, the court should fully explain its reasoning. In this way, the disqualified attorney and, more importantly, attorneys who face similar problems in the future, will have guidelines for future reference.

Any broader application of Canon 9 may defeat the goal of the Canon itself. As the Fifth Circuit in *Woods v. Covington Cty. Bank*, explained this concept:

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58 580 F.2d at 1321. "Chinese wall" was the term used by the Seventh Circuit to describe Kirkland's attempt to segregate its Washington attorneys from its Chicago attorneys.

59 At least one judge on the Seventh Circuit's three-man panel may have reached a different result in *Westinghouse* if this breach had not been shown. Judge Fairchild states that if it had been established that there was a real insulation in all relevant particulars between the lawyers working in the Washington office on the API report and those working in the Chicago office on the antitrust action, imputation of knowledge to all partners would have been eliminated from consideration in this case. 58 F.2d at 1321 n.28.

60 See, e.g., General Motors Corp. v. City of New York, 501 F.2d 639 (2d Cir. 1974).

61 See note 49 supra.

62 A close reading of the Seventh Circuit's opinion shows Kirkland's disqualification was based not only on the Canon 4 and Canon 5 violations, but also on a Canon 9 transgression. See 580 F.2d at 1321.

63 537 F.2d 804 (5th Cir. 1976).
It does not follow, however, that an attorney's conduct must be governed by standards which can be imputed only to the most cynical members of the public. Inasmuch as attorneys now commonly use disqualification motions for purely strategic purposes, such an extreme approach would often unfairly deny a litigant the counsel of his choosing. Indeed, the more frequently a litigant is delayed or otherwise disadvantaged by the unnecessary disqualification of his lawyer under the appearance of impropriety doctrine, the greater the likelihood of public suspicion of both the bar and the judiciary. An overly broad application of Canon 9, then, would ultimately be self-defeating.64

B. Imputation of Knowledge

The Seventh Circuit's holding that Canon 9 was a basis for disqualification of Kirkland in Westinghouse may have stemmed solely from the apparent impropriety which developed when the imputation of knowledge rule was applied. Indeed, the Seventh Circuit criticized the district court for "applying a different imputation of knowledge principle . . . than that 'traditionally' and recently applied by this circuit. . . ."65 In so commenting, the Seventh Circuit used Westinghouse to reaffirm its recent holding in Schloetter v. Railoc of Indiana, Inc.66 In Schloetter, a patent infringement case, a former partner of the law firm representing the defendant was shown to have previously been retained by the plaintiff's agent in prosecuting the original patent application.67 Noting that no question regarding the propriety of disqualification would arise if the former partner himself attempted to represent the defendant, the court went on to reiterate the traditional rule that confidential information possessed by one member of a law firm is imputed to all members of that firm.68 The Seventh Circuit thus affirmed the district court's disqualification of defendant's counsel.69

There is little question that imputation of knowledge between members of a law firm is the traditional rule.70 This rule, however, was designed for a time when law firms were relatively small, when interaction among the various partners was great, and when a firm's influence extended over a limited geographic area.71 Under such conditions, continuation of the rule can be supported as it is reasonable to assume that knowledge will be passed between firm members in such situations. In the large, multicity law firms of today, such conditions no longer exist. Law firms, as well as the clients they represent, have changed considerably over the years. Firms have become departmentalized to the extent that the individual departments can be thought of as law firms within themselves.
Partners are often separated by thousands of miles and have minimal contact with each other.

The modern law firm has outgrown the traditional rule. To continue to hold, as the Seventh Circuit did in *Westinghouse*, that "actual knowledge of one or more lawyers in a firm is imputed to each member of that firm,"\(^72\) regardless of the underlying circumstances, is neither practical nor justifiable. Realizing this, recent decisions have departed from the traditional rule.\(^73\) No longer should knowledge relating to every aspect of a firm's practice be imputed to every member of the firm. In an increasing number of cases involving the possibility of impropriety, courts have been scrutinizing the facts before applying the traditional rules of imputed knowledge. In essence, the modern judge prefers to exercise discretion rather than apply a rigid rule in such cases. Such action is to be applauded. By refusing to follow this trend, the Seventh Circuit imposed unrealistic standards on many law firms under its jurisdiction.

V. Conclusion

The Seventh Circuit's reversal of the district court's decision in *Westinghouse* was correct. The court's finding that an attorney-client relationship did exist between Kirkland and the oil companies was well reasoned. The oil companies believed that such a relationship existed, and solely as a consequence of this belief was the disputed confidential information disclosed. Kirkland itself may have perceived the existence of some type of professional relationship between the firm and the oil companies.\(^74\) Once such a relationship was shown, disqualification of Kirkland became a necessity because of the Canon 4 and 5 transgressions.

The Seventh Circuit's comments on the applicability of Canon 9, however, were not as well-reasoned. The court's decision opens the door for frivolous disqualification motions based solely on the appearance of impropriety. By this action, the fears so cogently stated in *Woods* have been advanced one step closer to reality. Further, by reaffirming its outdated imputation of knowledge standard, the Seventh Circuit closed its eyes to changes taking place in the American legal system. Such changes pose challenges, but if these challenges are to be effectively met, new rules and theories must be formulated. Clinging to outdated solutions under the guise of striving for high ethical standards is not the answer when conditions are such that the standards sought cannot be met. When next called upon to decide like issues, the Seventh Circuit should meet the challenges of the changing world head on and formulate rules which will be just to attorney and client alike.

Anthony F. Kahn

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\(^72\) 580 F.2d at 1321.


\(^74\) Confidentiality was certainly present in this relationship. If this were not the case, why would Kirkland have accepted API as a client when the demands of confidentiality were made by API? See note 11 supra. The demands of confidentiality made by API were solely for the benefit and protection of its members.