

NOTES

POWER OF REORGANIZATION COURT TO ENJOIN PROTECTIVE COMMITTEE FROM COMMUNICATING WITH SECURITY HOLDERS *

SECTION 77B of the Bankruptcy Act attempted to abate the abuses incident to the virtually uncontrolled operation of protective committees in equity receivership reorganizations¹ by subjecting committees to judicial supervision rather than by minimizing their office in the reorganization scheme.² One of the functions still reserved almost exclusively to committees is that of reporting to security holders on the status of the reorganization and on the virtues and deficiencies of particular proposals.³ The context and tenor of committee solicitations and circulars may exert a determining influence upon the makeup of the reorganization plan⁴ and may even prevent the consummation of any plan⁵ and thereby profoundly affect the interests of the various claimants. Some sort of supervision over committee communications is therefore necessary if recalcitrant committees⁶ or those seeking to serve interests adverse to those of the investors⁷ are to be prevented from thwarting or dominating a reorganization. Accordingly, even though specific statutory

* *In re Schroeder Hotel Co.*, 86 F. (2d) 491 (C. C. A. 7th, 1936); *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

1. See generally, S. E. C., REPORT ON PROTECTIVE AND REORGANIZATION COMMITTEES (1936-37) Parts I, III; Douglas, *Protective Committees in Railroad Reorganizations* (1934) 47 HARV. L. REV. 565, 567; Comment (1935) 35 COL. L. REV. 905. Curbing these excesses was one of the major objectives of § 77B. See Weiner, *Corporate Reorganizations: Section 77B of the Bankruptcy Act* (1934) 34 COL. L. REV. 1173, 1183.

2. See §§ 77B(b) (10), 77B(c) (4) (a) & (b), 77B(c) (9), 77B(e) (1), 77B(f) (5), 48 STAT. 912, 11 U. S. C. § 207(f) (5) (1934); Rohlich, *The New Deal in Corporation Law* (1935) 35 COL. L. REV. 1167, 1185; Weiner, *supra* note 1, at 1188 *et seq.* It is doubtful whether these regulations have achieved the desired results. Fortas, *The Securities Act and Corporate Reorganizations* (1937) 4 LAW & CONTEMP. PROB. 218, 228 *et seq.*

3. See Lowenthal, *The Stock Exchange and Protective Committee Securities* (1933) 33 COL. L. REV. 1293, 1320; Comment (1935) 35 COL. L. REV. 905, 911.

4. See p. 1392 *infra*; S. E. C., *op. cit. supra* note 1, Part III, at 86. On solicitation practices of committees, see S. E. C., *op. cit. supra* note 1, Part I, at 883 *et seq.*

5. See p. 1392 *infra*. Deposit agreements between committees and security holders usually empower committees to cast votes on a plan unless a dissent is filed within a specified period. See *In re Witherbee Court Corp.*, 88 F. (2d) 251 (C. C. A. 2d, 1937); S. E. C., *op. cit. supra* note 1, Part I, at 889. Depositors usually acquiesce passively to committee advice [Rohlich, *supra* note 2, at 1181] but where there are rival committees depositors may occasionally be moved to independent action. See, *e.g.*, Brief for Appellees, p. 5, *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

6. "Strikers" have often attempted to capitalize nuisance values in reorganization proceedings. See Comment (1934) 34 COL. L. REV. 1303, 1317 *et seq.*

7. See S. E. C., *op. cit. supra* note 1, Part III, at 86.

authority is lacking, some courts have adopted the practice of prescribing or inspecting the contents of committee literature.⁸

Two recent cases put in issue another device which is apparently being utilized with increasing frequency for the purpose of controlling committee communications. In one, the district court had directed the removal of a protective committee for communicating false information to bondholders in an effort to prevent the consummation of any plan of reorganization.⁹ When these obstructionist tactics were nevertheless continued, the court, upon the debtor's petition, enjoined the erstwhile committee members and their agents from communicating to any security holder, in writing or otherwise, ". . . any purported information or advice with regard to the proceedings or actions of this court." On appeal the Circuit Court of Appeals for the Seventh Circuit sustained the order as a permissible exercise of the lower court's power to effectuate the bankruptcy jurisdiction granted it by Congress, rejecting the argument that the injunction violated the defendant's constitutional right of free speech on the ground that they had previously abused their right.¹⁰

In a second case, a plan desired by the debtor, and supported by a committee with which 86% of the bonds had been deposited, was not approved by the necessary two-thirds of the bondholders because a minority group of bondholders, believing that the proposal showed undue solicitude for an insolvent debtor with no equity in the property,¹¹ had induced a sufficient number of bondholders to file dissents.¹² Since some investors had apparently switched their votes as many as three times because of the bitter circularization campaign waged by the opposing interests, the court issued an order restraining all parties from further written communication with the security holders. Subsequently a new plan was advanced and approved by the court. Requi-

8. See *In re Butterick Co.*, C. C. H. Bankr. Serv. 2414.06 (S. D. N. Y. 1935); *In re Saenger Theatres Inc.*, C. C. H. Bankr. Serv. 2328.02 (E. D. La. 1935). Communications from Federal District Judges Knight and Coleman to the YALE LAW JOURNAL state that this practice is regularly followed in their courts, and a communication to the YALE LAW JOURNAL from Clinton S. Ruch, of New York, states that it was employed by Judge Inch in a recent reorganization proceeding. See note 23, *infra*.

9. The removal was effected in a unique fashion. By resort to its authority to scrutinize and disregard provisions of the deposit agreement [§ 77B(b) (10), 48 STAT. 912, 11 U. S. C. § 207(b) (10) (1934); see Fortas, *supra* note 2, at 230], the court restrained the committee from exercising the power to represent depositors. See also, *Texas Hotel Securities Corp. v. Waco Development Co.*, 87 F. (2d) 395 (C. C. A. 5th, 1936) (Individual purchasing claims to block plan held entitled to vote).

10. *In re Schroeder Hotel Co.*, 86 F. (2d) 491 (C. C. A. 7th, 1936), (1937) 50 HARV. L. REV. 831.

11. The chief objectionable provision was that awarding one-third of the stock of the new corporation to another corporation owned by the debtor interests in satisfaction of a disputed claim against the debtor's furniture. See Brief for Appellees, p. 3, *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

12. It is unnecessary to obtain acceptances from classes having no equity in the property. § 77B (e) (1), 48 STAT. 918, 11 U. S. C. § 207 (e) (1) (1934). See *In re Reading Hotel Co.*, 10 F. Supp. 470 (E. D. Pa. 1935) (stockholders); *In re William Penn Garage*, C. C. H. Bankr. Serv. ¶ 2419.02 (W. D. Pa. 1935) (junior creditors).

site bondholder consent could apparently have been obtained to this proposal since it eliminated the objectionable features of the old plan. But the debtor petitioned for an order enjoining all other parties from communicating any new plan to the bondholders until it had enjoyed a "reasonable opportunity" to obtain acceptances to a slightly modified version of the old plan. Instead, the court entered an order continuing the injunction in force as to the petitioner but lifting it to allow the proponents of the new plan to circularize the bondholders. The debtor appealed on the ground that its right of free speech had been violated, but the order was affirmed without opinion by the Circuit Court of Appeals for the Second Circuit.¹³

This use of the injunction¹⁴ raises once again the question of the propriety of a previous restraint on freedom of speech. The constitutional prohibition against any such restraint¹⁵ embraces the individual's right freely to speak his mind not only on questions of public importance, but also upon matters of purely private interest, the proscription in the latter case being expressed by the courts in terms of the traditional concept that equity will not enjoin a libel.¹⁶ While the strict enforcement of this principle would manifestly outlaw orders of the type under discussion, some support therefor could be derived

13. *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

14. For similar uses of the injunctive power, see *In re Granville & Winthrop Bldg. Corp.*, 87 F. (2d) 101, 102 (C. C. A. 7th, 1936); *Straus v. Baker Co.*, 87 F. (2d) 401, 405 (C. C. A. 5th, 1937). Statutory sanction for these injunctions may be found in § 2 (15) of the Bankruptcy Act, 30 STAT. 546 (1898), 11 U. S. C. § 11 (15) (1934), which authorizes Bankruptcy courts to "make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement . . ." of the Act. For the broad scope of this provision in reorganizations, see *Continental Ill. Nat. Bank and Trust Co. v. Chicago, R. I. & Pac. Ry.*, 294 U. S. 648, 676 (1934), (1935) 48 HARV. L. REV. 1430. See also (1935) 44 YALE L. J. 677.

15. *Near v. Minnesota*, 283 U. S. 697 (1930); *Grosjean v. American Press Co.*, 297 U. S. 233 (1935). Although the First Amendment says that "Congress shall make no law . . . abridging the freedom of speech," there is no doubt that the federal courts are bound by the prohibition. See dissenting opinion, Harlan, J., in *Patterson v. Colorado*, 205 U. S. 454, 464 (1906); Concurring opinion, Van Orsdel, J., in *American Federation of Labor v. Bucks Stove & Range Co.*, 33 App. D. C. 83, 112 (1903); *Trinity Methodist Church South v. Federal Radio Comm.*, 62 F. (2d) 850, 851 (App. D. C., 1932). Cf. *State ex rel. Liversey v. Judge Civil Dist. Ct.*, 34 La. Ann. 741, 793, 799 (1882); *Crouch v. Central Labor Council*, 134 Ore. 612, 622, 293 Pac. 729, 732 (1930). The distinction between previous restraint and subsequent punishment, which is permissible where the privilege has been abused, is often tenuous. See Comment (1931) 31 COL. L. REV. 1148, 1155. And in any event the severity of the prescribed punishment rather than the abstract category into which it is placed, determines the effectiveness of a restriction on freedom. See Comment (1931) 41 YALE L. J. 262, 269.

16. *Brandreth v. Lance*, 8 Paige Ch. 23 (N. Y. 1835); *State ex rel. Liversey v. Judge Civil Dist. Ct.*, 34 La. Ann. 741 (1882); *Life Ass'n of America v. Boogher*, 3 Mo. App. 173 (1876); *Marlin Fire Arms Co. v. Shields*, 171 N. Y. 384, 64 N. E. 163 (1902). See Pound, *Equitable Relief Against Defamation and Injuries to Personality* (1916) 29 HARV. L. REV. 640, 648 *et seq.*; Simpson, *Fifty Years of American Equity* (1937) 50 HARV. L. REV. 171, 219.

from the exception to the rule, frequently applied in labor¹⁷ and patent infringement¹⁸ disputes, which permits the issuance of an injunction against the spoken or written word where irreparable injury to property would otherwise ensue.¹⁹ Thus it is arguable that a bankruptcy court may properly enjoin communications whose effect would be to impair or destroy the equity of the debtor or the property interests of any group of creditors—results which the successful execution of the appellants' design would probably have occasioned in the instant cases.²⁰ Although this doctrine²¹ would rest on cases where specific types of statements have been proscribed,²² the scope of an injunction theoretically does not affect its character as a previous restraint, so that the blanket injunctions issued in the principal cases seem equally as valid as orders requiring the submission of all communications to the court before dispatch,²³ or restraining the circulation of false and misleading in-

17. *Gompers v. Bucks Stove & Range Co.*, 221 U. S. 418 (1910); *Hitchman Coal & Coke Co. v. Mitchell*, 245 U. S. 229 (1917); *Campbell v. Motion Picture Machine Operators Union of Minneapolis, Local 219*, 151 Minn. 220, 186 N.W. 781 (1922); *Hughes v. Kansas City Motion Picture Machine Operators Local No. 170*, 282 Mo. 304, 221 S.W. 95 (1920); *Kraemer Hosiery Co. v. American Federation of Full Fashioned Hosiery Workers*, 305 Pa. 206, 157 Atl. 588 (1931). *Contra*: *Marx & Haas Jeans Clothing Co. v. Watson*, 168 Mo. 133, 67 S.W. 391 (1902) (apparently overruled by the *Hughes* case *supra*); *Lindsay & Co. v. Montana Federation of Labor*, 37 Mont. 264, 96 Pac. 127 (1908). See Notes (1911) 32 L. R. A. (N.S.) 1013, (1920) 6 A. L. R. 909, 971 *et seq.*, (1922) 16 A. L. R. 230, (1923) 27 A. L. R. 651, 658; Simpson, *supra* note 16, at 193 *et seq.*

18. *Emack v. Kane*, 34 Fed. 46 (C. C. N. D. Ill. 1888); *Maytag v. Meadows Mfg. Co.*, 35 F. (2d) 403 (C. C. A. 7th, 1929). See (1934) 23 GEO. L. J. 81; (1936) 34 MICH. L. REV. 570. For other situations in which property rights were similarly protected by the injunctive process, see *American Mercury, Inc. v. Chase*, 13 F. (2d) 224 (D. Mass. 1926); *Bausch & Lomb Optical Co. v. Wahlgren*, 1 F. Supp. 799 (N. D. Ill. 1932); *Lawrence Trust Co. v. Sun American Publishing*, 245 Mass. 262, 139 N. E. 655 (1923); *National Life Ins. Co. of U. S. v. Myers*, 140 Ill. App. 392 (1908).

19. The theory generally employed is that the forbidden utterances or publications are but part of an illegal conspiracy to damage property and as such are enjoined. See Notes (1911) 32 L. R. A. (N.S.) 1013, (1920) 6 A. L. R. 909, 911 *et seq.* In this connection it has been stated that "some courts have taken a rather doctrinaire attitude toward labor controversies, holding illegal peaceable and honest conduct directed toward ends considered by labor to be legitimate and necessary to its own economic protection." Simpson, *supra* note 16, at 197. Cf. Sayre, *Labor and the Courts* (1930) 39 YALE L. J. 682, 684 *et seq.*

In the *Schroeder* case the court seemed to rest its decision on its power to protect its bankruptcy jurisdiction, although it relied on cases based on the protection of property rights. For a discussion of the validity of this theory, see pp. 1395-96 *infra*.

20. See *In re Schroeder Hotel Co.*, 86 F. (2d) 491, 492 (C. C. A. 7th, 1936); *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

21. Where the communication privilege had previously been abused with consequent injury to the estate, a subsequent injunction would be even more clearly supportable. See cases cited notes 17, 18 *supra*.

22. See (1932) 41 YALE L. J. 923.

23. See note 8, *supra*. Although the propriety of the procedure has apparently not yet been questioned, the circuit court in the *Schroeder* case indicated that the lower

formation.²⁴ In any event, other precedents for allowing the 77B courts to exercise so broad an injunctive power are available. The power of the Postmaster-General to withdraw mailing privileges from publications he deems seditious²⁵ and the similar power of the Federal Communications Commission to refuse to grant or renew or to revoke broadcasting licenses as required by "the public convenience, interest or necessity"²⁶ represent for all practical purposes previous restraints on publications or utterances conveyed through these vital media of communication.²⁷ Since these instances indicate that grounds will be found for sustaining those previous restraints considered essential to the attainment of an end of sufficient importance,²³ control

court could have adopted it instead of issuing a blanket injunction, at the same time recognizing the administrative difficulty this procedure entails. 86 F. (2d) 491, 493. This practice is substantially similar to that which the S. E. C. is authorized to pursue with regard to security prospectuses. See Securities Act § 5, 48 STAT. 77 (1933), as amended by § 204, 48 STAT. 906, 15 U. S. C. § 77e (1934); § 8, 48 STAT. 79 (1933), 15 U. S. C. § 77h (1934); § 10, 48 STAT. 81 (1933), as amended by § 205, 48 STAT. 906, 15 U. S. C. § 77j (1934); 3 C. C. H. Stocks and Bonds Serv. §§ 3105-3111. The act was held a valid exercise of Congress' power over the mails in *Jones v. S. E. C.*, 79 F. (2d) 617 (C. C. A. 2d, 1935), *rev'd on other grounds*, 298 U. S. 1 (1936). See Comment (1935) 5 FORD. L. REV. 302, 312.

24. To justify the breadth of the injunction the court in the *Schroeder* case relied principally on *Nann v. Raimist*, 255 N. Y. 307, 174 N. E. 690, (1931) 31 COL. L. REV. 717, which sustained an injunction against all further picketing where the defendants had violated a previous order restraining only unlawful picketing. Prior illegal acts have often served as the basis for an injunction against all picketing, legal or illegal. See Comment (1931) 44 HARV. L. REV. 971. The fact that a publication may be libelous is in theory immaterial insofar as its liability to previous restraint is concerned. See *Patterson v. Colorado*, 205 U. S. 454, 462 (1906); *Near v. Minnesota*, 283 U. S. 697, 721 (1930).

25. 40 STAT. 230 (1917), 18 U. S. C. §§ 343-345 (1934); *Milwaukee Publishing Co. v. Burleson*, 255 U. S. 407 (1921); *Masses Publishing Co. v. Patten*, 244 Fed. 535 (C. C. A. 2d, 1918); *Gitlow v. Kiely*, 44 F. (2d) 227 (S. D. N. Y. 1930) (no constitutional guaranty of right of use of mails). Congress has excluded a great variety of matter from the mails. See Comment (1930) 10 B. U. L. REV. 246.

26. 48 STAT. 1085, 1086, 47 U. S. C. §§ 309a, 312(a) (1934).

This provision has been upheld as against the free speech argument. *Trinity Methodist Church South v. Federal Radio Comm.* 62 F. (2d) 850 (App. D. C., 1932), *cert. denied*, 284 U. S. 685; *cf.* *KFKB Broadcasting Ass'n Incorp. v. Federal Radio Commission*, 47 F. (2d) 670 (App. D. C., 1931). It has also been sustained against the due process objection. *Federal Radio Comm. v. Nelson Bros. Bond & Mt'ge Co.*, 289 U. S. 266 (1933). On censorship under the Tariff Act, see Comment (1931) 31 COL. L. REV. 1148, 1153. Motion picture censorship has been upheld. *Mutual Film Corp. v. Ohio Industrial Comm.*, 236 U. S. 230 (1915). See Comments (1931) 31 COL. L. REV. 1148, 1154; Legis. (1930) 44 HARV. L. REV. 113.

27. See dissenting opinions by Brandeis and Holmes, JJ., in *Milwaukee Social Democratic Publishing Co. v. Burleson*, 255 U. S. 407, 431, 437 (1921); *Cohn, Censorship of Radical Materials by the Post-Office* (1932) 17 ST. LOUIS L. REV. 95, 107 *et seq.*; *Siegal, Censorship in Radio* (1936) 7 AIR L. REV. 1, 19 *et seq.*; Comments (1933) 46 HARV. L. REV. 987, 990; (1931) 31 COL. L. REV. 1148, 1152 *et seq.*; (1935) 7 AIR L. REV. 313.

28. See Comments (1933) 46 HARV. L. REV. 987, 992; (1930) 40 YALE L. J. 967.

of committee communications to effectuate the bankruptcy power would seem constitutionally permissible.²⁹ A stronger argument can be presented for the latter restriction, moreover, since it involves an impairment of the right to speak freely on matters of private interest, and not of the more significant political aspect of the constitutional guarantee,³⁰ which is abridged by the postal and radio powers.

Since the blanket injunction against committee communications does not abridge political freedom, a decision as to the propriety of this newly-developed device should be governed not by abstract conceptions of free speech, but rather by a realization of the practical need for the injunction as a discretionary measure which the reorganization court may invoke to conserve the property under its jurisdiction. Courts have apparently resorted to this expedient not only to curb the excesses and deliberate misstatements of obviously predatory committees and to expedite the consummation of reorganization plans, but also to prevent apparently legitimate committees from flooding investors and creditors with conflicting and confusing information and opinions.³¹ The imperfections latent in a system dependent for its success in large part on informed and intelligent investor judgment³² may often make it advisable to confine the arena of combat to the reorganization court, an agency better equipped than unenlightened or biased creditors to evaluate opposing contentions as to the worth of a plan. Once a court, after fair hearing, has reached a decision on the merits of a plan, it can assist materially in obtaining creditor approval or disapproval by careful use of the injunction against communication. The same result could be achieved in more straightforward fashion by making creditor and investor consent to a plan unnecessary,³³ but

29. Invocation of the injunction in this situation should be distinguished from its use to ban the publication of court proceedings in order to expedite the jurisdiction of the court. Its employment for the latter purpose has generally been held invalid. *Dailey v. Superior Court of City & County of San Francisco*, 112 Cal. 94, 44 Pac. 458 (1896); *In re Shortridge*, 99 Cal. 526, 34 Pac. 227 (1893); *Ex parte Foster*, 44 Tex. Cr. R. 423, 71 S. W. 593 (1903); *Ex parte McCormick*, 129 Tex. Cr. R. 457, 88 S. W. (2d) 104 (1935); *cf. In re Times Publishing Co.*, 276 Mich. 349, 267 N. W. 858 (1936). But *cf. Tate v. State*, 132 Tenn. 131, 177 S. W. 69 (1915). See also (1937) 46 YALE L. J. 1259.

30. For an intimation that a distinction can be drawn between utterances on matters of public and of private interest, see *Near v. Minnesota*, 283 U. S. 697, 716. See also *Howell v. Bee Publishing Co.*, 100 Neb. 39, 42, 158 N. W. 358, 359 (1916). It seems probable, moreover, that the protection against previous restraint was intended to apply only to political utterances. Pound, *supra* note 16, at 650; Comment (1931) 31 COL. L. REV. 1148, 1155.

31. See Record, fols. 665, 666, *In re Madison Hotel Corp.*, S. D. N. Y., March 6, 1937, *aff'd without opinion*, C. C. A. 2d, May 17, 1937.

32. *Cf.* Comment (1937) 46 YALE L. J. 1177, 1198.

33. If certain conditions are met, a plan may be consummated without the consent of two-thirds of a class of creditors or of a majority of stockholders. §§ 77B (b) (4 and 5), 77B(e) (1), 48 STAT. 913, 914, 918. 11 U. S. C. §§ 207(b) (4 and 5), 207(e) (1) (1934). See Comment (1936) 46 YALE L. J. 119. The constitutionality of § 77B(b) (5) has been questioned. See *Tennessee Publishing Co. v. American*

the emotional and constitutional objections to such a proposal³⁴ are perhaps obstacles too formidable to overcome. While indiscriminate resort to the injunctive power by the 77B courts might operate to stifle constructive opposition, the salutary results which would doubtless flow from its judicious exercise to curb self-seeking and delay-provoking committees far outweigh any abuses possibly occasioned by its employment.

THE VENDEE'S LIEN ON PERSONALTY*

THE MISSOURI Pacific Railroad entered into contracts to purchase from the defendant, a non-resident corporation, stocks and bonds of certain Missouri corporations. The securities described in the contracts were deposited in escrow with a New York trust company, and the railroad company paid \$3,200,000 upon the agreed purchase price. Plaintiff, the trustee in bankruptcy of the Missouri Pacific Railroad, brought suit in Missouri to have the contracts rescinded, on the grounds, *inter alia*, that they were *ultra vires* and were induced by fraud and coercion, and also prayed that an equitable lien be impressed upon the stock and bonds for the amount paid on the purchase price. Jurisdiction *in rem* was sought to be obtained through service upon the non-resident defendants by publication under the Missouri statute providing for such service in suits for the enforcement of liens against personal property within the jurisdiction of the court.¹ Upon removal of

National Bank, 57 Sup. Ct. 85 (1936) (lower court decision holding section unconstitutional declared premature).

Under the proposed Chandler Bill [75th Cong., 1st Sess., H. R. 6439] the plan would originally be formulated by an independent trustee in bankruptcy, and thereupon submitted to the court. After a hearing, the court, provided it deemed the plan "worthy of consideration", would then be required, where the corporation's indebtedness exceeded \$5,000,000, to submit it to the S.E.C.; and in other cases might do so at its option. Should the court, upon receiving the Commission's report, find the plan fair, it would be sent, together with the court's opinion, if any, and the S.E.C. report to investors for their approval. Prior to this time all parties would be forbidden to solicit acceptances to a plan or authorities to accept. Chandler Bill, § 12-II(d) (5-8).

34. See Comment (1936) 46 YALE L. J. 116, 119 *et seq.* See also Wright v. Vinton Branch of Mountain Trust Bank of Roanoke, 57 Sup. Ct. 556 (1937); § 74(e) Bankruptcy Act, 48 STAT. 922, 11 U. S. C. § 202(e) 1934.

* Thompson v. Terminal Shares, No. 10,731 (C. C. A. 8th, April 13, 1937).

1. MO. STAT. ANN. (Vernon, 1932) § 739 *et seq.* The statute also provided for such service in attachment suits. Plaintiff sought to obtain jurisdiction by attaching and garnishing the securities forming the subject matter of the contract, under the well recognized rule that the securities of Missouri corporations have a situs for the purpose of attachment in the state, although physically outside. [See Wood, *Reaching Shares of Stock* (1932) 38 W. VA. L. Q. 219, 220 *et seq.*]. The District Court, however, held that writs of attachment could not issue under state law, since the petition was for equitable relief. Thompson v. Terminal Shares, 14 F. Supp. 459, 460 (W. D. Mo. 1936).

the cause to the federal court, the nonresident defendant's motion, entered at a special appearance, to quash process and dismiss the bill was granted on the ground that the bill failed to establish a cause of action for an equitable lien, and that, therefore, neither the state nor the federal court had acquired jurisdiction under the statute.² On appeal the Circuit Court of Appeals for the Eighth Circuit reversed the decision of the lower court and, without deciding the validity of the plaintiff's cause of action, held that the District Court had obtained jurisdiction under the statute, since the plaintiff's claim as pleaded was not so unsubstantial as to be completely without merit.³

It is a well established doctrine that the vendee under an executory contract for the sale of land has an equitable lien on the land for purchase money advanced where the contract fails or is rescinded by the vendee due to fault of the vendor.⁴ The extension of this principle to contracts involving personalty has occasioned a conflict of authority. The prevailing view, however, has sanctioned use of the device in the case of chattel contracts, at least where the purchaser has received possession of the personalty;⁵ in fact, under the Uniform Sales Act, a buyer entitled to rescind is expressly granted a lien upon the goods in his possession.⁶ Enforcement of the lien thus recognized has been secured in some cases by equitable foreclosure

2. *Thompson v. Terminal Shares*, 14 F. Supp. 459 (W. D. Mo. 1936), (1936) 50 HARV. L. REV. 138.

3. *Thompson v. Terminal Shares*, No. 10,731 (C. C. A. 8th, April 13, 1937).

4. 3 BLACK, RESCISSION AND CANCELLATION (2d ed. 1929) § 694; 2 JONES, LIENS (3d ed. 1914) §§ 1105, 1106; 3 POMEROY, EQUITY JURISPRUDENCE (4th ed. 1918) § 1263; Note (1926) 45 A. L. R. 352.

5. *Truman's Pioneer Stud Farm v. Hansen*, 108 Kan. 717, 196 Pac. 1087 (1921); *Scott v. Clarkson's Executrix*, 4 Ky. 277 (1808); *Witte v. Hobolth*, 224 Mich. 286, 195 N. W. 82 (1923); *Giarratano v. McIlwain*, 215 App. Div. 644, 214 N. Y. Supp. 582 (3d Dep't 1926); *Baranofsky v. Weiss*, 120 Pa. Super. 126, 182 Atl. 47 (1935); *Alexander v. Walker*, 239 S. W. 309 (Tex. Civ. App. 1922); *Free Sewing Machine Co. v. Atkin Furniture Co.*, 71 S. W. (2d) 604 (Tex. Civ. App. 1934); *Hall v. Bank of Baldwin*, 143 Wis. 303, 127 N. W. 969 (1910); *Mycok v. Beatson*, 13 Ch. D. 384 (1878); see 20 HALSBURY, LAWS OF ENGLAND (2d ed. 1931) § 719; Comment (1934) 33 MICH. L. REV. 108, 113 *et seq.* *Contra*: *People's Electric Ry. v. McKeen Motor Car Co.*, 214 Fed. 73 (C. C. A. 8th, 1914); *National Cash Register Co. v. Hude*, 119 Miss. 36, 80 So. 378 (1919). The lien has been restricted to cases where the defendant was insolvent. *Apple v. Edwards*, 92 Mont. 524, 16 P. (2d) 700 (1932); *Hackney Mfg. Co. v. Celum*, 189 S. W. 988 (Tex. Civ. App. 1916).

6. Section 69 (5) of the UNIFORM SALES ACT provides: "Where the buyer is entitled to rescind the sale and elects to do so, if the seller refuses to accept an offer of the buyer to return the goods, the buyer shall thereafter be deemed to hold the goods as bailee for the seller, but subject to a lien to secure the repayment of any portion of the price which has been paid, and with the remedies for the enforcement of such lien allowed to an unpaid seller by section 53."

A buyer is not entitled to a lien under the Act where his rescission is induced by the seller's fraud and not by the seller's breach of warranty. *Sammis v. Marks*, 69 Utah 26, 252 Pac. 270 (1926). The lien granted by the Act does not preclude equitable jurisdiction to grant a lien for purchase money advanced. *Goldberg v. Minerva Automobiles*, 278 Ill. App. 217 (1934).

and public sale,⁷ in accordance with the normal procedure in land cases;⁸ the Uniform Sales Act⁹ and a few courts acting without statutory authority¹⁰ have also permitted enforcement of the lien by the quicker and simpler method of resale, either public or private. In other jurisdictions where the right of resale has not been acknowledged, the buyer's interest in the goods has been viewed as analogous in effect to a common law lien, conferring upon him at least a right to the retention of the property as security for restitution.¹¹ While an interest such as the vendee's lien, unless conferred by statute, is enforceable only in a court of equity, a number of common law courts, adopting a somewhat similar approach, have recognized the buyer's interest in the subject matter of the contract where the contract fails or is rescinded after payment has been made. Thus, the purchaser's interest in goods received has been held sufficient to defeat an action of replevin;¹² and it appears that the buyer's tender of the property conditioned upon a return of purchase money paid is enough to satisfy the requirement of restitution as a condition precedent to recovery at law on the theory of rescission;¹³ it has even been held that subsequent to a conditional tender of the property and pending decision on the action to rescind, the buyer is entitled to the use of the property.¹⁴ In the light of this tendency of the

7. *Giarratano v. McIlwain*, 215 App. Div. 644, 214 N. Y. Supp. 582 (3d Dep't 1926); *Free Machine Co. v. Atkin Furniture Co.*, 71 S. W. (2d) 604 (Tex. Civ. App. 1934).

8. *Hafner v. Stuart Land Co.*, 246 Mich. 465, 224 N. W. 630 (1929); *Johnson v. Berns*, 111 Ore. 165, 224 Pac. 624, 225 Pac. 727 (1924).

9. Under Section 69(5) of the UNIFORM SALES ACT the buyer is granted the remedies for the enforcement of his lien allowed an unpaid seller by section 53. Section 53 provides that the seller has "(c) A right of resale as limited by this act." Section 60 (4), (5) permits resale either by public or private sale and without notice to the other party of the time or place of resale. *Brown & Co. v. Darling & Co.*, 238 App. Div. 487, 264 N. Y. Supp. 792 (4th Dept, 1933) (public sale); *Wilson & Co. v. Werk Co.*, 104 Ohio St. 507, 136 N. E. 202 (1922) (private sale). The buyer may sell to himself if he exercised "reasonable care" in making the resale. *Ibid.*

10. *Alexander v. Walker*, 239 S. W. 309 (Tex. Civ. App. 1922) (public sale); *Truman's Pioneer Stud Farm v. Hansen*, 108 Kan. 717, 196 Pac. 1087 (1921) (private sale).

11. *Hall v. Bank of Baldwin*, 143 Wis. 303, 127 N. W. 969 (1910); see *Apple v. Edwards*, 92 Mont. 524, 536, 16 P. (2d) 700, 704 (1932). *A fortiori*, the Uniform Sales Act authorizes retention of the goods as security. *Land Finance Corp. v. Sherwin Electric Co.*, 102 Vt. 73, 146 Atl. 72 (1929).

12. *Wellington-Stone Co. v. Thomas*, 11 La. App. 242, 123 So. 410 (1929); *Auto Brokerage Co. v. Ullrich*, 102 N. J. Law 341, 131 Atl. 901 (1926); *cf.* *Southern Iron & Equipment Co. v. Bamberg, E. & W. Ry.*, 151 S. C. 506, 149 S. E. 271 (1929).

13. *Whiting v. Squeglia*, 70 Cal. App. 108, 232 Pac. 986 (1924); see *Liquid Carbonic Co. v. Cochran*, 161 S. C. 40, 46, 159 S. E. 461, 464 (1931); *cf.* *Keefe v. Jefferson*, 151 Minn. 368, 186 N. W. 789 (1922); *Sisson v. Hill*, 18 R. I. 212, 26 Atl. 196 (1893). The Uniform Sales Act has been held to authorize a conditional tender. *Levy v. Chonavitz*, 163 N. Y. Supp. 658 (County Ct. 1917); *Feinman v. Weil*, 105 Misc. 298, 173 N. Y. Supp. 11 (Sup. Ct. 1918).

14. *Egan v. Parks*, 111 Cal. App. 415, 295 Pac. 866 (1931); *cf.* *Plotkin v. Galowitz*, 109 N. J. Eq. 304, 157 Atl. 153 (Ch. 1931). But *cf.* *Grainger Bros. Co. v. Am-*

courts to permit a plaintiff at law to retain the consideration received for the purchase price as security against possible failure to obtain full restitution, it has been suggested that in the future resort to equity for the enforcement of a vendee's lien of non-statutory origin may become necessary, especially if a power of resale for the vendor's account is eventually recognized at law.¹⁵

Although many courts have recognized vendees' liens, theories as to the actual basis of the lien are in utter conflict,¹⁶ a result apparently attributable to the efforts to justify logically a doctrine evolved by the courts on a practical level. The plaintiff in the instant case advanced the theory that since equity considers the vendee the equitable owner of the land from the moment the contract is executed, a rationalization allegedly developed to explain the vendee's right to specific performance of the contract, the vendee's lien on the land was based directly on his right to specific performance.¹⁷ This premise led to the conclusion that since the contract for the purchase of securities was also specifically enforceable, the plaintiff as purchaser was entitled to a vendee's lien on the personalty. The theory is not too convincing inasmuch as the vendee's lien on land has been recognized in many cases in which the contract was not specifically enforceable,¹⁸ and since, further, there would appear to be no sound reason for favoring the purchaser of unique chattels over the buyer of non-unique goods. In the last analysis, the vendee's lien appears to be no more than a remedial device developed by equity to do justice between the parties by giving the vendee a security interest against retention of both land and money by the vendor.¹⁹ From this viewpoint, there appears to be no reason for not employing the concept in favor of a wronged buyer of personalty,²⁰ unless the rights of innocent third parties are involved.

sinck & Co., 15 F. (2d) 329 (C. C. A. 8th, 1926); *Mallow v. Hall*, 209 Wis. 426, 245 N. W. 90 (1932).

15. Comment (1934) 33 MICH. L. REV. 108, 114.

16. See *Brown, Vendor's Lien for Purchase Money* (1922) 95 CENT. L. J. 42; Comment (1923) 7 MINN. L. REV. 231, 233; Comment (1932) 1 MERCER BEASELY L. REV. 70, 75; (1908) 8 COL. L. REV. 571.

17. See *Thompson v. Terminal Shares*, 14 F. Supp. 459, 461-462 (W. D. Mo. 1936); Memorandum of Professor Walter W. Cook, Plaintiff's brief in the District Court, p. 121 *et seq.*; *Bowman v. Adams*, 45 Idaho 217, 225-226, 261 Pac. 679, 681-682 (1927); *cf. Stone, Equitable Conversion by Contract* (1913) 13 COL. L. REV. 369.

18. See Note (1926) 45 A. L. R. 352, 360 and cases cited.

19. See *Gerstell v. Shirk*, 210 Fed. 223, 229 (C. C. A. 7th, 1913); *Carpenter v. Dummit*, 221 Ky. 67, 79, 297 S. W. 695, 700 (1927); *Apple v. Edwards*, 92 Mont. 524, 537, 16 P. (2d) 700, 704 (1932); *Williston, Transfers of After-Acquired Personal Property* (1906) 19 HARV. L. REV. 557; Comment (1930) 4 U. OF CINN. L. REV. 368, 372; *cf. Comment* (1934) 32 MICH. L. REV. 685.

20. Objection to extending the doctrine to contracts involving personalty has been made on the ground that, pending the court's decree, the property might be removed beyond its jurisdiction. *Gerstell v. Shirk*, 210 Fed. 223 (C. C. A. 7th, 1913). But this difficulty could be obviated by impounding the property prior to the action or by enjoining its transfer.

In the case of a vendee's lien on land, the lien does not depend on a retention of possession by the vendee.²¹ Cases have held, however, both at common law²² and under the Sales Act,²³ that possession is essential to the existence of the vendee's lien on chattels; and it is at least certain that where, as in the instant case, the vendee under a contract for the sale of personalty has not received possession of the property, the standing of his lien for the purchase money advanced must be examined in the light of different considerations. Determination of the status of such a lien, an interest whose recognition runs counter to the traditional policy of basing security interests on possession or public record, entails a resolution of conflicting social policies. On the one hand is a tendency to refuse enforcement of a creditor's right to property in the possession of a debtor and so far subject to his control and use as to deceive other creditors into dealing with him under a belief of full ownership. Against this must be weighed the desirability of permitting the borrower to obtain the maximum amount of credit—a consequence which enforcement of the lender's lien naturally entails.²⁴ In the instant case, however, it is not necessary to determine the advisability of enforcing a secret lien from this viewpoint, for the case merely involves the rights of immediate parties to the contract, or parties with notice;²⁵ and in any event there would seem to be slight possibility in such a situation of penalizing innocent third parties by enforcing the lien, for while the securities were not in the buyer's possession, they were also not within the seller's control or apparent ownership. Since the equities of the case appear to lie with the plaintiff,²⁶ and since the vendor is insolvent, there would appear to be no good reason for refusing to guaranty the plaintiff, as a wronged party, complete restitution by giving him a security interest in the stocks and bonds forming the subject matter of the contract.²⁷

21. *Bullitt v. Eastern Ky. Land Co.*, 99 Ky. 324, 36 S.W. 16 (1896); *Elterman v. Hyman*, 192 N.Y. 113, 84 N.E. 937 (1908).

22. *Bowman v. Adams*, 45 Idaho 217, 261 Pac. 679 (1927); *Allen v. Shortridge*, 1 Duv. 34 (Ky. 1863); *Johnson v. Berns*, 111 Ore. 165, 224 Pac. 624, 225 Pac. 727 (1924).

23. *In re Tuduri's Estate*, 156 Misc. 317, 281 N.Y. Supp. 630 (Surr. Ct. 1935).

24. See Britton, *Equitable Liens—A Tentative Analysis of the Problem* (1930) 8 N. C. L. REV. 388, 399.

25. See *Thompson v. Terminal Shares*, No. 10,731 (C. C. A. 8th, April 13, 1937) (fourth paragraph of opinion).

26. Plaintiff alleged that the vendor corporation was the wholly owned subsidiary of the Alleghany Corporation, a non-resident defendant, which also controlled the voting stock of the vendee, the Missouri Pacific Railroad; that O. P. Van Sweringen, who was the chairman of the board of both the vendee and the Alleghany Corporation, and who controlled the latter corporation with his brother, had instigated the vendee's purchase of the securities in the interest of the Alleghany Corporation, the real vendor, in an effort to recoup a depression shrinkage of value by unloading the securities on the vendee at pre-depression prices.

27. There is authority for declaring a vendee's lien even where the vendee is not in possession of the personalty. *Pratt v. Weeks*, 9 F. Supp. 953 (S. D. Fla. 1932); *Armstrong & Co. v. Darbro*, 10 Ky. L. Rep. 984 (1889); *Kline v. Cofield*, 159 Ky. 744, 169 S.W. 477 (1914); *Carpenter v. Dummit*, 221 Ky. 67, 297 S.W. 695 (1927) (vendee's lien on stock); *Swainston v. Clay*, 3 DeG., J. & S. *557 (1863); *Levy v. Stogdon*, [1891] 1 Ch. 478.

COMPULSORY LICENSING AND THE PATENT POOL PROBLEM*

THE PATENT pool, affording reciprocal patent privileges to its members, is a common feature of industries dependent upon patents.¹ Whenever basic patents are controlled by interests hostile to owners of improvement patents, or numerous letters patent have been issued which mutually overlap, manufacture of the patented articles is impossible and cooperative action to break the deadlock becomes imperative.² This cooperative action may take the form of either a pooling of patent rights by a series of cross-licensing agreements or an assignment of patents to a central unit which issues comprehensive licenses to subscribers.³ By exploitation of patents in combination the pool achieves a dominating position in the industry which may develop into a monopoly far more extensive than could be attained by independent exercise of the individual privileges⁴ and which may extend even beyond the ambit of protection intended by the patent laws—thereby exposing the licensing practices of the pool to attacks under the anti-trust legislation.⁵

The sanctions prescribed for the enforcement of the anti-trust laws appear ill adapted to resolve the problems presented by the patent pool. Injunctions by the government compelling dissolution of the pools may prove more harmful to the public than the practices sought to be condemned.⁶ The provision for private triple damage actions has appeared equally impotent, since strict requirements of proof make recovery difficult.⁷ A possible solution of the problem is suggested, however, by a recent suit for injunctive relief arising under Section 16 of the Clayton Act.⁸ An independent manufacturer of radio apparatus petitioned the Federal District Court of Delaware for a mandatory injunction compelling the Radio Corporation of America to issue him a license to manufacture under all patents controlled by a pool of

* F. A. D. Andrea, Inc. v. Radio Corp. of America, 14 F. Supp. 226 (Del. 1936), *aff'd*, 88 F. (2d) 474 (C. C. A. 3d, 1937), *cert. denied*, (1937) 4 U. S. L. WEEK 943.

1. See VAUGHAN, *ECONOMICS OF OUR PATENT SYSTEM* (1925) c. 2.

2. See NATIONAL INDUSTRIAL CONFERENCE BOARD, *TRADE ASSOCIATIONS, THEIR ECONOMIC SIGNIFICANCE AND LEGAL STATUS* (1925) c. 9; Vaughan, *The Relation of Patents to Industrial Monopolies* (1932) 14 J. PAT. OFF. SOC. 61, 95.

3. *Bement v. National Harrow Co.*, 186 U. S. 70 (1902); *Standard Sanitary Mfg. Co. v. United States*, 226 U. S. 20 (1912); *Blount Mfg. Co. v. Yale & Towne Mfg. Co.*, 166 Fed. 555 (C. C. Mass. 1909).

4. See *Standard Sanitary Mfg. Co. v. United States*, 226 U. S. 20, 48 (1912); *Blount Mfg. Co. v. Yale & Towne Mfg. Co.*, 166 Fed. 555, 562 (C. C. Mass. 1909).

5. See Comment (1931) 40 YALE L. J. 1297. It has been definitely established that patented articles are subject to the anti-trust laws. *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U. S. 502 (1917); *Standard Oil Co. v. United States*, 283 U. S. 163 (1931).

6. The impossibility of effectual enforcement of the criminal provisions of the anti-trust laws has been demonstrated by the necessity for supplementary remedies permitting private parties to initiate enforcement proceedings. See *infra*, p. 1405, for a discussion of the beneficial functions of patent pools.

7. See Comments (1929) 38 YALE L. J. 503; (1932) 32 COL. L. REV. 335.

8. 38 STAT. 737 (1914), 15 U. S. C. § 26 (1934).

which it was, in effect, the sole licensing agency.⁹ It was alleged that the Radio Corporation had, by means of agreements for the interchange of patent rights, acquired the status of an illegal monopoly in the radio apparatus industry, that it had employed its position to restrain trade in interstate commerce, and that its refusal to grant petitioner a license would necessitate dissolution of his manufacturing enterprise.¹⁰ The court granted a motion to dismiss the bill, holding that the relief demanded was not of the kind contemplated by Section 16 of the Clayton Act, and that a violation of the anti-trust laws had never required the forfeiture of a patent privilege to anyone injured by its exercise. This decree was affirmed by the Circuit Court of Appeals for the Third Circuit, and a writ of *certiorari* was denied by the United States Supreme Court.¹¹

Although the relief demanded in the principal case has been sought before,¹² it has never been granted. But the cases relied upon by the defendant as determinative involved suits for infringement in which cross-bills asking for compulsory licenses were stricken out because of the irrelevancy of the issues sought to be introduced into the infringement controversies,¹³ and because of failure to allege an injury special to the petitioner as distinct from a general injury to the public—an averment held essential to a proper bill for relief under Section 16.¹⁴ The bill in the principal case is clearly not vulnerable to the first exception, since no infringement claims were involved, and in view of the allegation of special damage it appears equally unassailable under the second.¹⁵ Consequently the court might well have

9. Under a consent decree entered in a suit by the government charging the Radio Corporation with monopolistic tendencies [United States v. Radio Corp., 3 F. Supp. 23 (Del. 1933)], the subscribers to the pool were authorized to issue licenses to outsiders under their individually owned patents. Comment (1933) 1 GEO. WASH. L. REV. 513. The Radio Corporation retained the power to issue comprehensive licenses, one of which was sought by petitioner in the principal case.

10. For an account of the development and structure of the radio patent pool, see VAUGHAN, *op. cit. supra* note 1, at 64-67; REPORT OF THE FEDERAL TRADE COMMISSION ON THE RADIO INDUSTRY (1924).

11. F. A. D. Andrea, Inc. v. Radio Corp. of America, 14 F. Supp. 226 (Del. 1936), *aff'd*, 88 F. (2d) 474 (C. C. A. 3d, 1937), *crt. denied*, (1937) 4 U. S. LAW WEEK 943.

12. General Electric Co. v. Minneapolis Electric Lamp Co., 10 F. (2d) 851 (Minn. 1924); Radio Corp. v. United Radio & Electric Corp., 50 F. (2d) 205 (N. J. 1926); Radio Corp. v. Majestic Distributors, 53 F. (2d) 641 (Conn. 1931), (1932) 45 HARV. L. REV. 1118; Radio Corp. of America v. Hygrade Sylvania Corp., 10 F. Supp. 879 (N. J. 1934).

13. See note 12, *supra*. It is settled that an allegation that a patentee has violated the anti-trust laws is not a proper defense to an infringement suit. Radio Corp. v. Hygrade Sylvania Corp., 10 F. Supp. 879 (N. J. 1934).

14. Duplex Printing Press Co. v. Deering, 254 U. S. 443 (1921); see Radio Corp. v. Hygrade Sylvania Corp., 10 F. Supp. 879, 884 (N. J. 1934); Radio Corp. v. Duovac Radio Tube Corp., 6 F. Supp. 275, 277 (E. D. N. Y. 1931).

15. In the principal case the bill alleged that the refusal to license petitioner was part of a plan to restrain trade generally and to compel this competitor in particular to leave the radio apparatus manufacturing trade completely. Such an allegation, aside from the question of its substantiation, would appear adequate to satisfy the requirements of Section 16. See Western Electric Co., Inc. v. Patent Reproducer Corp., 53 F.

distinguished these earlier cases and resolved the issues, as ultimately they must be, upon considerations of the social and economic policy underlying the patent laws and the privileges they are designed to protect.¹⁶

The primary purpose of the present patent system is to promote the sciences and useful arts by insuring the inventor a reward commensurate with the commercial success of his discovery.¹⁷ Congress has stipulated the manner in which this reward is to be realized by conferring on the patentee the exclusive right to make, use, and vend his device for a limited period of time.¹⁸ Although the courts have circumscribed the purposes for which the resulting monopoly may be employed,¹⁹ the patentee has been protected in the enjoyment of the basic privilege of excluding others from the exploitation of his discovery.²⁰ Compulsory licensing would appear to deprive the patentee of this power of exclusion, but when viewed in the light of actual patent practice no substantial departure from established formulae would result. The vast majority of patents are now exploited upon a royalty basis by which the inventor is compensated according to a schedule determined by contract. If the patentee were required to license applicants subject to the terms and conditions imposed upon existing licensees, no alteration would be required in the method by which the inventor's remuneration would be computed. Moreover, where a discovery is exploited exclusively on a royalty basis, the return to the patentee might possibly be increased by virtue of the additional units produced by the new licensee.²¹

(2d) 639, 641 (S. D. N. Y. 1930); *Radio Corp. v. Majestic Distributors*, 53 F. (2d) 641, 643 (Conn. 1931).

16. The only precedent discovered by counsel for petitioner to support his claim was a *dictum* of Mr. Justice Brandeis in *Standard Oil Co. v. United States*, 283 U. S. 163, 172 (1931): "Unless the industry is dominated, or interstate commerce directly restrained, the Sherman Act does not require cross-licensing patentees to license at reasonable rates others engaged in interstate commerce." The interpretation of this sentence which was pressed by the petitioner—that licensing might under proper circumstances be required—was discarded by the court as the Justice was concerned with the imposition of onerous rates and no plea for a license was involved. The decisions of the courts upon patent questions have been determined on questions of policy rather than legal precedent. Powell, *The Nature of a Patent Right* (1917) 17 *Col. L. Rev.* 663, 681, 684.

17. See TOULMIN, *TRADE AGREEMENTS AND THE ANTI-TRUST LAWS* (1937) § 94; Comment (1928) 38 *YALE L. J.* 246, 251.

18. 46 *STAT.* 376 (1930), 35 *U. S. C.* § 40 (1934), enacted pursuant to *U. S. CONST.* Art. I, § 8.

19. *Bauer & Cie. v. O'Donnell*, 229 U. S. 1 (1913); *United States v. Schrader's Son, Inc.*, 252 U. S. 85 (1920) (attempted control over resale prices of the patented article); *Motion Picture Patents Co. v. Universal Film Co.*, 243 U. S. 502 (1917) (attempted control over supplies and accessories for the patented article); *Carbice v. American Patents Corp.*, 283 U. S. 27 (1931) (attempted control over unpatented articles used in combination). But *cf.* *Lceads & Catlin Co. v. Victor Talking Machine Co.*, 213 U. S. 325 (1909). See *TRADE ASSOCIATIONS*, *op. cit. supra* note 2, at 133; Barnett, "Within His Domain the Patentee is Czar" (1935) 17 *J. PAT. OFF. Soc.* 92, 95, 105.

20. *TRADE ASSOCIATIONS*, *op. cit. supra* note 2, at 130, 147.

21. Where the patentee is himself engaged in the commercial exploitation of an invention, the royalties derived from the competitor-licensee might not compensate

Even though compulsory licensing should entail some variation from present patent doctrine—as distinguished from actual practice—a modification might be justified by the dictates of a superior public policy, especially since patent privileges have always been held subject to state police regulations,²² the right of eminent domain,²³ and obligations of user.²⁴ In the case of the patent pool, strict adherence to patent ideology may result in a monopoly irreconcilable with the policy of the anti-trust legislation—preservation of the competitive system.²⁵ To the extent that compulsory licensing would resolve this conflict and at the same time retain the essential benefits of the pools, there seems to be no objection to the adoption of this remedy by the courts. In the initial stages of a pool's development competition is stimulated: the patent deadlock is broken; the cost of infringement avoided; and the parties are free to produce articles with the combined improvements represented by numerous patents.²⁶ After the basic patents expire, however, the pool is perpetuated only by reason of its control over minor patents, its suppression of new discoveries, and its power to compel the transfer of new patents to the combination.²⁷ The expense of patent litigation will generally force compliance with the terms dictated by the pool, for the penalty of refusal may be infringement which the inventor will be powerless to enjoin and which may destroy the marketability of his product.²⁸ Furthermore, considerable coercion may be exercised by a pool due to its bargaining position as virtually the sole purchaser of patents in the trade. Although, at this stage of its growth, the pool may be said to have outlived its economic and social justification, dissolution would probably produce a second deadlock and would certainly terminate the cooperative research characteristic of this type of industrial organization.²⁹ A system of compulsory licenses, on the other hand, would in no way interfere with the effective operation of the pools and would infiltrate new competitors to dilute the monopoly from which their evils are said to arise. Since the courts will not take the initiative in arriving at a broader construction of

for the loss of an advantageous trade position. In the case of the patent pool, however, the manufacturing patentee might suffer no injurious effects from such a licensing policy, in view of the reciprocal patent privileges incident to membership in the combination. Toulmin, *Patent Pools and Cross Licenses* (1935) 22 VA. L. REV. 119, 144, *et. seq.*

22. *Patterson v. Kentucky*, 97 U. S. 501 (1878); *Allen v. Riley*, 203 U. S. 347 (1906); *John Woods & Sons v. Carl*, 203 U. S. 358 (1906); *Ozan Lumber Co. v. Union County Nat. Bank*, 207 U. S. 251 (1907).

23. *Crozier v. Krupp*, 224 U. S. 290 (1912).

24. *Missouri v. Bell Telephone Co.*, 23 Fed. 539 (C. C. E. D. Mo. 1885), *app. dismissed*, 127 U. S. 780 (1888); *State v. Delaware & A. T. & T. Co.*, 47 Fed. 633 (C. C. Del. 1891), *aff'd*, 50 Fed. 677 (C. C. A. 3d, 1892).

25. See VAUGHAN, *op. cit. supra* note 1, at pp. 34, 224.

26. See TOULMIN, *op. cit. supra* note 17, § 91; VAUGHAN, *op. cit. supra* note 1, at 70, 71; Toulmin, *op. cit. supra* note 21, *passim*.

27. See Comment (1936) 7 AIR L. REV. 98, 104, 105.

28. See VAUGHAN, *op. cit. supra* note 1, at 152.

29. See *Radio Corp. v. United Radio and Elec. Corp.*, 50 F. (2d) 206 (N. J. 1926).

the patent statutes,³⁰ as is evident from the principal case, it remains for the legislature to recognize the obsolescence of the present patent system with a view toward adapting it to modern industrial conditions.³¹ Legislation providing for compulsory licenses is said to have been successful abroad³² and is not without precedent in the United States.³³ In those industries, such as the radio industry, where the public interest may be directly concerned with the practices of the trade, the need for regulation appears urgent. In view of the availability of the regulatory machinery provided by the Communications Commission, by which broadcasting stations are already subjected to penalties supplementary to the Clayton Act,³⁴ it might be well to refer manufacturing as well as communication practices to that body, which is in the most favorable position to regulate the industry in the public interest.

ACCRUED INTEREST TAXABLE AS INCOME TO MORTGAGEE BIDDING IN AT FORECLOSURE SALE*

A LIFE insurance company foreclosed several farm mortgages and, as the only bidder at the foreclosure sales, bought in the properties at amounts equalling the principal of the loans and accrued interest. The bids were made without regard to actual value for the purpose of avoiding potential loss which might result from exercise by the mortgagors and junior lienors of their statutory power to redeem at the bid price plus interest from the date of foreclosure.¹ The company, keeping books on a cash-receipts-and-

30. The patent law has developed by growth and judicial decision rather than legislative enactments. See, *e.g.*, *Evans v. Eaton*, 20 U. S. 356 (1822); *Grant v. Raymond*, 31 U. S. 218 (1832); *Leeds & Catlin v. Victor*, 213 U. S. 325 (1909); *Ashley v. Tatum*, 240 Fed. 979 (S. D. N. Y. 1917). See Comment (1931) 40 YALE L. J. 954, 959.

31. Considerable dissatisfaction with the present patent system has been expressed. See VAUGHAN, *op. cit. supra* note 1, c. 8; Comments (1931) 40 YALE L. J. 954, 960, (1928) 38 YALE L. J. 246, 251.

32. See Benjamin, *Compulsory License Suits in Germany* (1935) 17 J. PAT. OFF. Soc. 962. England has a provision authorizing a compulsory exclusive license excluding even the inventor. *Id.* at 964.

33. Early patents provided for maximum royalties, loss of patent privileges for non-use, and compulsory training of apprentices. South Carolina had a compulsory licensing statute. Schechter, *Compulsory Licensing of Patents* (1936) 22 VA. L. REV. 287, 303-306. Compare the provisions of Section 1 of the Copyright Law, 35 STAT. 1075, 1088 (1909) 17 U. S. C. §1 (1934).

34. The Communications Commission may refuse a broadcasting license to any applicant who has previously been adjudged a violator of the anti-trust laws. 48 STAT. 1087 (1934), 47 U. S. C. §313 (1934).

* *Helvering v. Midland Mutual Life Ins. Co.*, 57 Sup. Ct. 423 (Feb. 15, 1937).

1. Most of the properties were located in Michigan, where the owner is given a year in which to redeem at that figure. MICH. COMP. LAWS (1929) c. 266, §§ 14435, 14436. Redemption statutes, varying in their provisions, exist in a majority of the states. See 32 HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS (1922) 280.

disbursements basis, recorded its investment in the properties at amounts including principal and costs of foreclosure but not accrued interest. Over the company's objection that the properties actually were worth even less than the principal, the Commissioner of Internal Revenue assessed the accrued interest as part of gross income. The Board of Tax Appeals affirmed the Commissioner's ruling² but was reversed by the Circuit Court of Appeals, which remanded the case for a finding of the properties' fair market value.³ The Supreme Court reversed, holding that the mortgagee had in legal effect received full payment of the accrued interest, that it constituted taxable income, and that inquiry into market value of the properties would only hamper tax administration.⁴

The decision that taxable income was thus received is based upon two fictions. The first is that there were two separate and distinct transactions involved in the same deal—one the purchase of real property, the other the payment of a debt. For the purpose of taxation, the effect of the transactions was deemed the same as if the purchase had been made with cash and this money in turn applied by the mortgagor to the payment of the principal and accrued interest;⁵ there was no actual exchange of cash only because the same parties participated in both transactions.⁶ The second fiction is that the purchase was in terms of an even exchange: that is, that the properties were worth the total of the principal and accrued interest, and, if not worth that much in the open market, at least the bid accorded with the company's estimate of the value of the land to itself. Part of that value was the collateral benefit of protection against an unfavorable redemption which the insurance company evidently preferred to its alternative of taking a deficiency judgment for the difference between the amounts due and the actual value of the properties.⁷

The weakness of these fictions becomes apparent from an examination of the realities of the situation. Foreclosure sales are usually attended solely by the mortgagee, whose primary interest is not to purchase land as an

2. *Midland Mutual Life Ins. Co.*, 31 B. T. A. 1249 (1934).

3. *Midland Mutual Life Ins. Co. v. Commissioner of Int. Rev.*, 83 F. (2d) 629 (C. C. A. 6th, 1936).

4. *Helvering v. Midland Mutual Life Ins. Co.*, 57 Sup. Ct. 423 (Feb. 15, 1937) (McReynolds, J., dissenting), (1937) 50 HARV. L. REV. 988, 85 U. OF PA. L. REV. 741.

5. See *Silver v. Wickfield Farms*, 209 Iowa 856, 861, 227 N. W. 97, 99 (1929); *Ledyard v. Phillips*, 47 Mich. 305, 308, 11 N. W. 170, 171 (1882).

6. Once the fiction is accepted, the doctrine of constructive receipt of cash income is applicable. See Magill, *The Taxation of Unrealized Income* (1925) 39 HARV. L. REV. 82. Since this doctrine in effect deprives the taxpayer of his right to report on a cash basis, the courts have insisted that it be sparingly applied "lest it become a means for taxing something other than income and thus violating the Constitution." John A. Brander, 3 B. T. A. 231, 235 (1925); Hal E. Roach, 20 B. T. A. 919, 924-925 (1930). That the ruling in the principal case represents a strained application of the doctrine, see *Midland Mutual Life Ins. Co. v. Comm'r of Int. Rev.*, 83 F. (2d) 629, 631 (C. C. A. 6th, 1936); 1 PAUL AND MERTENS, FEDERAL INCOME TAXATION (Supp. 1936) § 10.09A, n. 38c.

7. *Helvering v. Midland Mutual Life Ins. Co.*, 57 Sup. Ct. 423, 426-427 (Feb. 15, 1937).

investor but to salvage something from his loan.⁸ This is especially true where redemption statutes are in force, for would-be purchasers are discouraged by the provision that neither possession nor full title are to pass to them until the end of the redemption period.⁹ Consequently, the bid price almost invariably has no relation to the worth of the property; and often, as was true in the instant case, the figure is well in excess of market value because of a desire to protect against an unfavorable redemption.¹⁰ Under these circumstances, taxation of accrued interest constitutes an exaction upon unrealized income. The mortgagee's cash ability to pay any tax clearly has not been enhanced. Actually he has suffered a loss with little prospect of realizing any part of the original loan at least until the end of the redemption period, when he has his first real opportunity to dispose of the land.¹¹

Life insurance companies, particularly, suffer from the decision in the instant case. Since 1921, their gross income has been limited to interest, rents, and dividends — the so-called "investment income"¹² — and neither bad debt losses nor capital gains and losses figure in their returns.¹³ As a result, once taxed on the interest included in their bid, they, unlike all other taxpayers, cannot partially compensate themselves either by establishing a capital loss at the time of foreclosure,¹⁴ or by deducting as a capital loss on resale the

8. See *Home Building and Loan Ass'n v. Blaisdell*, 290 U. S. 398, 445-446 (1934). The mortgagee is "primarily a lender and a purchaser only through necessity . . ." *Midland Mutual Life Ins. Co. v. Commissioner of Int. Rev.*, 83 F. (2d) 629, 630 (C. C. A. 6th, 1936).

9. *Michigan Trust Co. v. Lansing Lumber Co.*, 103 Mich. 392, 402, 61 N. W. 668, 671 (1894); *Durfee and Doddridge, Redemption from Foreclosure Sale* (1925) 23 MICH. L. REV. 825, 843; *Carey, Brabner-Smith, and Sullivan, Foreclosure Methods and Redemption* (1933) 27 ILL. L. REV. 595, 615.

10. *Helvering v. Midland Mut. Life Ins. Co.*, 57 Sup. Ct. 423, 425 (Feb. 15, 1937).

11. See note 9, *supra*.

12. § 244 (a), REV. ACTS OF 1921, 1924, 1926; § 202 (a), REV. ACTS OF 1928, 1932, 1934, and 1936; *Independent Life Ins. Co. of America*, 17 B. T. A. 757, 761 (1929).

13. § 245, REV. ACTS OF 1921, 1924, 1926; § 203 (a), REV. ACTS OF 1928, 1932, 1934, 1936; *Midland Nat. Life Ins. Co.*, 18 B. T. A. 1240 (1930); *Volunteer State Life Ins. Co.*, 27 B. T. A. 1149 (1933).

14. Under the treasury regulations, when a creditor other than a life insurance company buys in mortgaged property and applies the obligations of the debtor to the purchase price, he is entitled to show that the fair market value of the property is actually less than the amount of the debtor's obligations so used, and to deduct the difference as a capital loss. U. S. Treas. Reg. 69, Art. 153 (1926); U. S. Treas. Reg. 74, Art. 193 (1928); U. S. Treas. Reg. 77, Art. 193 (1932); U. S. Treas. Reg. 86, Art. 23 (k)-3 (1934); U. S. Treas. Reg. 94, Art. 23 (k)-3 (1936); 371 C. C. H. 1937 Fed. Tax Serv. ¶ 209.025; *Hulse, Mortgage Foreclosures Under the Federal Income Tax Regulations* (1936) 14 TAX MAG. 451. Accrued interest is expressly excluded from this computation except when it has previously been returned as income. 3 PAUL AND MERTENS, FEDERAL INCOME TAXATION (1934) § 28.78, n. 48. Thus, when the taxpayer bids in at principal plus accrued interest, and the property is admittedly worth less than the principal, there is a varying degree of hardship:

(a) Deduction allowed to those reporting on an accrual basis = principal + accrued interest returned as income in previous years — fair market value of the property.

difference between the bid price and the amount then realized.¹⁵ Thus, it is to be expected that, as the largest investors in farm mortgages in the country,¹⁶ life insurance companies should be the most vigorous opponents of this taxation of "imaginary interest."¹⁷ But the decision may also work hardship upon the mortgagor. To escape taxation of the accrued interest, mortgagees may reduce their bids to the amount of the principal and take deficiency judgments for the balance, thereby increasing the mortgagor's burden — a result contrary to the modern legislative policy of protecting mortgagors against the use of deficiency judgments as instruments of oppression.¹⁸

The problem could be handled more equitably by regarding the foreclosure sale as a single transaction. Recognition might be given to the unique character of foreclosure sales as involving not a purchase of land by the mortgagee as an independent investment, but an exchange of one form of capital asset

(b) Deduction allowed to those other than life insurance companies reporting on a cash basis = principal — fair market value.

(c) Life insurance companies are allowed no deductions whatsoever.

Since the market value is the basis for computing capital loss or gain on resale, and since the bid price is presumed to be the market value only in the absence of rebuttal (Treas. Regs., *supra*), the taxpayer in class (b) who shows a loss in the year of foreclosure apparently cannot recover upon resale, as part of a possible capital loss deduction, the amount of the accrued interest previously taxed under the decision in the principal case. His choice, therefore, lies between taking an immediate deduction of the difference between the principal and the fair market value, and delaying in favor of a possible capital loss deduction upon resale including the amount of the accrued interest [bid price (principal + accrued interest) — resale price].

15. For the provisions as to capital gains and losses for taxpayers other than life insurance companies, see § 117, 48 STAT. 714, 26 U. S. C. § 101 (1934). Since the Revenue Act of 1934, the deductible losses from sales or exchanges of capital assets for such taxpayers have been limited to \$2,000 plus the capital gains for the period. 372 C. C. H. 1937 Fed. Tax Serv. ¶ 868.025.

16. 288 TECHN. BULL. (Dep't of Agric. 1932) 21.

17. Practically all the litigation on the question has been instigated by life insurance companies, and in every instance the accrued interest has been held taxable. In some cases the market value of the properties at time of foreclosure was deemed immaterial [Helvering v. Missouri State Life Ins. Co., 78 F. (2d) 778 (C. C. A. 8th, 1934), *aff'g*, 29 B. T. A. 401 (1933); National Life Ins. Co. v. United States, 4 F. Supp. 1000 (Ct. Cl. 1933), *cert. denied sub nom.* Lucey, Receiver v. United States, 291 U. S. 683 (1934)]; in others it was ignored. American Central Life Ins. Co., 30 B. T. A. 1182 (1934); Prudential Ins. Co. of Amer., 33 B. T. A. 332 (1935); see Great Southern Life Ins. Co., 33 B. T. A. 512, 522 (1935); *cf.* Reserve Loan Life Ins. Co., 18 B. T. A. 359 (1929). The only decisions involving mortgagees other than life insurance companies reach the same result. Manomet Cranberry Co., 1 B. T. A. 706 (1925) (market value held immaterial); Ewen MacLennan, 20 B. T. A. 900 (1930) (market value ignored).

18. See Louisville Joint St. Land Bank v. Radford, 295 U. S. 555, 594, n. 24 (1935). Although redemption statutes have not proved successful in enabling the mortgagor to refinance himself within the period allotted, the threat of possible redemption has benefited him by inducing the mortgagee to bid more than he otherwise would. See National Life Ins. Co. v. United States, 4 F. Supp. 1000, 1010 (Ct. Cl. 1933); Durfee and Doddridge, *supra* note 9, at 839 *et seq.*

for another. The deal could be treated as a non-taxable exchange, the land standing in place of the debt until resale,¹⁹ when any sum received in excess of the principal would be taxed as income up to the amount of the accrued interest, and anything beyond that as a capital gain.²⁰ While this procedure avoids the administrative difficulties of determining fair market value, it is contrary to the dominant trend away from the notion that, to be realized, income must be received only in cash.²¹ For this reason, a more acceptable method would be to regard the foreclosure sale simply as a transfer of property in exchange for the cancellation of a debt.²² Determination of whether or not any interest was received would depend on the market value of the land. Although the bid price would still be presumed to be indicative of such value, it would not be accorded the conclusiveness given to it by the court in the principal case, but could be rebutted by evidence of actual market value.²³ This procedure is followed in determining whether income has been received in the form of accrued interest when, instead of bidding at a foreclosure sale, the creditor obtains the mortgaged property by voluntary conveyance and cancels the debt in return;²⁴ and there seem to be only formal grounds for differentiating the two situations.²⁵ Moreover, the ob-

19. This is the method formerly used for determining gain or loss when a creditor other than a life insurance company bought in mortgaged property for the amount of the debt. U. S. Treas. Reg. 62, Art. 153 (1921); U. S. Treas. Reg. 65, Art. 153 (1924). In 1926 it was superseded by the method described in note 14, *supra*. 371 C. C. H. 1937 Fed. Tax Serv. ¶209.025. Application of the above regulations was never extended beyond the principal of the debt; when the bid price included the accrued interest, the interest was held taxable. *Manomet Cranberry Co.*, 1 B. T. A. 706 (1925).

20. In other words, the interest would be considered uncollected until actually received in cash. The differentiation of the excess into interest and capital gain is important because of the difference in the rates for taxing the two and because life insurance companies would be taxable only on the interest.

21. 1 PAUL AND MERTENS, FEDERAL INCOME TAXATION (1934) §10.01. Receipt of the equivalent of cash may constitute income even where the taxpayer is reporting on a cash basis, provided he has power to convert into cash. *Magill, When is Income Realized?* (1933) 46 HARV. L. REV. 933, 934; MAGILL, TAXABLE INCOME (1936) 201-204. The primary purpose of this doctrine is to prevent tax avoidance through indefinite postponement of receipt of cash. 1 PAUL AND MERTENS, *supra* §11.04.

22. That is, that the taxpayer has been paid in property as the equivalent of cash. This is to be distinguished from the constructive receipt doctrine. See note 6, *supra*. Both cash and equivalent-of-cash income may be constructively received.

23. The presumption of an even exchange is predicated on the theory of an open market sale between a willing buyer and a willing seller. Where the situation has clearly been shown to be otherwise, the courts have found the property received to be of a value different from the price paid. *Troxel Manufacturing Co.*, 1 B. T. A. 653 (1925); *Herbert N. Fell*, 18 B. T. A. 81 (1929); *Suncrest Lumber Co.*, 25 B. T. A. 375 (1932). Under the treasury regulations, taxpayers other than life insurance companies are expressly empowered to rebut the presumption of even exchange in computing deductible loss when, as creditors, they buy mortgaged or pledged property with the debtor's obligations. See note 14, *supra*.

24. *Henry Heldt*, 16 B. T. A. 1035 (1929); *American Central Life Ins. Co.*, 30 B. T. A. 1182 (1934); *Prudential Ins. Co. of America*, 33 B. T. A. 332 (1935).

25. In fact the mortgagee is actually in a worse position when he buys the property at foreclosure sale; for he suffers both a delay in obtaining full title and the

jection that inquiry into fair market value entails administrative inconvenience lacks cogency in light of the fact that the treasury regulations expressly permit such an inquiry for the benefit of mortgagees other than life insurance companies seeking to establish a capital loss arising from the foreclosure sale.²⁶ This method would not deprive the government of revenue to which it is entitled, for the presumption that the bid price and the market value are equal apparently could be rebutted by the government as well as by the taxpayer.²⁷

MANSLAUGHTER CONVICTION OF MOTOR VEHICLE OWNER FOR DEATH CAUSED BY DEFECTIVE BRAKES *

DEFECTIVE brakes were the proximate cause of an accident in which a roofer's truck struck and killed a pedestrian.¹ A New York statute provides that "Every motor vehicle . . . shall be provided with adequate brakes . . ."² and that a violation of this section shall constitute a misdemeanor.³ The owner and his driver, both of whom knew that the truck's brakes were defective, were found guilty of second-degree manslaughter based on culpable negligence,⁴ although the owner was not in the vehicle at the time of the accident.⁵

The case represents a rare instance of manslaughter conviction of a motor vehicle owner absent from the scene of the accident; and one of the very few manslaughter cases based on knowledge of defective equipment. The expansion of vicarious civil liability, aimed primarily at compensating parties injured by motor vehicles,⁶ has been accompanied by a striking neglect of the

burden of high foreclosure costs. *Midland Mutual Life Ins. Co. v. Commissioner of Int. Rev.*, 83 F. (2d) 629, 631 (C. C. A. 6th, 1936); 1 PAUL AND MERTENS (Supp. 1936) § 10.09A.

26. See note 14, *supra*. In almost all cases where property other than money is received, its fair market value has to be determined. PEARCE, *INCOME TAX FUNDAMENTALS* (1937) 34.

27. The treasury regulations providing for the ascertainment of a capital loss at the time of foreclosure state simply that the presumption of an even exchange is not conclusive. See U. S. Treasury Regulations, *supra* note 14. Seemingly, either the taxpayer or the Commissioner may introduce evidence in rebuttal.

* *People v. Rauch and Washington*, Queens County Ct. N. Y., N. Y. Times, Feb. 26, 1937, p. 10, col. 5.

1. There was evidence of faulty steering mechanism as well. Apparently the conviction might have been based on either defect.

2. N. Y. VEHICLE AND TRAFFIC LAW § 15. 1.

3. *Id.* § 70. 1.

4. N. Y. PENAL LAW § 1052 defines the common law crime of manslaughter.

5. *People v. Rauch and Washington*, Queens County Ct. N. Y., N. Y. Times, Feb. 26, 1937, p. 10, col. 5.

6. Nixon, *Changing Rules of Liability in Automobile Accident Litigation* (1936) 3 LAW & CONTEMP. PROB. 476. There would be little question of the civil liability of the owner as well as the driver in the principal case. 5 BLASHFIELD, *CYCLOPEDIA OF AUTOMOBILE LAW AND PRACTICE* (perm. ed. 1935) § 2923; 7-S HUDDY, *ENCYCLOPEDIA OF AUTOMOBILE LAW* (9th ed. 1931) § 88.

possibilities of criminal responsibility as a preventive or deterrent force. Occasionally automobile owners riding as passengers have been convicted of manslaughter where death resulted from allowing a chauffeur to drive recklessly,⁷ or from permitting an intoxicated⁸ or otherwise incompetent⁹ person to take the wheel. But in every instance the owner was in the car and his criminal liability arose from his opportunity to control the driver, and not from mere ownership.¹⁰ Seldom have automobile owners as such been held criminally liable, and then only in the field of minor offenses punishable by fine.¹¹ Perhaps the lack of precedent to support the manslaughter conviction of the absent owner in the principal case can be explained by an apparent oversight of the dangers of unsafe mechanical equipment attending emphasis upon the personal factor. For even the drivers of cars have rarely been convicted of manslaughter for deaths resulting from known faulty equipment,¹² and then usually other evidence of negligence was influential in securing the conviction.¹³ Almost invariably their liability has rested upon charges of driving while intoxicated, flagrant recklessness, or the violation of state statutes regulating the manner of operation.¹⁴

The conviction of the truck owner in the principal case, although unique, is not without support from familiar concepts of criminal law. Liability is imposed upon him not as owner, nor as employer, but as a party to the crime.

7. *Moreland v. State*, 164 Ga. 467, 139 S. E. 77 (1927), (1928) 41 HARV. L. REV. 398; see *People v. Scanlon*, 132 App. Div. 528, 535, 117 N. Y. Supp. 57, 63 (3d Dep't 1909).

8. *Story v. United States*, 16 F. (2d) 342 (App. D. C. 1926); *Ex parte Liotard*, 47 Nev. 169, 217 Pac. 960 (1923); *State v. Hopkins*, 147 Wash. 198, 265 Pac. 481 (1928), *cert. denied*, 278 U. S. 617 (1928).

9. *People v. Ingersoll*, 245 Mich. 530, 222 N. W. 765 (1929); *Armstrong v. State*, 48 Okla. Cr. 146, 289 Pac. 1115 (1930).

10. *Story v. United States*, 16 F. (2d) 342, 344 (App. D. C. 1926); *Moreland v. State*, 164 Ga. 467, 472, 139 S. E. 77, 79 (1927). This is emphasized in a similar conviction of one in charge of a car, though not the owner. *State v. Trott*, 190 N. C. 674, 130 S. E. 627 (1925). In another case, ownership was not mentioned. *State v. Leonard*, 195 N. C. 242, 141 S. E. 736 (1928).

11. Massachusetts has imposed absolute responsibility upon the owner for unlawful parking. *Commonwealth v. Ober*, 286 Mass. 25, 189 N. E. 601 (1934), (1935) 33 MICH. L. REV. 443. But *cf.* *People v. Forbath*, 5 Cal. App. (2d) 767, 42 P. (2d) 108 (1935). Under statutes limiting the number of persons to be carried in a vehicle, English courts have fined owner-employers even though their drivers acted contrary to instructions. *Griffiths v. Studebakers Ltd.*, [1924] 1 K. B. 102; *Gough v. Rees*, 142 L. T. R. 424 (1929). But see *Owners and Drivers* (1934) 178 L. T. 287.

12. *Largent v. Commonwealth*, 265 Ky. 598, 97 S. W. (2d) 538 (1936) (defective steering gear); *State v. Wilbanks*, 168 La. 861, 123 So. 600 (1929) (no lights); see *People v. Isbell*, 363 Ill. 264, 266, 2 N. E. (2d) 84, 85 (1936) (defective brakes).

13. *People v. Isbell*, 363 Ill. 264, 266, 2 N. E. (2d) 84, 85 (1936) (high speed); *Largent v. Commonwealth*, 265 Ky. 598, 97 S. W. (2d) 538, 541 (1936) (passing on a hill).

14. *Benton v. State*, 124 Neb. 485, 247 N. W. 21 (1933) (intoxication); *People v. Glasebrook*, 320 Ill. 567, 151 N. E. 489 (1926) (recklessness); *Wilson v. State*, 173 Miss. 372, 161 So. 744 (1935) (speed). For a collection of cases, see 8 BLASHFIELD, *op. cit. supra* note 6, §§ 5379-5389; (1935) 99 A. L. R. 756.

The controlling facts are that the defendant authorized another to operate his truck with bad brakes in violation of statute, and as a proximate consequence a woman was killed. The owner is as guilty of the homicide as the driver according to the unquestioned principle that the accessory before the fact to a lesser crime is likewise accessory to the resulting homicide.¹⁵ Although it has commonly been said that there can be no accessory before the fact to manslaughter because it is by nature an act of the moment,¹⁶ that maxim is inapplicable to "involuntary" manslaughter, where death results from the commission of an unlawful or culpably negligent act¹⁷ or the omission of a legal duty.¹⁸ Thus, paralleling the instant conviction is a case where the defendant counselled the sailing of a steamer with a defective boiler and was convicted of manslaughter following a fatal explosion.¹⁹ Apart from logical concepts, imposition of the penalty upon the truck owner is in fact less severe than the similar treatment of the driver. For the driver probably lacked authority to have the brakes fixed, and, realistically viewed, his choice was to pay the repair bill himself or to surrender his employment. Perhaps he should be allowed to escape criminal liability by reporting defects to his employer, but this would be contrary to the rule that obedience to a master is no defense to prosecution for an unlawful act.²⁰

It is necessary, however, to consider the limitations of the case as a means of enforcing the equipment statutes. Here the jury found both defendants culpably negligent under the circumstances. While the courts have sometimes ruled that where the violation of any statute is the proximate cause of death, the offender is guilty of manslaughter as a matter of law,²¹ in the motor vehicle cases convictions are generally based upon a finding of culpable negligence.²² Accordingly, jurors reluctant to impose heavy penalties may ab-

15. Sayre, *Criminal Responsibility for the Acts of Another* (1930) 43 HARV. L. REV. 689, 703-4.

16. 1 HALE, PLEAS OF THE CROWN (1st Am. ed. 1847) 436; *Bibithe's Case*, 4 Coke 43b (K. B. 1597); *State v. Robinson*, 12 Wash. 349, 41 Pac. 51 (1895). Section 2 of the N. Y. PENAL LAW, a statutory provision common to many states, abolishing the distinction between accessories before the fact and principals, does not solve the logical difficulty that one not present cannot be guilty of an unpremeditated crime.

17. *Regina v. Gaylor*, 7 Cox. C. C. 253 (1857); MILLER, CRIMINAL LAW (1934) § 76; 1 BISHOP, NEW CRIMINAL LAW (9th ed. 1923) § 678. See cases cited in notes 7, 8, 9 *supra*.

18. *United States v. Van Schaick*, 134 Fed. 592 (C. C. S. D. N. Y. 1904); *cf. Rex v. Russell* [1933] Vict. L. R. 59, (1934) 47 HARV. L. REV. 531.

19. *State v. McVay*, 47 R. I. 292, 132 Atl. 436 (1926), (1926) 40 HARV. L. REV. 321, 25 MICH. L. REV. 72.

20. *Smith v. District of Columbia*, 12 App. D. C. 33 (1897); CLARK AND MARSHALL, CRIMES (3d ed. 1927) § 195; MILLER, CRIMINAL LAW (1934) § 81.

21. *Wilson v. State*, 173 Miss. 372, 161 So. 744 (1935); *State v. Rountree*, 181 N. C. 535, 106 S. E. 669 (1921). For an extreme case disposing of the requirement of proximate cause, see *Keller v. State*, 155 Tenn. 633, 299 S. W. 803 (1927).

22. *People v. Black*, 111 Cal. App. 90, 295 Pac. 87 (1931); *People v. Flanagan*, 338 Ill. 353, 170 N. E. 265 (1930); *State v. Stansell*, 203 N. C. 69, 164 S. E. 580 (1932); see also note 14, *supra*. In New York the driver cannot be convicted of first-degree manslaughter based on statutory violation, but is subject only to the penalty of second-

solve owners as well as drivers by finding that the violation of the equipment statute does not constitute "more than ordinary negligence."²³ Another limiting factor is that the owner and the driver admitted knowledge of the defect. It is doubtful whether in the absence of such knowledge either could be convicted, so that the usual difficulty of proving actual knowledge, particularly on the part of an absent owner, may well defeat many prosecutions. Yet conscious wrongdoing is not essential to the violation of the type of statute here involved,²⁴ and, since the "should-have-known" concept is not foreign to criminal law,²⁵ a jury might conceivably be permitted to find the owner or the driver culpably negligent for failure to inspect equipment, and consequently guilty of manslaughter for death resulting from a discoverable defect. Beyond this, there is the remote possibility that the owner, as employer, might be held to an absolute criminal liability for his employee's violation of the equipment statute,²⁶ and consequently guilty of the proximately resulting manslaughter.

Even more speculative is the vulnerability of a corporate owner to manslaughter conviction under circumstances similar to those of the principal case, but the question is significant because of widespread corporate ownership of commercial vehicles. Convictions of corporations for all but the most personal crimes have been increasing,²⁷ sometimes extending even to manslaughter,²⁸ but the decisions are not clear as to whether a corporation may be

degree manslaughter based on culpable negligence. *People v. Grieco*, 266 N. Y. 48, 193 N. E. 634 (1934), (1935) 35 COL. L. REV. 446.

23. See Judge Colden's charge to the jury in the principal case (record not yet printed). This is the common definition of criminal or culpable negligence. *People v. Angelo*, 246 N. Y. 451, 457, 159 N. E. 394, 396 (1927); *Commonwealth v. Gill*, 120 Pa. Super. 22, 34, 182 Atl. 103, 108 (1935), (1936) 10 TEMP. L. Q. 327. Sometimes a definition approximating that of ordinary negligence is used. *People v. Wilson*, 193 Cal. 512, 518, 226 Pac. 5, 7 (1924); *Romines v. State*, 45 Okla. Cr. 40, 46, 281 Pac. 310, 312 (1929).

24. Intent is immaterial to the statutory misdemeanor of operating a car while intoxicated. *State v. Storrs*, 105 Vt. 180, 163 Atl. 560 (1933); *cf. Snyder v. State*, 204 Ind. 666, 672, 185 N. E. 507, 509 (1933) (overloading).

25. *United States v. Wilson*, 59 F. (2d) 97 (W. D. Wash. 1932); *State v. Workers' Socialist Publishing Co.*, 150 Minn. 406, 185 N. W. 931 (1921).

26. Under similar regulatory statutes, such as pure food, liquor and child labor laws, employers have frequently been fined even though their servants acted without their knowledge or consent or against express orders. *DeZarn v. Commonwealth*, 195 Ky. 686, 243 S. W. 921 (1922); *State v. Sobelman*, 271 N. W. 484 (Minn. 1937); *Simpson v. State*, 14 Okla. Cr. 484, 173 Pac. 529 (1918); see Sayre, *supra* note 15, at 713 *et seq.*

27. See Edgerton, *Corporate Criminal Responsibility* (1927) 36 YALE L. J. 827.

28. *State v. Lehigh Valley R. R.*, 90 N. J. L. 372, 103 Atl. 685 (Sup. Ct. 1917), *aff'd* 94 N. J. L. 171, 111 Atl. 257 (1920), (1920) 5 MINN. L. REV. 74; *cf. United States v. Van Schaick*, 134 Fed. 592 (C. C. S. D. N. Y. 1904). *Contra: Commonwealth v. Illinois Cent. R. R.*, 152 Ky. 320, 153 S. W. 459 (1913); *Rex v. Cory Bros. Ltd.* [1927] 1 K. B. 810, (1927) 37 YALE L. J. 118. The New York statutory definition of homicide, as the killing of one human being by another (PENAL LAW § 1042), has been strictly construed to preclude convictions of corporations. *People v. Rochester Ry. & Light Co.*, 195 N. Y. 102, 88 N. E. 22 (1909). A corporation cannot be prosecuted for a

charged with the knowledge and purpose of any of its agents,²⁹ which would of course include vehicle drivers, or only for acts authorized by directors or officers.³⁰ Since the decisive element in conviction of the owner in the principal case is control over the car and driver rather than mere ownership, the individuals directly responsible for the violation and consequent death should be held, regardless of whether the corporation is penalized.³¹ Accordingly, on the basis either of actual knowledge or of negligent failure to discover defects, liability might be imposed on the intermediate agent responsible for supervision and inspection of vehicles.³²

The effectiveness of possible manslaughter convictions as a deterrent force upon owners and drivers who are careless of their equipment may be questioned, in view of the fact that irresponsible persons are evidently willing to take the chance that mechanical defects will not result in a killing. But the same might be said of the accepted treatment of the drunken driver. The action of both prosecutor and jury in the principal case apparently reflects a shift of public sentiment towards recognition that a car without brakes is as great a menace as one in the hands of an intoxicated driver.³³ If the penalty seems severe, compulsory inspection provides a less drastic and perhaps more effective method of securing compliance with the equipment statutes.³⁴

crime when the punishment is only death or imprisonment. *People v. Strong*, 363 Ill. 602, 2 N. E. (2d) 942 (1936).

29. *State v. Pennsylvania R. R.*, 84 N. J. L. 550, 87 Atl. 86 (Sup. Ct. 1913) (railroad indicted for smoke nuisance committed by employees); *People v. Sheffield Farms-Slawson-Decker Co.*, 225 N. Y. 25, 121 N. E. 474 (1918) (dairy fined where delivery man hired child to help him); see *N. Y. Central & Hudson River R. R. v. United States*, 212 U. S. 481, 494-5 (1909).

30. Corporations have been held immune from conviction when the acts were not authorized by officers. *People v. Canadian Fur Trappers Corp.*, 248 N. Y. 159, 161 N. E. 455 (1928); see *American Socialist Soc. v. United States*, 266 Fed. 212, 214 (C. C. A. 2d, 1920); *Grant Bros. Const. Co. v. United States*, 13 Ariz. 388, 395, 114 Pac. 955, 957 (1911). Often the question is ignored. *State v. Lehigh Valley R. R.*, 90 N. J. L. 372, 103 Atl. 685 (Sup. Ct. 1917); *Postal Telegraph-Cable Co. v. Charlottesville*, 126 Va. 800, 101 S. E. 357 (1919).

31. For the argument that fining the corporation penalizes only the stockholders without providing an adequate deterrent to the active officers, see Canfield, *Corporate Responsibility for Crime* (1914) 14 Col. L. Rev. 469, 478. But see Edgerton, *supra* note 27, at 832 *et seq.*

32. Officers of the corporate owner of the steamer "General Slocum," which burned and sank at the cost of 900 lives, were convicted of manslaughter as having aided and abetted the corporation in not providing adequate life preservers, where a federal statute provided the penalty for the owner, but made no mention of corporations or corporate officers. *United States v. Van Schaick*, 134 Fed. 592 (C. C. S. D. N. Y. 1904).

33. Another recent instance of apparently unprecedented action on the part of a prosecutor, again reflecting the public attitude, was the charging of a passenger as accessory after the fact to a hit-and-run driver. *People v. Inch and McCarron*, Queens Felony Ct. N. Y., N. Y. Times, March 26, 1937, p. 1, col. 2.

34. Action has been taken along this line in a number of states. In Connecticut the commissioner of motor vehicles may establish and maintain a system of semi-annual inspections; the registration of a motor vehicle owner who fails to comply will be sus-

THE "PROTECTED" LOAN AS A CONTRACT OF INSURANCE*

THE "PROTECTED" loan is a combination loan and insurance contract which provides for insurance on the borrower's life during the term of the loan, so that the obligation to repay will be cancelled in case of death.¹ This type of contract, in varied forms, has been in wide use during the past twenty years in the industrial banking field.² Recently, with the expansion of industrial banking interests into real estate financing, the insurance feature has been extended to mortgage loans. To both borrower and lender the "protected" loan offers definite advantages. Since the risk of death during the term of the loan is spared both parties, the borrower's property may pass to his family unencumbered, and the lender is freed from the necessity of proceeding against the decedent's estate, a very unsatisfactory method of collection where the loan is small and the borrower impecunious.

Whatever its social desirability, some forms of the "protected" loan tread dangerously near the edge of illegality. An agreement to lend money which provides that the duty of repayment is to be cancelled in the event of the obligor's death is a contract of insurance,³ at least where the transaction is one of a number in a plan to spread the risk.⁴ Consequently, the borrower may set up the loan company's failure to comply with the insurance laws of the state as a valid defense to an action on the debt.⁵ On the other hand, the lender may legally insist that as further security for the loan an existing insurance policy on the borrower's life be assigned to it,⁶ or that a new

pendent. CONN. GEN. STAT. (Supp. 1935) § 617c, amending CONN. GEN. STAT. (1930) § 1603. Cf. MASS. ANN. LAWS (Lawyer's Co-op., 1933) c. 90, § 7A; PA. STAT. ANN. (Purdon, Supp. 1936) tit. 75, § 431; ILL. ANN. STAT. (Smith-Hurd, Supp. 1936) c. 95½, § 26b. In New York inspection is required only for public service vehicles. N. Y. PUB. SERV. LAW, § 61.14.

* Philbrick v. Puritan Corp., 178 Okla. 489, 63 P. (2d) 38 (1936).

1. For a description of how the "protected" loan operates, see HERZOG, THE MORRIS PLAN OF INDUSTRIAL BANKING (1928) 39-44.

2. "Industrial banking" is the business of making small personal loans to salary-earners for consumption purposes. The Morris Plan banks and similar chains confine themselves to this type of loan almost exclusively. Recently, the commercial banks have entered the field, and in 1930, 147 commercial banks maintained small loan departments. See CLARK, FINANCING THE CONSUMER (1931); ROBINSON & NUGENT, REGULATION OF THE SMALL LOAN BUSINESS (1935).

3. Missouri, K. & T. Trust Co. v. Krumseig, 77 Fed. 32 (C. C. A. 8th, 1896), *aff'd on other grounds*, 172 U. S. 351 (1899); Attorney General v. C. E. Osgood Co., 249 Mass. 473, 144 N. E. 371 (1924); State v. Beardsley, 88 Minn. 20, 92 N. W. 472 (1902); Barna v. Clifford Country Estates, Inc., 143 N. Y. Misc. 813, 258 N. Y. Supp. 671 (N. Y. City Ct. 1932); United Sec. Life Ins. & Trust Co. v. Ritchey, 187 Pa. 173, 40 Atl. 978 (1898); see (1924) 23 MICH. L. REV. 191.

4. See VANCE, INSURANCE (2d ed. 1930) 2, 57.

5. See cases cited *supra* note 3.

6. But if the interest charged on the loan is usurious, the assignment of the policy will be void. Connecticut Gen. Life Ins. Co. v. Benedict, 88 F. (2d) 436 (C. C. A. 2d, 1937).

policy be taken out naming the lender as beneficiary.⁷ The duty to repay will then be terminated when the lender receives the proceeds of the policy. Although illegality may be avoided by introducing a licensed insurance company to write the policy, a certain measure of security is lost, for there is generally no assurance that the borrower will maintain the policy in force by punctual payment of premiums. To eliminate this uncertainty, borrowers have been required to pay the insurance premiums directly to the lender, who transmits them to the insurer, and the maturity of the loan is accelerated upon failure to pay premiums on the policy. When the legality of such a transaction is attacked the courts must decide whether the lender, by collecting the premiums, has made its own illegal contract of insurance, or whether it has merely required an insurance policy as security for the loan.

A recent case indicates the difficulties encountered in such a decision. Upon applying for a loan from the plaintiff mortgage company, affiliated with the Morris Plan system, the defendant was required to sign three instruments: a note, a mortgage upon the defendant's home given as security for the note, and an application for an insurance policy on the defendant's life. The policy, naming the plaintiff as beneficiary, was secured from the Morris Plan Insurance Society, another Morris Plan subsidiary, licensed to do business in Oklahoma,⁸ but the premiums were made part of the principal sum of the note and paid directly to the plaintiff, which transmitted the portion of each installment representing the premium to the Insurance Society.⁹ The defendant failed to pay eight consecutive monthly installments on the note, and suit was brought to foreclose the mortgage. Rejecting the defense that the mortgage included a contract of insurance between the plaintiff and the defendant, which was illegal because of the plaintiff's non-compliance with the insurance laws, the court held, one judge dissenting,¹⁰ that the defendant had merely been required to hypothecate an insurance policy issued by an independent company.¹¹

7. A creditor has an insurable interest in the life of his debtor which will support an assignment of an existing policy or a new policy naming the creditor as beneficiary. See *Cammack v. Lewis*, 15 Wall. 643 (U. S. 1872); *Morrow v. National Life Ass'n*, 184 Mo. App. 308, 168 S. W. 881 (1914); see VANCE, *INSURANCE* (2d ed. 1930) 165; Glenn, *Creditor Insurance and Creditors' Rights* (1921) 21 COL. L. REV. 209, 220.

8. The plaintiff dealt exclusively with the Morris Plan Bank of Tulsa, as agent for both the plaintiff and the Insurance Society. But a statute [OKLA. STAT. (Harlow 1931) § 10515] prohibits any corporation from acting as the agent of an insurance company. Although the record does not indicate, it is probable that one of the officers of the Morris Plan Bank of Tulsa, and not the bank itself, was the agent of the Insurance Society. The statute has never been construed by the Oklahoma courts. For the effect of a similar law, see *Cordy v. Hale*, 177 Wis. 68, 187 N. W. 663 (1922).

9. The plaintiff paid the life insurance premium amounting to 1½% of the sum originally loaned in advance for the year to come to the Insurance Society, and then collected it from the defendant as a part of his installment each month. The face value of the policy decreased annually so as to equal the sum due on the note. *Philbrick v. Puritan Corp.*, 178 Okla. 489, 63 P. (2d) 38 (1936), record p. 65, 79.

10. One judge dissented, but when a motion for reargument was denied, a second judge, absent at the first trial, also dissented.

11. *Philbrick v. Puritan Corp.*, 178 Okla. 489, 63 P. (2d) 38 (1936).

It might be argued, as was done in the dissenting opinion, that the plaintiff mortgage company made its own contract of insurance with the defendant entirely apart from the policy with the licensed insurer. This contention finds support both in the facts that the premiums were paid directly to the lender, and that the plaintiff advertised that a mortgage loan need not be repaid in case of death but made no mention of the necessity of an insurance policy. The plaintiff might then be said to have become bound by its offer, even if no insurance policy were ever issued, when the defendant, induced by the advertisement, made formal application for the loan and the plaintiff accepted this application. In that event the insurance policy later obtained would be considered merely a form of reinsurance.¹² However, since evidence of preliminary negotiation at variance with the terms of an integrated written instrument is inadmissible to contradict the written instrument if the latter is complete on its face,¹³ this analysis would be inapplicable to the instant case, because the final mortgage provided that the condition precedent to the cancellation of the note was not the death of the defendant,¹⁴ but payment of the debt either by the defendant or by receipt of the proceeds of the insurance policy.¹⁵ Since the plaintiff did not promise to do anything in the event of the defendant's death, the payment of premiums directly to the plaintiff is not alone so significant as to make the agreement one to insure.

The majority's conclusion may also be questioned, since it was based in large part upon the assumption that the insurance policy was carried by a "wholly independent insurance company"¹⁶ when as a matter of fact the plaintiff and the insurance company were part of the same financial organization. Despite the preservation of two corporate entities, the same Morris Plan interests executed the mortgage and insured the defendant's life. If the corporate forms were to be disregarded because they were part of a scheme to circumvent a legal prohibition,¹⁷ the mortgage and the insurance

12. This is the conclusion that was reached by way of dictum in the similar case of *Missouri K. & T. Trust Co. v. Krumseig*, 77 Fed. 32 (C. C. A. 8th, 1896).

13. *Seitz v. Brewers Refrig. Mach. Co.*, 141 U. S. 510 (1891); *Kilroy v. Schimmel*, 243 Mass. 262, 137 N. E. 366 (1922); *Ruppert v. Singhi*, 243 N. Y. 156, 153 N. E. 33 (1926); see 3 WILLISTON, *CONTRACTS* (Rev. ed. 1936) § 633.

14. By the terms of the agreement the note would not have been cancelled had the defendant died while the insurance company had a valid defense to a claim upon the policy.

15. For a series of cases in which the condition precedent to cancellation of a mortgage was the death of the borrower, see *Missouri, K. & T. Trust Co. v. Krumseig*, 77 Fed. 32 (C. C. A. 8th, 1896); *Missouri, K. & T. Trust Co. v. McLachlan*, 59 Minn. 468, 61 N. W. 560 (1894); *Mathews v. Missouri, K. & T. Trust Co.*, 69 Minn. 318, 72 N. W. 121 (1897).

16. Nowhere in the record was the court advised of the intercorporate relationship of the plaintiff and the Insurance Society. The Industrial Finance Corp., the top holding company of the Morris Plan interests, controls, *inter alia*, two subholding companies, one of which owns the plaintiff Puritan Corp., and the other the Morris Plan Insurance Society. MOODY'S BANKS, INSURANCE, REAL ESTATE, INVESTMENT TRUSTS (1936) 966-9; POOR'S FISCAL VOLUME (1936) 2563-6.

17. *Cf. Chicago, M. & St. P. Ry. v. Minneapolis Civic Ass'n*, 247 U. S. 490 (1918); *United States v. Lehigh Valley R. R.*, 254 U. S. 255 (1920). But *cf. United States v. Elgin, J. & E. Ry.*, 298 U. S. 492 (1936), (1936) 46 YALE L. J. 299.

policy might be declared part of the same agreement. Such a combination, however, would closely approximate "advance insurance,"¹⁸ which has been declared lawful whenever the mortgagee-insurer has complied with the regulations placed upon insurance companies by state law. These regulations are imposed in order to supervise the investments of insurance companies for the protection of those members of the public who are beneficiaries. Although this consideration might have induced the court to say that the statute was inapplicable to a situation where the beneficiary is the mortgagee-insurer itself,¹⁹ there was no necessity for such a decision in the instant case for the Morris Plan Insurance Society is licensed to do business in Oklahoma. On the other hand, if it should seem desirable to supervise the investments of a mortgagee-insurer, it might be thought inadvisable to permit the union of these two businesses, for insurance assets would be concentrated in non-liquid real estate mortgages. But even this objection was satisfied in the instant case, since the insurance risk was borne by a separately incorporated insurance company which segregated its assets from those of the lender and invested them in the manner prescribed by law. Yet there is one further difficulty which a mortgagee-insurer must face. Under some decisions, the premiums payable on a combined mortgage and insurance contract will be computed as additional interest on the loan, and if the total exceeds the legal rate of interest, the transaction will be declared usurious.²⁰ This requirement may have the effect of placing part of the cost of the insurance on the lender—a result which does not seem unreasonable in view of the fact that the insurance benefits him as well as the borrower. But in the instant case it would seem that even this prerequisite to a valid contract had been satisfied, for the total charge to the borrower was slightly under the maximum rate.²¹

18. This is an insurance contract distinguished by the fact that the benefits are paid in advance. The insurance company pays the insured the amount of his policy on the day it is issued, and the insured promises to pay annual premiums until his death. A mortgage on the insured's property is taken as security for the payment of premiums. These contracts were upheld in *United Sec. Life Ins. Co. v. Ritchey*, 187 Pa. 173, 40 Atl. 978 (1898); *United Sec. Life Ins. Co. v. Brown*, 270 Pa. 264, 113 Atl. 443 (1921); *United Sec. Life Ins. Co. v. Perugini U. M. R. Ass'n*, 273 Pa. 554, 117 Atl. 413 (1922); see *United Sec. Life Ins. Co. v. Bond*, 16 App. D. C. 579 (1900).

19. See Comment (1936) 36 Col. L. Rev. 456, 464.

20. *Missouri Valley Life Ins. Co. v. Kittle*, 2 Fed. 113 (C. C. Neb. 1880); *National Life Ins. Co. v. Harvey*, 7 Fed. 805 (C. C. Iowa 1881); *Brower v. Life Ins. Co. of Va.*, 86 Fed. 748 (C. C. W. D. N. C., 1898); *Miller v. Life Ins. Co. of Va.*, 118 N. C. 612, 24 S. E. 484 (1896); *Carter v. Life Ins. Co. of Va.*, 122 N. C. 338, 30 S. E. 341 (1893).

21. In Oklahoma, the maximum rate is 10%. OKLA. STAT. (Harlow, 1931) § 9518. The borrower received \$4000, which he was to pay back in monthly installments of \$44 over a fifteen year period. The monthly installment included the interest on the loan (8% of the unpaid principal) and the premium on the insurance policy (\$60 per year, or 1½% of the original principal). The total of the two would seem to be just under 10%, the maximum rate.

REGULATION OF PICK-UP AND DELIVERY SERVICE BY THE
INTERSTATE COMMERCE COMMISSION*

IN ORDER to check loss of l. c. l. (less-than-carload) freight to competitive intercity highway truckers,¹ railroads have established truck pick-up and delivery service in connection with rail line-haul.² The railroads' use of their own motor trucks between station and shipper's door meets the shipper's demand for complete service, reduces the overall time of transportation,³ and achieves numerous economies resulting primarily from speedier movement of freight through the terminals.⁴ Because these advantages of an integrated rail and truck service were offset, in part at least, by unregulated motor carrier competition particularly in short-haul, l. c. l. freight,⁵ railroads pressed for legislation to regulate this growing competitive branch of the transportation system.⁶ Their efforts culminated in the passage of the Motor Carrier Act.⁷

Recently, the railroads discovered that the Act might be invoked by the trucking companies themselves to protect their own position. Various trucking associations appeared before the Interstate Commerce Commission⁸ to

*American Trucking Associations, Inc. v. United States, 17 F. Supp. 655 (D. D. C. 1936).

1. L. c. l. traffic has suffered a greater loss than any other class—one not explained by the business depression alone. Coordination of Motor Transportation, 182 I. C. C. 263, 283 (1932); MERCHANDISE TRAFFIC REPORT (Federal Coordinator of Transportation, Section of Transportation Service, 1934) 4. This loss is generally attributed to highway truck competition, which serves substantially the same territory as rails. Motor Bus and Truck Operation, 140 I. C. C. 685, 723 (1928); Coordination of Motor Transportation, *supra*, at 374.

2. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 447 (1936). In 1932 a number of eastern railroads provided free pick-up and delivery service for l. c. l. freight moving 260 miles or less, with "plus charges" for longer distances. To a limited extent, pick-up and delivery have been performed by railroads in this country since 1859. *Id.* at 443-445.

3. *Id.* at 457; Motor Bus & Motor Truck Operation, 140 I. C. C. 685, 715 (1928); Coordination of Motor Transportation, 182 I. C. C. 263, 339 (1932). The shipper's desire for a door-to-door service was largely responsible for the growth of highway transportation. MERCHANDISE TRAFFIC REPORT, *op. cit. supra* note 1, at 5 and n. 31.

4. Terminal costs constitute a very large proportion of a railroad's operating expenses and are particularly heavy on l. c. l. freight. Motor Bus & Truck Operation, 140 I. C. C. 685, 715 (1928); MOULTON, THE AMERICAN TRANSPORTATION PROBLEM (1933) xiv, 671; MERCHANDISE TRAFFIC REPORT, *op. cit. supra* note 1, at 9, n. 105. The use of truck pick-up and delivery, by relieving congestion in terminal districts, allows a reduction in number and capacity of freight stations. It also obviates the need for many switching movements, reduces the cost of station handling of l. c. l. freight, and permits heavier loading of cars. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 450; MERCHANDISE TRAFFIC REPORT, *op. cit. supra*, at 5.

5. *Id.* at 326, 362-4 (comments of railroad executives).

6. Coordination of Motor Transportation, 182 I. C. C. 263, 382 (1932); see MCCOLLESTER AND CLARK, FEDERAL MOTOR CARRIER REGULATION (1935) 81, 83-84.

7. 49 STAT. 543 (1935), 49 U. S. C. § 301 (Supp. 1936).

8. Pick-up and Delivery in Official Territory, 218 I. C. C. 441 (1936).

protest the unlawfulness of new tariff schedules by which eastern railroads proposed to establish substantially universal "free" pick-up and delivery service, with a uniform allowance to shippers performing their own service.⁹ They argued that the railroads performing store-door collection and delivery were common carriers by motor vehicle within the meaning of the Motor Carrier Act,¹⁰ and therefore subject to its requirement of obtaining certificates of public convenience and necessity.¹¹ Further, they alleged that since the existing l. c. l. rates for station-to-station transportation were not sufficiently remunerative to cover the additional expense of the pick-up and delivery service, these rates constituted an unfair competitive practice in violation of Section 202 of the Act;¹² to remedy this, the petitioning truckers insisted that compensatory collection and delivery charges should be quoted separately from station-to-station rates.¹³ But while the Commission raised the minimum rate in conjunction with which free pick-up service might be rendered,¹⁴ it otherwise approved the disputed tariffs. The complainants then sought injunctive relief in a federal district court.¹⁵ Without passing upon the question of the petitioner's standing in court to attack the Commission's orders, the three-judge statutory court refused to review the rates authorized by the Commission on the ground that they were not clearly unreasonable, and interpreted the Motor Carrier Act as not requiring railroads to secure certificates of public convenience and necessity before engaging in pick-up and delivery service.¹⁶

9. The new tariffs removed all "plus charges" and provided for a refund of five cents per 100 pounds to any consignor or consignee performing his own service.

10. "The term 'common carrier by motor vehicle' means any person who or which undertakes . . . to transport passengers or property . . . for the general public in interstate or foreign commerce by motor vehicle for compensation . . . including such motor vehicle operations of carriers by rail or water, and of express or forwarding companies, except to the extent that these operations are subject to the provisions of part I." § 203(a) (14), 49 STAT. 544 (1935), 49 U. S. C. § 303(a) (14) (Supp. 1935).

11. § 206(a), 49 STAT. 551 (1935), 49 U. S. C. § 305(a) (Supp. 1935).

12. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 475 (1936). Compare Brief for American Trucking Ass'ns, pp. 43 *et seq.* (argument of protestants based on cost study) with Brief for Eastern Railroads, pp. 48 *et seq.* (rates justified on "added traffic theory").

13. Transport Topics, Aug. 31, 1936, p. 4, col. 2. Local truckmen, particularly, objected to the free service proposed. *Id.*, April 6, 1936, p. 5, col. 1; May 18, 1936, p. 1, col. 2.

14. The Commission, finding that traffic was being handled at an out-of-pocket loss, increased the minimum rate from 30 cents per 100 pounds to 45 cents. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 480 (1936).

15. American Trucking Associations, Inc. v. United States, 17 F. Supp. 655 (D. D. C. 1936). A similar application for an interlocutory injunction was denied in Merchant Truckmen's Bureau of New York v. United States, 16 F. Supp. 993 (S. D. N. Y. 1936), and the petition for a permanent injunction in this case is pending.

16. American Trucking Associations, Inc. v. United States, 17 F. Supp. 655 (D. D. C. 1936).

Apart from the question of statutory interpretation,¹⁷ there would seem to be little practical reason for compelling railroads to obtain certificates. Since the Commission exercises no control over the numerous independent motor carriers engaged in purely intrastate activity,¹⁸ and since the certificate requirement is expressly inapplicable to contract and private motor carriers,¹⁹ imposition of the restriction would not prevent unnecessary duplication of facilities in terminal districts. Moreover, the relatively high degree of financial responsibility of the railroads obviates the need for employing the certificate device as a method of excluding irresponsible units.²⁰

A more useful weapon in securing the ends of the Interstate Commerce Act is the Commission's power to control rates. As already indicated, the Commission may set the minimum line-haul rate with free pick-up and delivery service²¹ so as to eliminate an unremunerative combined rail-motor service for shorter distances more cheaply and efficiently handled by trucks alone.²² Further use of its rate power would remove the discriminatory

17. The language of the Act is ambiguous. See note 10, *supra*. The court reasoned that since the Commission under Part I of the Interstate Commerce Act had taken jurisdiction over the terminal motor operations of railroads long before the passage of the Motor Carrier Act (Part II of the Interstate Commerce Act), it must have been the intention of Congress in adding the proviso, "except to the extent that these operations are subject to the provisions of part I," to exclude rail pick-up and delivery service from the requirements of Part II and to include only the previously unregulated intercity motor vehicle operations of railroads. But the wording permits of a contrary construction that, insofar as railroad terminal motor service is not completely within the regulatory scope of the Commission under Part I, it is included in the provisions of Part II. See *Pick-Up & Delivery in Official Territory*, 218 I. C. C. 441, 499-500 (1936) (Commissioner Lee dissenting).

18. See *McCOLLESTER AND CLARK, op. cit. supra* note 6, c. 15.

19. Contract carriers must obtain permits as a prerequisite to engaging in interstate transportation. These will be granted if the operations are "consistent with the public interest and the policy declared in Section 202(a)." § 209, 49 STAT. 552 (1935), 49 U. S. C. § 309 (Supp. 1936). For a discussion of the distinction between the requirement of a permit and of a certificate of public convenience and necessity, see *McCOLLESTER AND CLARK, op. cit. supra* note 6, c. 26.

20. Shippers can rely on the financial capacity of railroads to reimburse them for goods damaged, lost or stolen in pick-up and delivery service; receiverships and reorganizations have not destroyed the railroads' ability to furnish dependable service.

21. See note 14, *supra*.

22. Truck service is undoubtedly superior for distances under 75 miles and generally up to 150 miles. *Coordination of Motor Transportation*, 182 I. C. C. 263, 376 (1932); *MERCHANDISE TRAFFIC REPORT, op. cit. supra* note 1, at 5, 17. Trucks do not have the burdensome packing requirements of railroads. And their speed and flexibility of schedule, as well as willingness to call for shipments after railroad freight stations have closed, enable them to make early morning deliveries and handle emergency shipments. *Coordination of Motor Transportation, supra*, at 301; *TALBOT, THE SHIPPING SITUATION BETWEEN NEW YORK CITY AND PHILADELPHIA* (1931) 20, 25-26; *MERCHANDISE TRAFFIC REPORT, op. cit. supra*, at 6, n. 43. For a suggestion that coordination cannot be effected through adjustment of rates with the aim of directing movement of traffic to the proper agencies, but only through the formation of unified transporta-

aspects of the present tariff; for the granting of free pick-up and delivery service in conjunction with unaltered rail-haul rates constitutes a rate reduction which, by disregarding the cost differential of the trucking service at different points²³ and by failing to provide for compensating rate revision at those places without the service,²⁴ not only discriminates against shippers and receivers in various localities, but also means probable performance of the function below cost at some points with resulting harm to competing local independent truckers. If the Commission were to require a separate statement of line-haul and terminal charges, these elements of discrimination could be eliminated, and at the same time the Commission would find it easier to determine whether either part of the transportation service is being conducted below cost.²⁵

As a matter of sound business policy, the railroads would probably find it profitable to impose self-limitations upon entrance into pick-up and delivery service; for the idea of integrating this function with rail haul under the management of railroads has an emotional appeal that might easily impel uneconomic action. In certain situations, the railroad companies' employment of only a few subsidiary and affiliated motor companies under contract²⁶ may be ill-advised. Independent local truckmen are familiar with local conditions and individual delivery requirements. Many have trade connections useful in solicitation of freight. And in the smaller towns, where the tonnage is not large enough to warrant a railroad's maintaining a truck and operator, local truckmen can rely upon the support of other business besides the service performed for the rail carrier.²⁷ In these circumstances, to take the business of collection and delivery from the independent draymen is to threaten the loss of a useful ally.

tion companies, see Moulton, *Our Transport Plant is Overbuilt* (1936) 101 Rv. Age 719.

23. In New York City the railroads pay 16.5 cents per 100 lbs. for pick-up or delivery; in Pittsburgh, 10 cents; Philadelphia, 10 and 11 cents; Boston, 9 cents; Buffalo, 8 cents; a number of other cities, 6 cents; and in the majority of towns, 5 cents. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 450 (1936). Thus, in effect, the line-haul rate is reduced disproportionately. See *id.* at 485, 487.

24. Though termed "universal," the service is not rendered at all points. Compare CURLETT, PICK-UP AND DELIVERY SERVICE TARIFF, I. C. C. No. A-524, with SHEFFIELD, LIST OF FREIGHT STATIONS, I. C. C. No. F-3062.

25. See Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 486 (1936); Constructive and Off-Track Freight Stations, 156 I. C. C. 205, 232 (1929).

26. The Pennsylvania Railroad had contracts with only 849 trucking concerns for the service at 1,282 stations, including but 3 concerns at New York City. In contrast, the policy of western carriers at St. Louis and Chicago has been to make contracts with any truck operator conforming to certain qualifications. Pick-up and Delivery in Official Territory, 218 I. C. C. 441, 449 (1936).

27. See SEN. DOC. No. 152, 73d Cong., 2d Sess. (1934) 266.

SUIT BY STOCKHOLDER WHEN DIRECTORS REFUSE TO BARGAIN
COLLECTIVELY WITH EMPLOYEES *

RECURRING controversies between labor and capital have centered around the basic issue of union recognition, for many employers actively combat unionization initially, or else refuse to negotiate with the representatives of already organized employees.¹ From time to time legislatures have devised various expedients to curb the activities of anti-union employers,² and in the recently validated National Labor Relations Act collective bargaining was finally made mandatory in industries affecting interstate commerce.³ While the enactment of similar state statutes⁴ would place a like compulsion upon industries whose activities are under the current definition, not considered to be in interstate commerce, a recent case suggests a device to enforce collective bargaining both where no such statute exists and where there is such a statute but it cannot be enforced by the usual sanctions because the corporate owner has closed its doors.⁵ A minority stockholder, obviously a union sympathizer, brought suit for the appointment of a temporary receiver, the recovery of damages, and a decree compelling the corporation to bargain collectively, alleging that the corporation had been placed in imminent danger of insolvency as a result of a prolonged strike and boycott precipitated by the refusal of the directors to deal with employees. The Circuit Court for Milwaukee County in Wisconsin denied a motion to strike these allegations,⁶ resting its decision principally on the public policy of the state in favor of collective bargaining as expressed in a state statute⁷ similar to the Norris-LaGuardia Act.⁸

A minority stockholder may resort to the courts to protect the corporation against the directors' fraud, gross mismanagement, or illegal or ultra vires acts.⁹ While a refusal to bargain does not constitute fraudulent or ultra vires

*Pieplow v. A. J. Lindemann & Hoverson Co., Circuit Court Milwaukee County, Wisconsin, December 24, 1936.

1. See Magruder, *A Half Century of Legal Influence Upon the Development of Collective Bargaining* (1937) 50 HARV. L. REV. 1071.

2. *Ibid.*

3. 49 STAT. 449 (1935), 29 U. S. C. §§ 151, 157 (Supp. 1936). National Labor Relations Board v. Jones & Laughlin Steel Corp., 57 Sup. Ct. 615 (1937).

4. Such statutes have already been adopted by Wisconsin and Utah. N. Y. Times, April 15, 1937, p. 2, col. 7; (1937) 144 THE NATION 170. A similar New York statute has passed both houses of the legislature and is now awaiting ratification by the governor. N. Y. Times, May 15, 1937, p. 6, col. 2.

5. See N. Y. Times, May 25, 1937, p. 17, col. 1. This device could be similarly used to supplement the National Labor Relations Act, and would be applicable to the other unfair labor practices, besides refusal to bargain, mentioned in these statutes.

6. Pieplow v. A. J. Lindemann & Hoverson Co., Circuit Court Milwaukee County, Wisconsin, December 24, 1936.

7. WIS. STAT. (1935) § 103.51.

8. 47 STAT. 70 (1932) 29 U. S. C. §§ 101, 102 (1934).

9. Hawes v. City of Oakland, 104 U. S. 450 (1881); Bush v. Bonner, 156 Ga. 143, 118 S. E. 658 (1923); Anglo-American Royalties Corp. v. Brentnall, 167 Okla. 305, 29 P. (2d) 120 (1934); 13 FLETCHER, CYCLOPEDIA CORPORATIONS (perm. ed. 1932) §§ 5823-28, 5829 n. 44; 16 *id.* 7714. Before bringing suit the complainant must make reasonable efforts to procure the present directors to redress his grievances. Central

conduct, it may amount to gross mismanagement or illegality. A suit based on gross mismanagement lies, conventionally, when the directors have breached their trust,¹⁰ but not when they have honestly exercised their discretionary powers.¹¹ If the circumstances that give rise to and the results that flow from the same act vary sufficiently, it may be placed in either of these flexible categories on different occasions.¹² Inferences of gross mismanagement are thus sometimes drawn when a course of conduct pursued by directors jeopardizes the financial position of a corporation.¹³ And while the determination of a labor policy would seem to be a typical discretionary act,¹⁴ occasionally a decision may be so ill-advised as to amount to actionable mismanagement. When, as in the instant case, the obduracy of directors in refusing to deal at all with employees occasions a costly and prolonged labor dispute, sufficiently grave to threaten the financial stability of the corporation, there are convincing grounds for asserting that the directors have abused their discretion.

In those states with public policy statutes similar to that of Wisconsin¹⁵ a cause of action may perhaps be stated, in the absence of gross mismanage-

Holding Co. v. Bushman, 238 Mich. 261, 213 N. W. 120 (1927). For a general discussion of minority stockholder suits, see Rohrlich, *Suits in Equity by Minority Stockholders as a Means of Corporate Control* (1933) 81 U. OF PA. L. REV. 692; Glenn, *The Stockholder's Suit—Corporate and Individual Grievances* (1924) 33 YALE L. J. 580; Comment (1936) 45 YALE L. J. 649, 665.

10. The relationship of the directors to the stockholders is said to be that of trustee and cestui que trust. BALLANTINE, *MANUAL OF CORPORATION LAW AND PRACTICE* (1930) 596.

11. The typical statement is that the directors are elected for the very purpose of determining the corporate management policy, and that an error in business judgment, made honestly and in good faith, does not in itself give a minority stockholder a cause of action. *Farmers Loan and Trust Co. v. Hewitt*, 94 N. J. Eq. 65, 118 Atl. 267 (Ch. 1922). The judgment of the directors on questions of management enjoys the presumption that it was formed in good faith. See *Davis v. Louisville Gas and Electric Co.*, 16 Del. Ch. 157, 169, 142 Atl. 654, 659 (Ch. 1928).

12. Compare *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 663 (1919) (extra dividend declared by court), with *City Bank Farmers Trust Co. v. Hewitt Realty Co.*, 257 N. Y. 62, 177 N. E. 309 (1931) (declaration of dividend refused). See 2 COOK, *CORPORATIONS* (8th ed. 1923) § 545.

13. *Gibbons Mfg. Co. v. Milan*, 17 S. W. (2d) 844 (Tex. Civ. App. 1929); cf. *Prairie Lee Production Co. v. Tiller*, 286 S. W. 638 (Tex. Civ. App. 1926). Insolvency or imminent danger of insolvency does not "per se" give rise to a cause of action. *Atlantic Trust Co. v. Consolidated Elec. Storage Co.*, 49 N. J. Eq. 402, 23 Atl. 934 (Ch. 1892). See *Wichita Royalty Co. v. City National Bank of Wichita Falls*, 36 S. W. (2d) 1057, 1059 (Tex. Civ. App. 1931). A cause of action may of course be stated when the corporation is solvent. *Adams v. Farmers National Bank*, 167 Ky. 506, 180 S. W. 807 (1915).

14. See note 9, *supra*. But cf. *Gibbons v. Milan Mfg. Co.*, 17 S. W. (2d) 844 (Tex. Civ. App. 1929).

15. Public policy statements are included in 11 of the 13 state statutes similar to the Norris-LaGuardia Act and in one less comprehensive statute. See (1937) 46 YALE L. J. 1064. The states which have adopted anti-injunction statutes of this type will in all likelihood be the first to adopt acts similar to the National Labor Relations Act. See note 4, *supra*.

ment, by resort to the concept of illegality. While the basis of stockholders' suits for the violation of mandatory statutes has never been clearly indicated, perhaps because of the paucity of cases, courts have been moved for the most part either by considerations of public policy or by a desire to protect the corporation from loss or injury. If the former theory is adopted, redress would clearly be given under the public policy statutes.¹⁶ For even though the corporation was uninjured, a stockholder's suit has been sanctioned not only when the management has violated a positive statute but also when, in the absence of statutory breach, the directors have acted in contravention of public policy.¹⁷ Under the view that an action lies for illegality only when it is accompanied by injury to the corporation,¹⁸ there is more difficulty in establishing a cause of action. If the injury contemplated by the courts is that which would result from the imposition of penalties for statutory violation,¹⁹ manifestly a breach of a public policy statute is not actionable. But if, as some courts have indicated, an illegal act is redressable when accompanied by any harm whatsoever to the corporation,²⁰ a stockholder's suit for a refusal to bargain collectively will almost invariably lie under a public policy statute, since such a course of management generally occasions costly labor strife.

The stockholder's suit gives labor another weapon, of doubtful potency, with which to induce intrastate industries to bargain collectively. Since there will generally be few stockholders in the comparatively small corporations

16. The minority stockholder would then be the enforcing agent of the state's public policy as codified in specific statutory enactment. *Cf.* *Roth v. Robertson*, 64 Misc. 343, 118 N. Y. Supp. 351 (Sup. Ct. 1909); *Thoroughgood v. Georgetown Water Co.*, 9 Del. Ch. 330, 82 Atl. 689 (Ch. 1912); see *Carver v. Southern Iron and Steel Co.*, 78 N. J. Eq. 81, 94, 78 Atl. 240, 246 (Ch. 1910); *Hatch v. Lucky Bill Mining Co.*, 25 Utah 405, 411, 71 Pac. 865, 866 (1903). But *cf.* *Coquard v. National Linseed Oil Co.*, 171 Ill. 480, 49 N. E. 563 (1898); *Skeen v. Warren Irrigation Co.*, 42 Utah 602, 132 Pac. 1162 (1913). The Wisconsin court has interpreted this statute uniquely to give it the effect of substantive law, thereby enabling a labor union, in a suit in its own name, to enjoin the employer from interfering with the right of the employees to associate freely, organize, and designate representatives for collective bargaining. *Trustees of Wis. State Fed. of Labor v. Simplex Sewing Machine Co.*, 215 Wis. 623, 256 N. W. 56 (1934), (1934) 10 WIS. L. REV. 116, (1934) 19 MARQ. L. REV. 49. Under such an interpretation a minority stockholder's suit would not be necessary to enforce collective bargaining, and it is difficult to see why a direct action was not brought by the labor union in the instant case.

17. *Roth v. Robertson*, 64 Misc. 343, 118 N. Y. Supp. 351 (Sup. Ct. 1909); *Central R. R. v. Collins*, 40 Ga. 582 (1869); *cf.* *Harding v. American Glucose Co.*, 182 Ill. 551, 55 N. E. 577 (1899). But *cf.* *Venner v. N. Y. Cent. & H. R. R.*, 177 App. Div. 296, 164 N. Y. Supp. 626 (2d Dep't 1917). See note 16, *supra*.

18. Compare *Harding v. American Glucose Co.*, 182 Ill. 551, 55 N. E. 577 (1899) (injury proven and relief granted), with *Venner v. N. Y. Cent. & H. R. R.*, 177 App. Div. 296, 164 N. Y. Supp. 626 (2d Dep't 1917) (no injury to assets and no relief on similar facts); *Cope v. District Fair Ass'n of Flora, Ill.*, 99 Ill. 489 (1881); 13 FLETCHER, *op. cit. supra* note 9, § 5948.

19. See *Rogers v. Lafayette Agr. Works*, 52 Ind. 296, 304 (1875); 10 FLETCHER, *op. cit. supra* note 9, § 4860, p. 283, n. 8.

20. See *Harding v. American Glucose Co.*, 182 Ill. 551, 626, 55 N. E. 577, 602 (1899).

engaged in intrastate commerce, a union may have some difficulty in instituting an action by purchasing stock in the name of the union or of an officer,²¹ or by persuading a sympathetic stockholder to maintain suit.²² And in any event the practical value of this device may otherwise be limited, for while compulsion, in the form of a mandatory injunction,²³ can be exercised on a corporation which has refused to negotiate with employees if the court concedes the existence of a cause of action, the stockholder's suit will probably have no great prophylactic effect. Should states with public policy statutes once allow a stockholder's action based on illegality, employers, it is true, may hesitate thereafter to refuse to bargain collectively. In other states, however, the mere threat that suit may be brought is not likely to induce corporate directors to deal with employees, since the recognition of a cause of action for gross mismanagement on one occasion would not furnish a necessarily persuasive precedent for a refusal to bargain under different circumstances.²⁴ Directors are more likely to be impelled to deal with employees once an action is actually instituted, especially if the early stages of attack are survived. After the motion to strike in the instant case was overruled, for example, the directors conferred with representatives of the employees and the controversy was settled.²⁵ In the final analysis the effectiveness of the stockholder's suit both as compellent and deterrent will, of course, depend largely on whether or not courts are moved to manipulate the available legal doctrine in accordance with the oft-expressed principle that the public interest and policy²⁶ are persuasive factors in inducing equity to grant relief.²⁷

21. As a holder of stock the union is entitled to the protection of the courts without regard to its motive, or the amount of its holdings. See *Wagner Electric Corp. v. Hydraulic Brake Co.*, 269 Mich. 560, 565, 257 N. W. 884, 886 (1934); *Gordon v. Brucker*, 208 Ill. App. 181 (1917); 13 FLETCHER, *op. cit. supra* note 9, § 5878. Nor is it necessary under the majority rule that the alleged wrongs be committed after acquisition of stock by a complainant. 13 FLETCHER, *op. cit. supra* note 9, §§ 5943, 5920, 5931 and cases there cited.

22. This device was apparently used in the instant case. Objections are sometimes raised on the ground that the complainant is not the real party in interest; but even the nominal party in interest has been allowed to maintain suit where public policy demands. See *Carver v. Southern Iron and Steel Co.*, 78 N. J. Eq. 81, 94, 78 Atl. 240, 246 (1910).

23. See, *e.g.*, *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668 (1919) (extra dividend declared by court). See *Stott Realty Co. v. Orloff*, 262 Mich. 375, 381, 247 N. W. 698, 699 (1933). Damages may prove an inadequate remedy since obdurate directors may be willing to suffer liability to damages rather than submit to collective bargaining, especially since damages will often be insubstantial. *Cf. Mississippi Theaters Corp. v. Hattiesburg Local Union No. 615*, 174 Miss. 439, 164 So. 837 (1936); Comment (1936) 36 COL. L. REV. 776, at 783.

24. See p. 1425, *supra*. It is of course doubtful that an action based on gross mismanagement would be recognized under any circumstances.

25. Communication to the YALE LAW JOURNAL from Max J. Raskin, Milwaukee, Wisconsin, counsel for the complainant in the principal case, April 26, 1937.

26. For a general survey of the progress made by labor in the courts and legislatures, see Magruder, *loc. cit. supra* note 1, Sayre, *Labor and the Courts* (1930) 39 YALE L. J. 682. The danger that this device may be used in "strike" suits is not a persuasive objection.

27. See *Virginian Ry. v. System Federation No. 40*, 57 Sup. Ct. 592, 601 (1937).