The Student Body: 1958

The current student body of the Law School is made up of residents of a great many states, and graduates of an even larger number of universities and colleges. The total enrollment of 352 includes students who make their homes in the following states:

- Alabama
- Alaska
- Arizona
- California
- Colorado
- Connecticut
- Delaware
- District of Columbia
- Florida
- Georgia
- Idaho
- Illinois
- Indiana
- Iowa
- Kansas
- Kentucky
- Maine
- Maryland
- Massachusetts
- Michigan
- Minnesota
- Missouri
- Montana
- Nebraska
- New Jersey
- New York
- North Carolina
- Ohio
- Oregon
- Pennsylvania
- Rhode Island
- South Dakota
- Tennessee
- Texas
- Utah
- Virginia
- Washington
- Wisconsin

Represented also are Hawaii, and Australia, Canada, Egypt, England, Germany, Iraq, Israel, Scotland, Switzerland and Yugoslavia. Counting the District of Columbia, students of the School come from 38 states. Exactly one-fourth are from the city of Chicago; one-fifth are from the College of the University of Chicago. The current entering class was selected from the largest number of applications in the history of the School.

The one hundred eighty-nine colleges and universities represented in the student body are:

- Aberden University
- Aberdeen University
- Albion College
- Albion College
- American University
- American University
- Amherst College
- Amherst College
- Antioch College
- Antioch College
- Augustana College
- Augustana College
- Baghdad Law College (Iraq)
- Baghdad Law College (Iraq)
- Balliol College, Oxford University
- Balliol College, Oxford University
- Bard College
- Bard College
- Barnard College
- Barnard College
- Beloit College
- Beloit College
- Brown University
- Brown University
- University of British Columbia
- University of British Columbia
- Brussels Institute of Technology
- Brussels Institute of Technology
- University of California
- University of California
- Calvin College
- Calvin College
- Carleton College
- Carleton College
- University of Chicago
- University of Chicago
- The Citadel
- The Citadel
- City College of San Francisco
- City College of San Francisco
- Clark Junior College
- Clark Junior College
- Coe College
- Coe College
- Colby College
- Colby College
- College of the Holy Cross
- College of the Holy Cross
- College of Idaho
- College of Idaho
- University of Idaho
- University of Idaho
- Illinois College
- Illinois College
- Illinois Institute of Technology
- Illinois Institute of Technology
- University of Illinois
- University of Illinois
- Indiana University
- Indiana University
- Johns Hopkins University
- Johns Hopkins University
- University of Kansas
- University of Kansas
- Kent State University
- Kent State University
- Kenyon College
- Kenyon College
- Knox College
- Knox College
- Lake Forest College
- Lake Forest College
- Lawrence College
- Lawrence College
- University of Leiden (Netherlands)
- University of Leiden (Netherlands)
- London School of Economics
- London School of Economics
- Louisville Municipal College
- Louisville Municipal College
- Loyola University (Chicago)
- Loyola University (Chicago)
- Macalester College
- Macalester College
- University of Maine
- University of Maine
- University of Marburg (Germany)
- University of Marburg (Germany)
- Marquette University
- Marquette University
- Maryville College
- Maryville College
- Massachusetts Institute of Technology
- Massachusetts Institute of Technology
- University of Melbourne (Australia)
- University of Melbourne (Australia)
- Mercer University
- Mercer University
- University of Miami
- University of Miami
- Michigan State University
- Michigan State University
- University of Michigan
- University of Michigan
- Middlebury College
- Middlebury College
- Mills College
- Mills College
- Millikin University
- Millikin University
- University of Minnesota
- University of Minnesota
- University of Missouri
- University of Missouri
- Montana State University
- Montana State University
- Morton Junior College
- Morton Junior College
- Mount Holyoke College
- Mount Holyoke College
- University of Munich (Germany)
- University of Munich (Germany)
- University of Munster (Germany)
- University of Munster (Germany)
- National University of Mexico
- National University of Mexico
- University of Nebraska
- University of Nebraska
- University of New Mexico
- University of New Mexico
- New York University
- New York University
- Niagara University
- Niagara University
- University of North Carolina
- University of North Carolina
- University of North Dakota
- University of North Dakota
- North Park Junior College
- North Park Junior College
The Philosophy of Midcentury Corporation Statutes

by WILBER G. KATZ

James Parker Hall Professor of Law, The University of Chicago Law School.


In the "New Look" title for this symposium, the Editor suggests a tempting figure of speech concerning fashions in corporation laws. He invites contributors to examine the models now on display and to describe what it is that constitutes the "new look." It might be entertaining to see how far one could spin out the fashion-show analogy. (One uninhibited commentator has, indeed, suggested that the contours of the American Bar Association's Model Business Corporation Act make it a seductive invitation to irresponsibility.) My pen, however, is too heavy for such a task; and the Editor has used the term "philosophy" in defining my subject. What is expected from me, I take it, is a discussion of contemporary theories concerning the purposes of corporation statutes and the provisions appropriate for the accomplishment of those purposes. In trying to meet this assignment, it seems most promising to look not for theories embodied in toto in particular statutes, but for theories reflected in various statutes in different degrees and proportions.

The general purpose of incorporation statutes is to provide a particular legal mold for the organization of business enterprise. If we are to try to be "philosophical," we must begin at the beginning; we must begin with the concept of business enterprise and the function of the law of business organization. For our purposes, analysis of the concept of enterprise discloses three elements: risk, control, and profit. Problems of business organization are problems in the allocation of these elements among the parties to the enterprise. The law of business organization (agency, partnerships, corporations) is principally concerned with (1) defining the area within which parties are free to allocate risk, control, and profit as they wish, and (2) prescribing the allocation of these elements in the absence of express agreement.

I shall be interpreting the general problem of corporate legislation as a problem in regulating the allocation of these elements of enterprise so as to promote responsibility of investment and management. In the simplest type of business unit, the unincorporated one-man enterprise, no such problem arises. Risk, control, and profit are concentrated in the
individual enterpriser. He operates under the general rules of contracts, torts, and property—rules which are backed up by remedial law, including the law against transfers in fraud of creditors. These rules, in effect, assign to the enterpriser (as profit or loss) the consequences of his business decisions. Since he thus takes the consequences, he has an incentive to act responsibly—i.e., to act in the light of reasonable anticipations. To the extent that he does so, his actions are responsible in a broader sense also. Where enterprise is free and enterprisers act responsibly in their own interests, they are led by market disciplines to serve the social interest as well. For our purposes, we need not spell out why this is so, since discussions of the modern corporation invariably assume that individual enterprise has this desirable characteristic. What such discussions question is the relevance of this analysis to the large corporation, with its separation of ownership from control.

It is not only the corporate form of organization, however, which creates problems concerning separation of the elements of enterprise. Such problems arise as soon as the enterprise makes use of employees. Basic rules of agency law deal with these problems and are best understood, it seems to me, as efforts to prevent such separation of risk, control, and profit as would jeopardize responsible management. The rule respondeat superior, always difficult to justify on ordinary tort principles, is understandable as an effort to place the risks of the enterprise upon the enterprise, to require the enterpriser to weigh such risks in making his business calculations. Similarly, the liability of the undisclosed principal, which is hard to explain on contract principles, represents an effort to assure responsibility in the decisions made by the owner of

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The Tax Avoidance Problem in the United States

by Walter J. Blum
Professor of Law
The University of Chicago Law School

The following paper was delivered at the Twelfth Tax Conference of the Canadian Tax Foundation in Winnipeg, Canada, in November, 1958. It is printed here with the kind permission of the Foundation.

I have taken on the task of commenting briefly upon the tax avoidance problem under the United States income taxes.

Let me begin by defining the problem. I conceive of it as centering on the question of what is to be done about efforts of taxpayers to minimize their taxes by arranging their affairs in more or less abnormal or forced ways so as to comply literally with statutory provisions that confer certain tax advantages. Please note that I have narrowed the topic somewhat. Excluded from it are attempts to stretch or distort accounting judgments or classifications in computing taxable income. Also left out are efforts to defraud the government by willfully and knowingly making out a false return, or by manufacturing untrue evidentiary documents, or by doing the numerous things that are commonly regarded as tax crimes.

My subject concerns the gentle and sophisticated tax dodger who hopes to succeed by taking advantage of the law rather than by disobeying it. Fortunately, I am not called upon to locate a precise line of demarcation between tax avoidance and tax fraud or evasion.

Our campaign against the tax dodger has been anchored mainly in the judiciary and legislature. While the Treasury has attempted to combat avoidance in the promulgation of regulations, this activity has been of secondary importance, except where the statute confers special power on the administrators in avoidance situations. Some commentators have suggested that the most logical way to deal with the whole tax dodger problem would be to invest the Treasury with broad substantive power to refine the statutory rules in response to taxpayer ingenuity. There is, however, virtually no support for undertaking so far reaching a reform in our tax system. On the contrary, the impartiality of the Treasury is still widely questioned.

The courts generally have been in the forefront in dealing with the avoidance problem. From the judicial perspective, the central question can be restated as this: Under what circumstances is formal compliance with the explicit terms of the statute enough to attain a tax advantage which it purports to confer? Obviously this is basically a matter of statutory interpretation. But it is one of peculiarly vital importance for our tax structure. If the courts were to hold the view that form always must prevail (unless the legislature has specified otherwise), tax dodging would be too easy, the public would soon become disturbed, and the voluntary compliance foundation of our system would be weakened. If the courts were to take the extreme opposite view that form need never prevail (unless explicitly provided by statute), tax law would become too uncertain, and the resulting chaos would materially impede business and financial operations. Our courts understandably have chosen a middle ground: form must sometimes prevail but not always. And thus we face the basic judicial problem of under what circumstances is it to prevail?

In reading the innumerable decisions in which this question was at issue, one is not likely to find many comfortable answers. In part the difficulty lies in the rhetoric of saying that a taxpayer is free to arrange his affairs so as to minimize taxes, and that a tax savings motive is immaterial in applying the statutory rules (unless the statute states otherwise). This kind of talk by courts solves nothing. The intent to minimize taxes cannot control the question whether form should prevail because almost all rationally planned business transactions do take taxes into account; and

Professor Walter J. Blum.
it should be equally plain that if such an intent were not present, there would be no tax dodger problem.

Another part of the difficulty is that decisions often seem to be by invective alone. It appears that the taxpayer loses because something he has done is said to be a “sham” or “artifice,” or “device” or even worse. Such a finding might be a sound basis for decision where the taxpayer has represented that he has done something—such as organized a corporation—when in fact he has done nothing of the kind. In the cases we are dealing with, however, the taxpayer in fact has followed the form he has selected, even though he chose it only because of tax considerations. To call one of these transactions a sham is merely a way of stating the conclusion that the form is not controlling, without telling us why adherence to form in the particular case was not acceptable. It probably is also a way of revealing the emotional reaction of the court to the taxpayer’s cunning.

A similar trouble is encountered in decisions which go against the taxpayer on the precept that the tax result is to be governed by what was actually done rather than by some declared purpose, or that the transaction under scrutiny is not in fact what it appears to be in form. These are both ways of stating that in the particular case substance is to govern over form, but in themselves they fail to teach us why these cases differ from the many situations in which form does control.

Equally unenlightening are most of the decisions which rest merely on a purported discovery of a more or less particularized legislative intention. Almost always the actual controversy arises because the legislature has not provided a sufficient guide on the point and the court is called upon to repair the omission. Although judicial deference to legislative intention is statesmanlike, it need not obscure the fact that

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The High Court of the Trust
Territory of the Pacific Islands

The author of this article, The Honorable Philip R. Toomin, a member of the Law School Class of 1926, engaged in private practice of law in Chicago prior to his appointment as Associate Justice of the High Court of the Trust Territory. At the invitation of the Record, he has provided us with this description of the organization and work of his court.

Five thousand miles west of San Francisco sits an unique court of the United States, carrying on its daily business despite conditions of discomfort, hardship, and occasionally peril. Its territorial jurisdiction is probably the largest in the world, and its jurisdictional subject matter practically unlimited. People who come before it speak nine languages, none except their own being intelligible to any of them, and none being intelligible to any member of the court.

No appeal lies from the final decisions of this tribunal, nor is it bound to accord more than polite recognition to the decisions of the United States Supreme Court. Moreover, in order to become a working member of this court, it is necessary to pass the United States drivers’ road test, since the only method of transportation on land is by truck or jeep. This exposes the court to the charge that its opinions are prepared by truck drivers. While this is in a sense true, it is hoped they also reveal some influence of the legal scholar.

Half of the year is spent by the two justices in circuit-hopping to the various judicial centers in an area of some 3,000,000 square miles of water and 657 of land. Travel is by plane, by freighter, launch, and jeep; if necessary, it would be by outrigger canoe.

This court is known as the High Court of the Trust Territory of the Pacific Islands. These islands are those formerly mandated to Japan, in the Marianas, Marshalls, and Carolines groups, now under United States Trusteeship. They fan out to the southwest and southeast from Guam, which is the administrative center of the administration, though not included in the trusteeship. Included are famous battlefields of World War II such as Saipan, Peleliu, and Kwajalein, and the scenes of atomic bomb testing at Eniwetok and Bikini.

One of the sources of irritation in the relations between the United States and Japan in the 1930’s was the persistence of the latter in fortifying these islands in violation of its mandate from the League of Nations. It will be remembered that one of the first acts of Japan, after its declaration of war against Germany in 1914, was the seizure of these islands. Upon confirmation by the League of its control as mandatory power in 1920, Japan undertook to incorporate the islands into its economic orbit. Its control was complete and direct. Administrators from Japan took over direction of political and economic affairs, with comparatively few posts being allocated the island populations. Production of crops was geared to the needs of Japan’s expanding economy, and colonization went on at an accelerated pace, until finally many of the principal islands counted more oriental migrants than indigenous inhabitants.

After 1935, when Japan withdrew from the League of Nations, its economic control over the islands was broadened in keeping with the needs of its military machine. Many of the fine harbors and their approaches were fortified, airstrips were installed, and the principal islands dotted with military installations and supply depots.

In 1944, the roll back of Japanese colonization and development started with the United States invasion of the Marshalls, and terminated with surrender of the Palau group the following year. As each island group surrendered, its administration passed to the Department of the Navy.

Initially the only administration the Navy was authorized to establish was strictly military, in accordance with the international law of belligerent occupation. The legal system applied was that of the military government, with law and order enforceable by the military forces, and only such civil rights recognized as accorded with the needs and views of the military authorities.

After creation of the United Nations, however, the situation changed, with the acceptance by the United

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The Planning Committee of the Eleventh Annual Federal Tax Conference sponsored by the Law School, with a number of the Conference speakers. A detailed report of the Conference will be found in this issue of the Record.
The Eleventh Annual Federal Tax Conference

In the last week in October, the Law School, for the eleventh successive year, sponsored its annual Conference on Federal Taxation. The Conference, which was held in the auditorium of the Prudential building, is intended to present an analysis of principal current issues in federal taxation, by authorities in the field. It is a three day long affair, which this year attracted about four hundred fifty lawyers, tax accountants, corporate executives who work with tax problems, and representatives of the Internal Revenue Service. The Planning Committee which arranged the Conference consisted of: John Potts Barnes, MacLeish, Spray, Price and Underwood; Walter J. Blum, Professor of Law, The University of Chicago Law School; Charles W. Davis, Hopkins, Sutter, Owen, Mulroy and Wentz; Frederick O. Dicus, Chapman and Cutler; William M. Emery, Chairman, McDermott, Will and Emery; William N. Haddad, Bell, Boyd, Marshall and Lloyd; James D. Head, Winston, Strawn, Smith and Patterson; Paul F. Johnson, Ernst and Ernst; Robert R. Jorgensen, Sears, Roebuck and Company; William A. McSwain, Eckhart, Klein, McSwain and Campbell; James M. Ratcliffe, Assistant Dean, The University of Chicago Law School; Frederick R. Shearer, Mayer, Friedlich, Spiess, Tierney, Brown and Platt; Michael J. Sporrer, Arthur Andersen and Company.

The program of the Conference was as follows:

ADDRESS OF WELCOME
Donald L. Cartland, Comptroller, The University of Chicago

THE ACTIVITIES AND INTERESTS OF THE
CHIEF COUNSEL
Arch Cantrall, Chief Counsel, U. S. Internal Revenue Service; Washington

FRINGE BENEFIT PROGRAMS
Matthew F. Blake, of Hardman and Cranston; New York

PROBLEMS ENCOUNTERED IN VALUING
INVENTORIES
Everett C. Johnson, Arthur Andersen and Company

TRUSTS AND THE GRANTOR
James P. Johnson, of Bell, Boyd, Marshall and Lloyd

TAX CAUTIONS IN ESTATE PLANNING
Anderson Owen, of Hopkins, Sutter, Owen, Mulroy and Wentz

PANEL DISCUSSION OF TWO PREVIOUS TOPICS:
Frederick O. Dicus, of Chapman and Cutler
James P. Johnson, of Bell, Boyd, Marshall and Lloyd
Anderson Owen, of Hopkins, Sutter, Owen, Mulroy and Wentz
James C. Daubenspeck, of Kirkland, Ellis, Hudson, Chaffetz and Masters
Roland K. Smith, of Isham, Lincoln & Beale

REDEMPTION PROBLEMS – THE HOLSEY AND ZIPF CASES
Robert F. Graham, of Gardner, Carton, Douglas, Roemer and Childsren

CORPORATE ACCUMULATION OF EARNINGS
David Altman, of the Illinois Bar

PANEL DISCUSSION OF TWO PREVIOUS TOPICS:
Charles W. Davis, of Hopkins, Sutter, Owen, Mulroy and Wentz
Robert F. Graham, of Gardner, Carton, Douglas, Roemer and Childsren
David Altman, of the Illinois Bar
Frank H. Urie, of Pope and Ballard
William M. Emery, of McDermott, Will and Emery

CORPORATE SEPARATIONS
Seymour S. Mintz, of Hogan and Hartson; Washington

RECENT DEVELOPMENTS PERTAINING TO
COLLAPSIBLE CORPORATIONS
Irving 1. Axelrad, of Mitchell, Silberberg and Knapp; Los Angeles

PANEL DISCUSSION OF ABOVE TOPICS:
James D. Head, of Winston, Strawn, Smith and Patterson
Seymour S. Mintz, of Hogan and Hartson
Irving 1. Axelrad, of Mitchell, Silberberg and Knapp
Walter J. Rockler, of Ledcerer, Livingston, Kahn and Adsit
Frederick R. Shearer, of Mayer, Friedlich, Spiess, Tierney, Brown and Platt

SUBCHAPTER S-CORPORATIONS
Max E. Meyer, of Lord, Bissell and Brook

LITIGATION POLICY OF THE CHIEF COUNSEL’S
OFFICE IN CIVIL TAX CASES
Paul E. Treusch, U. S. Internal Revenue Service; Washington

PRIORITY OF FEDERAL TAX LIENS
Herman T. Reiling, U. S. Internal Revenue Service; Washington

PANEL DISCUSSION OF SECOND TOPIC:
John Potts Barnes, of MacLeish, Spray, Price and Underwood
Paul E. Treusch, U. S. Internal Revenue Service
Herman T. Reiling, U. S. Internal Revenue Service
Ralph F. Huck, of Chapman and Cutler
Daniel S. Wentworth, Jr., of Chicago Title and Trust Company

INTERNAL REVENUE SERVICE ROUND TABLE
A discussion of procedures and programs of the Internal Revenue Service in dealing with the administration of federal taxation.

Walter J. Blum, Chairman, Professor of Law, The University of Chicago Law School
Charles W. Davis, of Hopkins, Sutter, Owen, Mulroy and Wentz
William N. Haddad, of Bell, Boyd, Marshall and Lloyd
David F. Long, Regional Counsel, U. S. Internal Revenue Service

Wallace T. Morris, Assistant Regional Commissioner, U. S. Internal Revenue Service
Andrew J. O'Donnell, Jr., Assistant Regional Commissioner, U. S. Internal Revenue Service
H. Lloyd Brownlow, Executive Assistant to Assistant Regional Commissioner, U. S. Internal Revenue Service
The Students and Mr. Jenner

Early in each academic year, the Law School sponsors a public lecture, usually on some topic connected with the practice of law or the legal profession, and intended primarily for students who have just begun their work at the School. The lecture is preceded by a dinner for the entering students.

This autumn, the speaker was Albert E. Jenner, Jr., of the Chicago firm of Thompson, Raymond, Mayer, Jenner and Bloomstein. Mr. Jenner has served as President of the Illinois State Bar Association, and is currently President of both the American Judicature Society and the American College of Trial Lawyers. His topic was "The People's Privileged Few." The text of Mr. Jenner's lecture will appear in the Winter Quarter, 1959, issue of the Law School Record.

Prior to the lecture, the Faculty and entering students were joined at dinner by the members of the Visiting Committee of the Law School, and members of the Board of the Law School Alumni Association. In addition to informal photographs of the evening's events which may be found on this, and contiguous pages, several pictures of members of the Visiting Committee and of the Alumni Board may be found elsewhere in this issue of the Record.

Albert E. Jenner, Jr., Esq., of the Visiting Committee, speaking in Breasted Hall.

Before the dinner for entering students, Laird Bell, JD’07, LLD’53 (hon.), member of the Visiting Committee and former Chairman of the Board of Trustees of the University, chats with Hon. Walter L. Pope, JD’12, Judge of the U. S. Court of Appeals for the 9th Circuit; San Francisco, and Justice Walter Schoefer, JD’28, of the Illinois Supreme Court.

At the reception preceding the lecture by Mr. Jenner, left to right, Kenneth Montgomery, of the Visiting Committee, Glen A. Lloyd, JD’23, Chairman of the Board of Trustees of the University and former president of the Law Alumni Association; John Leary, Associate Director of the American Bar Foundation; Hon. Willis W. Ritter, JD’34, Chief Judge of the U. S. District Court, Salt Lake City, and George Barney, Jr., Trustee of the University and member of the Visiting Committee.
The dinner for entering students, which opened the Autumn Quarter.

Justice Charles H. Davis, JD'31, of the Illinois Supreme Court, with William C. Burns, JD'31, Vice President of the Alumni Association, and Stuart B. Bradley, JD'30, of the Alumni Board.

Albert E. Jenner, Jr., center, who addressed the entering students, talking with Ben Heineman, left, of the Visiting Committee, and Charles A. Bane, '37, right, member of the Alumni Board and Lecturer in Law.
Among the Members of the Visiting Committee of the University of Chicago Law School

Upper right:
Left to right, standing, Thomas R. Mulroy, JD’28, Ben W. Heineman, George E. Hale, JSD’40; seated, Kenneth E. Montgomery, Thomas Sunderland, Hon. Samuel B. Epstein, JD’15.

Lower right:
Left to right, standing, George Ranney, Jr., Frank J. Madden, JD’22, Paul H. Moore, JD’23; seated, Herbert C. DeYoung, JD’28, Hon. Walter V. Schaefer, JD’28, Erwin Roemer.

Below:
Left to right, standing, Laurence A. Carton, JD’47, Owen Fairweather, JD’38; seated, Harry N. Wyatt, JD’21, Hon. Hugo M. Friend, JD’08, Tappan Gregory.
A New Publication

In October, the Law School published the first issue of a new annual, The Journal of Law and Economics. The journal will be devoted to matters of interest to both lawyers and economists. It is edited by Aaron Director, Professor of Economics in the Law School. The first issue contained the following articles:
- British Monopoly Policy 1944-56
  by John Jewkes
- Price Discrimination in Medicine
  by Reuben A. Kessel
- The Economics of Scale
  by George J. Stigler
- The United States Taxation of Foreign Income
  by Stanley S. Surrey
- Managing the Public Debt
  by Herbert Stein
- Competition and Democracy
  by Gary S. Becker
- Economics and the Conservation Question
  by Scott Gordon
- Government and Agriculture: Is Agriculture a Special Case?
  by D. Gale Johnson
- Predatory Price Cutting: The Standard Oil (N. J.) Case
  by John S. McGee
- City Planning: An Analysis of the Content of the Master Plan
  by Allison Dunham

In Memoriam

We note with regret the death of four eminent alumni.

Alison Reppy, JD’22, entered private practice in St. Louis, following his graduation, with the firm of Buder and Buder. He later taught, primarily in the fields of Constitutional Law and Common Law Pleading, at the University of Oklahoma, Rutgers, and New York University. For twenty-two years he edited the New York University Law Quarterly; he founded and edited the Air Law Review. From 1950 until his death he was Dean of the New York Law School.

Albert Stump, JD’17, of Indianapolis, was Democratic nominee for Senator from Indiana in 1926 and 1928. A partner in the firm of Stump and Emswiller, Mr. Stump was considered an authority on medical malpractice law. For more than thirty years, he lectured on this subject at the Medical School of Indiana University.

Robert Redfield, Jr., JD’21, was Robert Maynard Hutchins Distinguished Service Professor of Anthropology at the University of Chicago. One of the most distinguished anthropologists in the history of the discipline, Mr. Redfield spent the major portion of his professional career at the University. Among his many accomplishments should be listed his service as the dean of the Division of the Social Sciences at the University, in which capacity he succeeded in carrying through a sweeping reorganization to create the functioning entity active today. At a memorial service for Mr. Redfield, former Chancellor Hutchins quoted these words of Mr. Redfield’s: “The end of man’s existence is not cooperation. It is not even safety. It is to live up to the fullest possibilities of humanity. And man is human only as he knows the good and shares that knowledge with those to whom he is, in humanity, bound... the movement of man cannot be stayed. We go forward, even toward uncertainty and doubt... it is enough if we can find the effort a significant joy.

Edgar N. Durfee, JD’08, spent his entire professional career in the teaching of law and in legal research. Following his graduation he was for a brief period a member of the faculty of the University of Idaho. In 1911 he joined the faculty of the University of Michigan, where he remained until his retirement. He taught and wrote widely in a variety of fields, including legal history, remedies, and debtor-creditor relations. He was the author of well-known casebooks on Equity and on Security.
The Delegation Grows

We can make no attempt at this time to list completely the alumni who were elected to high governmental positions in November. We congratulate them all and hope to bring news of them as we continue to survey our alumni. As representative of all who were elected we might mention Governor A. A. Ribicoff, LLB'33, of Connecticut; Senator Roman L. Hruska, 32, of Nebraska; Attorney-General-elect Stanley Mosk, '35, of California; and Congressman-elect William S. Boylston, JD'50, of Florida.

Katz—Continued from page 3

a business, to make it impossible for the owner to hide behind an irresponsible agent. This explanation applies also to the common-law liability of secret partners. Furthermore, the rules establishing agents' fiduciary duties and disabilities represent attempts to promote responsible action by agents in the interest of their principals. Again, the rule that agency powers are ordinarily revocable, even when stated to be irrevocable, represents another striking effort to check the irresponsible action which might result from irrevocable separation of risk and control. This interpretation explains also the exception to this rule in the case of powers coupled with an interest or powers given as security. The exception permits one who thus participates in the risks of the enterprise to be given irrevocably a share in its control.

These rules reflect concern lest responsible management be jeopardized by arrangements separating risk, control, and profit. They leave great freedom, however, for the allocation of these elements. For example, one who lends money or sells goods to a partnership may agree to look solely to partnership assets, thus assuming a share of the enterprise risk. A lender may agree to take a share of the profits in lieu of interest, or an employee may do so in lieu of fixed salary. They thus become participants in both the profits and the risks of the enterprise, but without sharing the liability of partners. The variety of these voluntary arrangements for sharing risk, control, and profit is enormous. As already indicated, a primary function of the law of business organization is the setting of limits to the possible variations. When the corporate form of organization is made available by statute, the principal legislative question is whether there are special threats to irresponsibility inherent in the corporate form which require special restraints on the freedom to allocate risk, control, and profit. "Philosophies" of corporate statutes reflect divergent answers to this question. Some of these theories will first be stated briefly; in the next part, representative statutory provisions will be examined to ascertain the relative influence of the various theories; and then we should be in a position to consider whether there is a dominant philosophy of the "new look."

1. The first contemporary theory which I shall consider is the theory that a corporation statute should be merely an "enabling act." Under this theory, the privilege of incorporation with "limited liability" should be made freely available, and promoters should have freedom in defining the scope of the enterprise and in allocating risk, control, and profit through the corporation's security structure. This theory prescribes also that relatively unhampered procedures should be available to meet changing conditions by effecting changes in corporate purposes and security structures.

No special conditions on the use of the corporate form are deemed necessary. This theory implies that decisions for commitment of funds are the individual responsibility of the investor or lender, protected, however, by the law of deceit. Adherence to the agreed allocation of risks is deemed adequately assured by the rules of contracts and fraudulent conveyances; management loyalty is adequately promoted by the rules concerning fiduciary duties and disabilities. This theory reflects also a skepticism as to the effectiveness of protective devices suggested by alternative theories. It is feared also that incomplete legislative protections may result in relaxation of individual efforts at self-protection, efforts which are deemed indispensable if investment decisions are to be responsibly made.

Advocates of the "enabling act" theory reject the notion that a corporation statute should deal with the problem of possible monopoly. This theory, therefore, calls for no limitations of size, duration, purposes, or general powers.2

The "enabling act" theory does not mean that an adequate corporation statute can be simple and brief. To serve effectively as an enabling act, it must make its grants of power and its authorized procedures sufficiently detailed to minimize doubts, including doubts which might arise from previous statutes and their judicial interpretation.

2. The second theory, like the first, is grounded on the premise that the social interest is best served through responsible individual decisions in the furtherance of individual interests. The second, however, reflects a belief that for corporate organization, the basic common-law doctrines of contracts, torts, and agency are inadequate to assure responsible individual decision, that these doctrines should be elaborated and supplemented at various points to make it less likely that agreements as to division of risk, control, and profit may be inadvisedly made or ineffectually implemented.

For example, to provide a setting for responsible in-
detailed provisions as to the relative rights of creditors and shareholders, and of holders of different classes of shares—provisions which leave the parties free to determine these rights, but which formalize the way in which the determination must be made and which provide rules applicable in the absence of contrary determination by the parties. A statute drawn on this theory might spell out the application of the law of deceit in the corporation setting. It might go further and relieve lenders and investors of the burden of asking the appropriate questions, creating affirmative duties of disclosure in order to make it more probable that decisions as to commitment of funds, exercise of voting rights, etc., will be responsibly made. Such a statute might also codify other general rules in their particular application to corporate organization, such as the rules prescribing fiduciary standards of loyalty and prohibiting transfers in fraud of creditors. In such codification, the rules might be strengthened to block evasion opportunities peculiar to the corporate situation. In short, the second theory still looks to individual decisions made with responsibility, but it advocates the creation of a statutory setting fostering such responsibility.

3. The third theory prescribes a more drastic remedy, lest risks be inadvertently assumed and powers inadvisedly exercised. It prescribes restrictions on the freedom of the parties to allocate risk, control, and profit by contract. It conceives the task of the legislature as including that of identifying particular types of allocation which are deemed to jeopardize responsible investment and management. For example, the statutes might outlaw nonvoting stock, prescribe a specified margin of safety for creditors, or require more than a simple majority vote for various corporate readjustments.

A point should be added which is applicable to both...
the second and third theories. Their purpose in attempting to check irresponsible enterprise may be not only to protect the investors and creditors directly involved, but also to reduce the likelihood of financial catastrophes which might destroy the climate of reasonable confidence which business enterprise requires. But whichever may be the dominant motive, the statutes are designed to promote responsible decisions in the interests of investors and creditors. Since the third theory attempts to do this by limiting the area of permissible arrangements, it may fairly be called a “paternal responsibility” theory.

4. The fourth theory is a theory of “social responsibility.” Its adherents disparage the foregoing theories as all but irrelevant to the large corporation with its wide dispersion of ownership among inactive stockholders. It is asserted that management neither can nor should be made wholly responsible to stockholders. Absentee owners who have abdicated control have no ethical basis for a claim that the enterprise be conducted to maximize their return. Furthermore, in many industries, so large a fraction of the business is said to be concentrated in a few large corporations that consumers are inadequately protected by market competition. Similarly, where a single plant employs a large fraction of the labor force of the locality, it is argued that alternate employment opportunities furnish adequate protection against management decisions to reduce operations or to relocate. It is urged that corporate managers should be under no obligation to maximize profit, but should have a wider responsibility; that they should exercise corporate powers in the interest not only of shareholders, but also of employees, customers, and the “general public.” While this theory has been much discussed by philosophers of corporation law, it has almost no reflection in the actual statutes. The one exception is the wide adoption of provisions authorizing corporate gifts to charity. Professor Berle considers the charitable-gift statutes as showing the direction of a “20th Century Capitalist Revolution.”

We shall consider other statutory changes which a “social responsibility” theory might support when we have reviewed the way in which midcentury statutes deal with a representative group of problems and after we have attempted to measure the influence of the first three theories.

II

1. Creditors’ margin of safety

Nineteenth-century corporation statutes embodied in various ways the concept of a capital fund, or margin of safety, for creditors as a substitute for the personal liability of shareholders. The amount of the margin was the par value of the shares issued. The margin requirement was implemented, in varying degrees of effectiveness, by provisions making subscribers liable for the full amount of the par value and protecting this “capital” against impairment through dividends or purchase of outstanding shares. Some of the statutes prescribed a maximum ratio of debt to stock investment, but these provisions were gradually eliminated and the amount of the creditors’ margin left to the will of the incorporators; except for a purely nominal flat minimum. American statutes were, thus, similar to the British Companies Act which W. S. Gilbert lampooned in Utopia, Ltd. According to Gilbert, the statute required of incorporators nothing more than “a public declaration to what extent they mean to pay their debts.”

The American statutes often left serious gaps in the implementation of the margin-of-safety concept. There were sometimes no teeth in the requirement that the capital be paid in, and provisions as to maintenance of capital were commonly incomplete. Of more importance, there were often provisions authorizing reduction of capital without any restriction for protection of existing creditors such as the British requirement of court approval. Authorization of no-par value shares introduced further complexities and doubts. While most of the statutes probably left some place for “stockwatering” liability on no-par value shares, it was doubtful whether the shareholders were required to underwrite the valuation of the entire consideration for their shares or only the portion labeled “stated capital,” excluding any amount allocated to “paid-in surplus.” This became an important question as to par value shares also with the advent of the current practice of issuing shares with an arbitrarily low par value and a large paid-in surplus.

Following the Model Act as revised in 1955, several recent statutes have cleared up the confusion as to paid-in surplus. This has been accomplished by re-
quiring that the consideration for shares, whether par or no-par value, shall be fixed in dollars and by imposing shareholders' liability in terms of par or stated value, but of the full consideration fixed for the shares (subject to good faith valuation of property transferred in payment). The same statutes, however, often leave creditors without protection against distributions in "partial liquidation," even to the extent of the stated capital. The extension or clarification of stock-watering liability in these statutes cannot, therefore, be interpreted as an implementation of the margin-of-safety notion, but merely as an effort to check the obtaining of credit through an intentionally misleading balance sheet.

As already suggested, twentieth-century statutes have often permitted formal reduction of capital without protection of existing creditors. Several recent statutes, following the Model Act, have abolished even the necessity of formal reduction and have authorized dividends out of stated capital in partial liquidation if the articles so provide or if shareholder vote is secured. The limit to such distribution is reached only at the point of insolvency, which is usually defined in recent statutes as an inability to pay debts as they mature in the usual course of business.

Some of the recent statutes, however, retain and revitalize the margin-of-safety concept. Thus, neither Texas nor North Carolina authorizes distributions directly "out of" stated capital, and both put restraints upon distribution of surplus created by reduction of stated capital. Texas dramatically departs from the Model Act by providing that distributions of reduction surplus shall make directors liable to creditors existing at the time of the reduction in the event of later insolvency. North Carolina requires that any distribution of capital surplus (including reduction surplus) must leave assets at least twice the amount of the debts. Both of these statutes appear designed to block distributions which would subject creditors to risks which they might not reasonably anticipate. The Texas provision establishes a limit to creditors' risks in terms of stated capital, but the stated capital may be fixed at an arbitrary minimum. The North Carolina provision cannot be reduced to nominal effect, since it covers not only stated capital, but also capital surplus; the margin originally fixed may be reduced, however, so long as there remains a margin of 100 per cent over debts. None of the statutes contains any substantial requirement of original junior investment.

In this field, therefore, none of the statutes reflects the "paternal responsibility" theory, as do the Public Utility Holding Company Act and chapter ten of the Bankruptcy Act, with their control of debt-equity ratios. What the recent statutes do, in varying degrees, is to protect a margin once established or purported to have been established. They thus illustrate my second theory, clarifying the original agreement or representation as to risk and providing relief by adapting general principles of contracts or deceit. But since most of the statutes take few steps in this direction, they illustrate basically the first or "enabling act" theory, leaving it to creditors to make their own bargains for the limitation of their risk. As a result, elaborate covenants restricting dividends and other distributions and share purchases are now common features not only of bond and debenture indentures, but also of other types of agreements for extension of credit.

2. Promotion and security flotation

Apart from statute, courts have imposed upon corporate promoters duties beyond those established by the common law of deceit. Promoters have been held to be fiduciaries subject to an affirmative duty of disclosure, for breach of which the corporation may, in certain situations, recover. But it has been open to the promoter to avoid this result by having all the shares issued initially to himself, with sales to the public made by him rather than by the corporation. In this situation, the promoter is free from common-law liability, unless his conduct amounted to deceit. It is usually not difficult to arrange the promotion transactions in the form which thus minimizes risk of liability.

The recent North Carolina statute is unique in closing this loophole. It includes within its definition of "watered shares" (which are made subject to cancellation or assessment) all shares issued to promoters for overvalued property which unfairly dilute the holdings of other shareholders to whom adequate disclosure has not been made. Thus, in North Carolina, corporation lawyers can no longer defeat the requirement of disclosure by mere technical arrangement of promotion transactions.

Draftsmen of other corporation statutes have ignored this problem, perhaps because the separate securities acts or "blue sky" laws provide statutory remedies for purchasers of stock. While these statutes are beyond the scope of this symposium, one point may be noted as to how they illustrate the general theories considered in this paper. This is the familiar contrast between the Federal Securities Act of 1933 and the typical state securities law. The federal act, like the North Carolina promoters' profit provision, is a disclosure act; it thus illustrates my second theory, supplementing and reinforcing the law of deceit in order to promote responsible investment. The state securities acts, on the other hand, usually vest in their administrators discretionary power to halt the sale of securities which are deemed to be "unequitable" or which would "tend to work a fraud." For example, under
these statutes, maximum selling commissions are often established and particular types of financing arrangements are forbidden. Such provisions illustrate, or course, my third, or "paternal responsibility," theory. Even the SEC, furthermore, exercises influence on the terms of security flotations not only through its disclosure requirements, but also by conditioning the exercise of its discretionary power to accelerate registration upon compliance with certain approved standards.12

3. Fiduciary duties and their enforcement

Application to corporate officers and directors of the agency standards of fiduciary loyalty has generally been accomplished without the aid of statute. Legislation in this field, however, has been on the increase. A few of the statutory provisions have tightened fiduciary standards. Several recent statutes have flatly forbidden all loans to officers and directors. A few have facilitated derivative suits by subjecting nonresident directors to jurisdiction on constructive service. In general, however, there has been little effort in state legislation to keep corporate fiduciaries away from temptation. State legislatures have not followed the federal lead with devices like the recapture of profits from "short trading"13 or in extending fiduciary duties to dealings with individual shareholders.14 Some of the recent statutes may have actually reduced the force of the common-law rules. For example, many state courts have declared that transactions authorized through the vote of a director adversely interested are voidable regardless of fairness. The North Carolina statute, however, provides that a transaction shall not be set aside if proved to have been "just and reasonable to the corporation" at the time it was approved.15 Several recent statutes, furthermore, authorize the fixing of executive compensation without a disinterested majority in the board and without shareholder ratification. There have been several provisions authorizing stock option plans for executives. Some of these have followed the Model Act optional provision which requires approval by shareholders.16

With respect to enforcement of fiduciary duties through shareholders' derivative suits, recent statutes are primarily concerned with the "strike suit" problem. They continue the trend toward the rule disqualifying plaintiffs who were not shareholders at the time of the alleged wrong. The recent statutes typically authorize indemnification of defendant directors for litigation expenses in cases where the litigation is settled as well as where defendants are judicially exonerated. Most of these provisions follow the Model Act in rejecting both the California requirement of court approval and the New York requirement of reporting to shareholders.17 The North Carolina statute, however, does require court approval.18

A few of the recent statutes include provisions for posting by shareholder-plaintiffs of security for litigation expenses of defendants. Wisconsin gives defendants a right to such security from plaintiffs holding less than three per cent of the shares of any class.19 North Dakota enacts the Model Act optional provision under which no security may be required of plaintiffs whose holdings exceed $25,000 in market value.20 A companion provision authorizes the court, at the end of any derivative suit, to require plaintiffs to pay defendants' expenses if the court finds that the action was brought without reasonable cause.21

On balance, the recent legislation concerning fiduciary duties illustrates the "enabling act" theory, since its major concern has been lest application of common-law doctrines should be unduly restrictive of corporate management.

4. Election of directors

Most American statutes have not regulated the allocation of voting rights as a means of promoting management responsibility to those bearing the ultimate risk. To be sure, provisions for removal of directors, with or without cause, are increasingly common. Removal action, however, can be taken only by shareholders with voting rights, and all of the recent statutes permit denial of voting rights to any class or classes of shares. The statutes have no general requirement of "equitable" distribution of voting power like those of the Holding Company Act and chapter ten of the Bankruptcy Act.22 Nonvoting common shares are permissible, and exclusive voting control may thus apparently be vested in a small, closely-held class of "management shares" representing only nominal investment. Furthermore, express authorization of voting trusts is now customary, usually limited to ten

Ronan E. Degnan, Associate Professor of Law, University of Utah, Visiting Professor at the University of Chicago Law School during the Summer Quarter, 1958.
years' duration, but without time limit under the Wisconsin statute.\(^{20}\) The importance of the statutory freedom to separate risk and voting control is somewhat reduced, however, by the fact that the New York Stock Exchange refuses to list nonvoting common shares. Mandatory cumulative voting to permit minority representation is provided in the Ohio\(^{24}\) and North Carolina\(^{25}\) statutes and in the original Model Act.\(^{26}\) These statutes reflect a belief that, on balance, responsible management is promoted by providing this channel of criticism, notwithstanding the dangers of dissension within the board. Most of the states following the Model Act have chosen the alternative provision for permissive cumulative voting.\(^{27}\) Massachusetts, however, has recently repealed its permissive provision and now has no authorization.\(^{28}\)

5. Preferred shares

"... preferred stockholders are not—like sailors or idiots or infants—wards of the judiciary."\(^{29}\) This dictum of Judge Frank was pronounced in a case involving "noncumulative" preferred stock. Paraphrasing Gertrude Stein, he insisted: "... a contract is a contract is a contract."\(^{30}\) To what extent, we may ask, do preferred stock provisions of midcentury corporation statutes reflect a similar philosophy? To what extent, on the other hand, have preferred stockholders become wards of the legislature? The North Carolina statute has gone farthest in the latter direction. I shall summarize the principal provisions which support this statement and indicate some of the contrasts afforded by other statutes.

Before this is done, however, it should be noted that the North Carolina statute has also some unique provisions designed to obviate troublesome problems of interpretation without limiting contractual freedom. It is provided that preferred shareholders are excluded from participating beyond their stated preferences (dividend and liquidation), unless the language clearly indicates the contrary. Similarly, the amount of any dividend arrearage is to be added to the stated liquidation preference, unless this result is clearly inconsistent with the charter wording.\(^{31}\)

None of the state statutes approaches the kind of standardization of preferred-stock provisions and regulation of capital structures which the Securities & Exchange Commission has developed under the Public Utility Holding Company Act. No state requires, as do these SEC regulations, that holders of preferred stock be empowered to elect a majority of the directors when dividends are in arrears; nor do the state statutes regulate the ratio of preferred to common stock investment.\(^{32}\) The North Carolina statute however, does provide that, regardless of charter language, noncumulative preferred shareholders shall be entitled to a "dividend credit" to the extent that their dividends are earned but not declared in any year.\(^{33}\)

Another unique provision of this statute enables preferred shareholders to protect themselves against distributions of capital surplus to common shareholders in partial liquidation. Such a distribution requires a majority vote of each class.\(^{34}\) (There is no corresponding restriction, however, on the use of the same funds to purchase common shares.) The statute also contains a general prohibition of dividends and purchases of shares if the action would reduce net assets to an amount below the aggregate liquidation preferences of preferred shareholders.\(^{35}\)

Contemporary statutes deal in increasing detail with changes in the position of preferred shareholders through charter amendment, merger, etc. They typically contain express authority for cancellation of arrearages but require approval by preferred shareholders voting as a class, even if the class has no voting rights in elections of directors. Following Delaware, North Carolina requires only a simple majority of the class,\(^{36}\) while the Model Act requires two-thirds.\(^{37}\) The North Carolina statute adds a caveat: "No inference shall be drawn from the broad power of amendment conferred by this chapter that an exercise of that power in a particular case is fair and equitable."\(^{38}\) Contrary to the Model Act, appraisal rights are given to dissenting preferred shareholders in certain cases.

John P. Stevens, of Rothschild, Hart, Stevens and Barry, Chicago, Lecturer in Law for the Summer Quarter, 1958.
of charter amendment as well as merger, and an appraisal floor is set at two-thirds of the liquidation preference if junior shares participate in the plan without contribution.

The North Carolina draftsmen removed one of the sources of the pressure sometimes exerted upon preferred shareholders to agree to a reduction of their rights. In states where dividends out of current earnings are forbidden when capital is impaired payment of preferred dividends may require a reduction of capital, which common shareholders are in a position to block. The North Carolina statute not only permits payment of preferred dividends out of current profits when capital is impaired, but also makes this provision override any charter limitation to the contrary. Purchases of preferred shares at prices depressed by suspension of dividends are somewhat restricted by the requirement of prior notice of intention to make such purchases. Under the Texas statute, no shares may be purchased when dividends are in arrears.

Most of the recent statutes have no similar provisions restricting the allocation of risk, control, and profit among holders of various classes of shares. They leave it to investors in preferred shares (as they do to creditors) to bargain out acceptable protective provisions.

III

The foregoing summary makes clear that the recent statutes reflect, in general, an "enabling act" theory, more or less modified by the theory that corporation statutes while assuring freedom of contract, should reinforce in various ways the responsibility of individual decisions; and the theory that freedom of the parties should be limited in order that the results of responsible freedom may more nearly be approximated. Only the North Carolina statute has gone very far in applying the latter theories; it thus has a kind of "new look" which is conspicuous in the parade of new statutes.

Apart from this almost unique design, what is there in the other recent statutes, particularly those patterned after the Model Act, which justifies the term "new look"? It is sometimes suggested that the novelty of design is to be appreciated by contrasting the Delaware General Corporation Law. A principal draftsman of the Model Act reported the opinion of the American Bar Association Committee that the Delaware Act is poor in sequence and loose in its provisions. . . . It bids for the corporate business of promoters. It makes little or no effort to protect the rights of investors. Hence, in the opinion of the committee, it was not the type of statute which the committee should present as a model. . . . The model act makes use of only one provision of the Delaware statute and that is the provision empowering corporations to indemnify their directors. . . .
Some Members of the Class of 1908 on their Fiftieth Anniversary

The Honorable Hugo M. Friend, Judge of the Illinois Appellate Court.

Albert L. Hopkins, of Hopkins, Sutter, Owen, Mulroy and Wentz, Chicago.

Luther D. Swanstrom, Assistant United States Attorney, Chicago.
C. Arthur Bruce, of Memphis, Tennessee, Chairman of the Board of the E. L. Bruce Company of Memphis.

Thurlow G. Essington, of Essington, McKibbin, Beebe and Pratt, Chicago. Mr. Essington is a former member of the Illinois Senate.

The Honorable Robert L. Henry, of Baltimore, formerly Judge of the Mixed Court of Egypt.
Katz—

Continued from page 19

up and rearrangement of sections, but unwieldy sentence structure still predominates. The Model Act has, indeed, a new look: it is vastly easier on the eyes. (Some of my friends out here in the provinces say that it's the difference between Chicago and New York styles of corporate draftsmanship.)

IV

We have seen that a more or less unmodified "enabling act" philosophy is dominant in most of the recent corporation statutes, as it is in the Delaware statute. It is a curious fact, however, that this philosophy is seldom articulated and almost never defended with confident vigor. Its objective—responsible management in the interests of shareholders—has been under attack for over a generation. The attack has come from many sources—from social philosophers and theologians, from economists and law teachers and business executives.

This movement began with Thorstein Veblen, who caustically depicted the modern corporation, with its inactive stockholders, as a prime example of "absentee ownership." Of greater importance, perhaps, were the pronouncements of corporation executives in the twenties, heralding a new orientation of management loyalty. Henry Ford, in trying to defend his limited dividends against minority stockholder attack, disclaimed any intention to maximize profits and proposed, instead, to reduce prices for the benefit of car buyers and to create more jobs. While the Supreme Court of Michigan flatly rejected this view of corporate purposes, other leading executives espoused the same philosophy. Owen D. Young wrote that he considered himself a trustee not merely for stockholders, but for the corporate "institution"—i.e., for stockholders, employees, customers, and the general public.

In 1932, Adelf A. Berle and Gardiner C. Means, in The Modern Corporation and Private Property, gave strong support to this idea, and their work was widely hailed as a contribution of outstanding importance. Tracing the extent of the separation of ownership from control in the modern corporation, they challenged the ethical claim of the inactive investor to the residual profits of industry. They declared that it seems almost essential if the corporate system is to survive, that the "control" of the great corporations should develop into a purely neutral technocracy, balancing a variety of claims by various groups in the community and assigning to each a portion of the income stream on the basis of public policy rather than private cupidity.

True, when Professor E. Merrick Dodd called for legal recognition of the new principle of wider respon-
sibility, Professor Berle suggested caution. In rejoinder, Dodd insisted that a principle of “vicarious acquisitiveness” has little ethical or emotional appeal either to managers or to the general public. For Dodd, the principle of trusteeship for absentee investors presented a melancholy dilemma: “Abandon it as yet, we dare not—enforce it with more than moderate success, it is to be feared we cannot.”

I have said that the “social responsibility” philosophy has had almost no influence upon recent statutes. The one exception is the now popular authorization of corporate gifts to charity. Even before these statutes, of course, many types of donations were defensible as means of creating consumer or employee goodwill. The recent statutes, however, cover much broader ground. The pressure for corporate giving was a result of tax laws which made it increasingly difficult to finance charities through individual gifts. Congress was induced to provide a limited tax deduction for corporate donations. One cannot dismiss the state statutes, however, as merely dealing with a tax problem. They do represent a limited acceptance of the social responsibility theory, as the New Jersey court recognized in the leading case. Many of the recent statutes, furthermore, have set no limits upon corporate gifts, either in terms of amount or of shareholder approval. Ohio has recently repealed its previous limitations.

As already noted, Professor Berle considers that these statutes are signs of a corporate revolution. Magnanimously, he now concedes victory to Professor Dodd in their 1932 controversy over “To Whom Are Corporate Managers Trustees?” I find it hard to believe that the charitable-gift statutes and practices will prove to be forerunners of a major change. Under the traditional view, risk-taking investment is typically made in the hope not only of cash dividends, but also of appreciation reflected in stock prices and often “realized” through stock dividends and splits with gradually increasing total cash distributions. I see no reason to think that this concept of common stock is soon to be replaced by a concept under which the expectation of stockholders will be limited, like that of holders of perpetual debentures, with no claim upon residual profits. Corporate giving may increase, but it is unlikely that whatever profits are left after “reasonable dividends” will come to be regarded as at the disposal of the directors in accordance with their views of public welfare.

Apart from these provisions for charitable contributions, the new concept of social responsibility has had almost no elaboration. It is not merely that the theory has had no further influence on the actual statutes, but in a quarter of a century, neither the originators of this philosophy nor their disciples have sketched with any detail or persuasiveness the lines of possible practical application. And the few suggestions which have been made justify skepticism as to the seminal quality of the new theory.

In 1954, George Goyder, an English businessman, published The Future of Private Enterprise—A Study in Responsibility. In his view, the weakness of Company Law at present is that the directors are without legal guidance as to their responsibilities to the workers, the consumers or the community. What is wanted is a General Objects Clause, declaring management responsibility for “fair and reasonable prices,” “regular dividends,” “stable employment under good conditions so far as possible,” etc. Once defined, the legal responsibilities . . . of the directors, can be made actionable in a court of law . . .

Nothing could be simpler; but the history of utility regulation and of emergency price and wage controls is soberly relevant. To say the least, standards of “fair” prices and wages are hard to come by, and few lawyers can be optimistic about the litigation process as a mode of developing such standards.

More cautious is the approach of Howard R. Bowen in Social Responsibility of the Businessman, part of a study commissioned by the Federal Council of Churches and published in 1953. Dr. Bowen endorses the “social responsibility” concept, but, as an economist, he recognizes that businessmen are often not in a good position to know how they can best serve society, and their decisions based on the service motive may often hit wide of the target . . . . They need short-cut methods of reaching decisions that do not involve all the complexities of relating every individual action to the social interest. The price system provides that short-cut method. With all its imperfections, it is a marvelous device for registering.
social valuations and thus providing a system of easily recognizable signals by which individuals can reconcile their own self-interest and the social interest. . . . [Thus, the businessman should] rely primarily on profit as his guide. . . . [He should depart from this guide only when it leads him toward] restrictive monopoly, exploitation, fraud, misrepresentation, political bribery, waste of natural resources, economic insecurity, etc.

Here, again, these terms offer little guidance to the conscientious director (except as to misrepresentation and other conduct forbidden by law).

In general, one may question the extent to which socially responsible deliberation would actually lead management to decisions different from those indicated by long-range profit considerations. For example, concern for employee goodwill might well cause management to seek ways to cushion the effects of production cut-backs, automation, plant relocation, etc. If advocates of "social responsibility" would have management go much farther in maintaining unprofitable operations, it is by no means clear that such action would be socially responsible. And with respect to price policy, however seriously management might regard its social responsibility, perhaps the influences operating to further the social interest would still be principally those resulting from competition among products and producers for consumers' spending.69 In any event, management must be concerned with the extent to which the new concept of corporate responsibility may influence behavior of consumers or employees. If public opinion comes to expect corporations to assume some new responsibility, this is a fact which profit-conscious management can not ignore.
Another "reform" proposed in the name of social responsibility is the abolition of shareholder voting rights. This is a measure advocated by Peter F. Drucker after a period as official philosopher-in-residence at General Motors. According to Drucker, "there is absolutely nothing in the nature of investment that either requires or justifies ownership rights, that is rights of control"; voting power should be "vested in perpetuity in the Board of Directors," who would elect to their number "representatives" of investors, management, and the "plant community." Drucker regards this as merely legalizing the disfranchisement already existing in fact. Criticizing this position, Lloyd K. Garrison expressed belief that "upon close examination it will be found that even in the case of the great corporations whose securities are widely distributed and largely voted by management proxies, effective control over many basic policy decisions is lodged in some stockholder group—perhaps in a very small minority, but in an effective one... Drucker brushes aside or disapproves not only the influence of particular stockholders, but also the general influence arising from the possibility of organized opposition. But after recent examples of proxy warfare, it would be rash to assert that these possibilities exert no wholesome stimulus or restraint upon management. When poor management is reflected in reduced earnings, the resulting decline in stock prices may create attractive opportunities to accumulate shares in a bid for control. To be sure, the stock market is not an ideal mechanism for the discipline of management. But, whatever may be the dangers from corporation "raiders," it is at least doubtful that management responsibility would be improved by making it impossible to acquire working control through purchases of stock.

The vitality of the "social responsibility" theory is not to be measured by the limited enthusiasm which these typical proposals have engendered. The theory
is important as a perennial insistence that there just
must be some new way of disciplining corporate profit-
seeking. Expressing his disappointment with Bowen's
report, the Rev. F. Ernest Johnson asked almost
wearily "Is it not possible to devise instruments of a
more authentic corporate responsibility?" But the
prospect of a break-through on this front is not en-
couraging, for what is demanded is a contrivance
which would operate neither through individual re-
sponsibility and competitive markets nor through
political controls.

The new philosophy has thus far succeeded in pro-
ducing only an unresolved discontent with existing
corporation law. It has obscured the values served by
the older philosophies and the fact that these philos-
ophies also can lay claim to the "social responsibility"
label. Perhaps corporation law critics should keep
straining to catch Professor Berle's vision of "The
Modern Corporation and the City of God." But in
the meantime, we need not be defensive about the
statutes of North Carolina and Texas—or even those
of Illinois and Delaware. None of them, to be sure, is
a model ordinance for the City of God. But the cor-
porate organizations they make possible are institutions
not inappropriate for economic activity in the Earthly
City.

FOOTNOTES
1 Harris, The Model Business Corporation Act—Invitation to
2 Recent corporation statutes show almost no traces of the gen-
eral restrictive theory of which the classical statement is the
opinion of Mr. Justice Brandeis in Louis K. Liggett Co. v. Lee,
288 U. S. 517, 541 (1933).
Examples of this theme can be found in the writings of Jerome N. Frank and William O. Douglas. See dissenting opinion of Commissioner Frank in In the Matter of The North American Company, 4 S.E.C. 434, 462 (1939); William O. Douglas, Democracy and Finance (1940).


Cf. Model Business Corporation Act § 41.

Id.


Cf. Model Business Corporation Act § 18A.


Wis. Stat. § 180.05(4) (1953).

N.D. Laws 1957, c. 102, § 44: cf. Model Business Corporation Act § 43A.

Id.

Id. note 10 supra.


Model Business Corporation Act § 41.

Cf. id. alternative § 41.


Id.


the court is supplying the rule to govern the situation in issue.

This brings us to the crux of the judicial dilemma: if a legislative pronouncement on the point is lacking (and I pass over what qualifies as such), how should a court decide whether formal compliance with a given rule is enough? I suggest that, in seeking guidelines for implementing legislation, at best the court can only fall back on an examination of the dominant legislative purpose or theme behind the particular rule or the complex of inter-related rules of which it is a part. Unfortunately courts sometimes seem to believe that they should look further afield in this quest for the statutory drift. They then are in danger of discovering only that the policy of the tax law is to raise revenues for the government. (In one opinion the Supreme Court held against the taxpayer because, among other reasons, it found that the section of the statute in question was an aspect "of the comprehensive tax program enacted by the Revenue Act of 1942 to increase the national revenue to further the prosecution of the great war in which we were then engaged"). When a court properly restricts itself to considering the function and purpose of the rule within the framework of the technical law, as revealed by history and legislative surroundings, it is in a position at least to make an informed judgment whether the thrust of the statutory rule is better promoted by rigid adherence to form or otherwise. Nothing more can be asked of the judiciary.

There has been much argument through the years about the judicial legislation which occurs when a court refuses to apply a rule literally. I should like to remark only that giving a rule literal application is likewise a variety of judicial legislation, except that it generally favors the taxpayers and hence is less likely to draw condemnation from their advisors.

The most celebrated instances of judicial limitations being placed upon literal application of the statutory rules involved corporate reshelings, where, under our statute, different forms for corporate distributions and adjustments carry different tax consequences. It is in this area that the courts frequently restricted availability of the more advantageous form to transactions which were found to have a business purpose and not merely a tax savings motif. Our experience with these judicial versions of the business purpose doctrine nicely illustrate some of the more pronounced consequences of relying on the courts to defeat the tax dodger. Taxpayers are never sure which of the many corporate reshuffling rules will attract the business purpose qualification, and they never know how much (or whose) business purpose...
will suffice. If only a modicum of such purpose is enough, the skilled tax practitioner perhaps can be counted on to arrange for its presence. But if a very substantial dose is demanded, the requirement might defeat many transactions which the business community regards as normal. From the Treasury’s viewpoint, however, the uncertainty might be other than an evil. Taxpayers are forced to operate without a roadmap for successful tax dodging, and the resulting doubts about the terrain clearly have the effect of reducing the magnitude of the problem by discouraging experimentation with novel transactions.

These characteristics of the judicial approach to coping with tax dodging bring us to the legislative efforts. In the main they have followed three patterns.

One has been to specifically qualify certain rules with a broad directive regarding the consequences of a tax savings motive or an absence of business purpose. Legislative directions of this nature have been given a variety of expressions. The taxpayer is to lose if tax avoidance is found to be a principal purpose, or he is to lose only if it is found to be the principal purpose, or only if it is found to be a major purpose; and furthermore, the words with which the burden of proof is placed on the taxpayer have differed in their forcefulness. All such directives, however, have one thing in common. Regardless of their particular phrasing, they embody a kind of circularity. Improper tax minimization is enjoined by requiring a showing that tax avoidance was not high on the list of motivations. But since the transaction, if it passes muster, does result in a tax advantage, and since we can’t expect the rational taxpayer to be blind to this fact, the courts ultimately are required to distinguish between acceptable tax minimization and unacceptable tax avoidance. It is only a slight overstatement to say that the legislative directives inveigh against tax dodging by instructing the courts to strike down instances in which tax avoidance loomed large, without defining what tax avoidance is. The courts thus must determine when minimization constitutes avoidance, and when such avoidance is so large a component of the motivation as to run afoul of the statutory directive. It can be seen that a legislative business purpose rule operates essentially not unlike its judicial counterpart.

An important exception deserves mention. A statutory directive—and particularly one that explicitly puts discretionary power in the hands of the Treasury—is apt to cause taxpayers to seek prior administrative clearance of transactions which conceivably could run afoul of the anti-avoidance doctrine. Possibly the most significant consequence of the statutory directives is to place enormous leverage in the Treasury through its power to rule or refuse to rule on proposed transactions. The wisdom of this result has not gone unchallenged.

A second legislative pattern has been the enactment of specific rules to meet new tax avoidance situations as they are discovered. This approach, for example, has typified our handling of the capital gain versus the ordinary income question presented by bonds issued at a discount and bonds purchased with coupons detached. Its efficacy depends in large part on the willingness of the legislature to backstop the

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Some Indiana Alumni of the Law School

Melvin H. Specter, JD'28, has practiced law in East Chicago for thirty years. He has served as president, or a member of, the Library Board, Red Cross, Salvation Army Board, Community Chest, Brotherhood Week, the Boys Club, and numerous professional organizations. Mr. Specter was cited by the University of Chicago Alumni Association for public service and good citizenship.

L. Albert Wehling, JD'35, head of the department of government of Valparaiso University. He has written widely in the field of public law and government and is a member of two bar associations and four learned societies.

Von E. Livingston, JD'28, is a partner in Campbell, Livingston, Dildine and Haynie, in Fort Wayne, to which city he moved in 1941, after practicing for thirteen years in Chicago. He is a director of four corporations, and has taken a prominent part in the work of the Chamber of Commerce, the Rotary Club, the Executives Club, and a variety of professional and fraternal groups. He is presently Chairman of the Committee on Administrative Law of the Indiana State Bar Association.
John Schindler, Jr., of Mishawaka, is a partner in Schindler and Schindler. He has served as President of the Chamber of Commerce, as a Governor of the County Bar Association, City Attorney, Chairman of the Mayor’s Advisory Committee on Urban Renewal, member of the Committee of 100 of South Bend-Mishawaka, and has been active in numerous other civic enterprises.

The Honorable Norman F. Arterburn, JD’26, has been a Justice of the Supreme Court of Indiana since 1955. Before becoming a member of the Court, he taught law at Washburn College, served as prosecuting attorney, and engaged in the private practice of law for twenty-eight years. Judge Arterburn has engaged in numerous civic activities and written widely for legal publications.

Robert H. Mohlman, JD’41, is Assistant Vice President of the Inland Container Corporation, in Indianapolis. He is a director of the Anderson Box Company, and has served as president of his church, member of the Allocations Advisory Committee of the United Fund of Greater Indianapolis, and Regional Chairman of the Law School Alumni Fund.
Jerome Hall, JD'23, is Distinguished Service Professor of Law at Indiana University, in Bloomington. He was a Special Fellow at Columbia University, Benjamin Research Fellow at Harvard Law School, and has received an honorary Doctor of Laws degree from the University of North Dakota. He was Fulbright Lecturer in the United Kingdom and served the U. S. Department of State as a Specialist on their Educational Exchange Program. Mr. Hall has written widely, principally in the fields of criminal law and jurisprudence.

Richard J. Smith, JD'39, is the owner of Smith Chevrolet, in Hammond. He is Chairman of the Governmental Affairs Committee and member of the Executive Committee of the Chamber of Commerce, and a Great Books leader.

Benjamin Blumberg, JD'13, of Terre Haute, describes himself as retired, although it appears that he is Honorary President of the County Boy Scout Council, Vice President of Indiana Blue Cross, Honorary Life Director of the YMCA, a director of Highland Iron and Steel and of the local taxpayer's association, Past President of the Chamber of Commerce, the United Hebrew Congregation, and a member of more than a dozen other civic, professional and fraternal groups.
Henry R. Sackett, '29, of Gary. Mr. Sackett is a partner in the firm of Sackett, Pyatt and Waitkus. He has served as Deputy Prosecuting Attorney for Lake County, and Assistant United States Attorney. Immediately following the war, Mr. Sackett was Assistant Prosecutor, under Justice Jackson, at the Nuremberg Trials, and later served as an Assistant Prosecutor at the Japanese War Crimes Trial in Tokyo. He is a past president of the Gary Chamber of Commerce.

John E. Newby, Jr., of Newby and Lewis, La Porte. Engaged in the general practice of law, Mr. Newby is president of the Park Board of his city, and active in a variety of other civic enterprises, such as the Chamber of Commerce and the Kewanis Club.

Charles D. Kelso, JD'50, a former law clerk to Mr. Justice Sherman Minton, is Assistant Professor of Law at Indiana University School of Law, Indianapolis.
Joseph J. Wasko, '35, practices law in East Chicago, where he has served as special counsel for the city, and is currently Probate Commissioner of the Superior Court. He has been active in the Red Cross, the Elks, his church, and a variety of bar groups. Mr. Wasko is currently President of the East Chicago Urban Renewal and Redevelopment Commission.

William B. Merrill, JD'28, of Merrill and Reiber, Fort Wayne. In addition to his private practice, Mr. Merrill is presently Associate City Attorney. He has participated in a variety of civic activities, and is currently Deputy Grand Master of the Odd Fellows for the State of Indiana.

Benjamin Piser, JD'27, of South Bend, is in individual practice, with two associates in his office. He is an Associate Editor of the NACCA Law Journal and was Vice President of NACCA in 1957. Mr. Piser is a member of the state Board of the ACLU, and is active in United World Federalists, the Jewish Welfare Fund and the United Fund.
Wayne Guthrie, '22, of the Indianapolis News, is author of the daily column, "Ringside in Hoosierland." Mr. Guthrie has been on the staff of the News since 1921, successively as reporter, assistant city editor, city editor and assistant managing editor. He has spoken extensively, on a national basis, on the atomic bomb tests which he covered at Bikini. In addition to many other civic activities, Mr. Guthrie has three times served as International Chairman of Kiwanis.

Paul B. Huelmer, JD’52, is in practice in Hammond.

Jerome F. Kutak, LLB’28, is President of the Guarantee Reserve Life Insurance Company of Hammond, and of the National Protective Life Insurance Company. He is a director of the Southeast National Bank and of the Life Insurance Company of America. Mr. Kutak has been active in Kiwanis, the Chamber of Commerce, in Masonry, and in a variety of bar associations. His son, Robert, was graduated from the Law School in 1957.
Tax Avoidance Problem in U. S.—Continued from page 29

statute year after year with a considerable mass of mere or less trivia. Even with a completely cooperative legislature, however, the approach cannot avoid the vexatious problem of the innovator. Should the early bird be allowed the advantage which is being denied to others, so that speed and daring in tax avoidance is rewarded; or should the legislation be made retroactive to cover everybody; or should some compromise position be taken? Generally we have shied away from giving our so-called loophole closing measures an effect prior to their date of enactment or introduction into the legislature, probably in the thought that retroactivity is unsportsmanlike and may even be unconstitutional. But we frequently have accompanied them with an expression of committee intention that no inference about the prior law is to be drawn from the statutory charge, thus offering the courts a free hand to make the law for the earlier period. Occasionally we have tried to move in the opposite direction by statements to the effect that the new statutory language is intended only to be declaratory of what is thought to be the existing law. While this procedure may be persuasive with the courts, it cannot serve to bind them.

A third legislative pattern has consisted of dealing more or less comprehensively with a given area of tax law by trying to anticipate the situations which might arise and prescribing specifically on which side of the tax line they fall. The collapsible corporation provisions of our statute are illustrative of this technique. Such highly detailed provisions answer many particular questions which actually arise or might otherwise come up—but at a very real price. Obviously they add considerably to the bulk of the law. It is also evident that the legislature can neither anticipate all the line-testing questions which might arise nor safeguard completely against ambiguity in the many words employed in disposing of the questions covered. Inherent in this technique, moreover, is what some regard as the unfortunate quality of providing tax minimizers with an excellent blueprint of avoidance plans which apparently have received legislative blessing. Specificity and clarity, in brief, make the use of tax savings techniques a lot easier and the code a lot longer.

To this juncture I have considered tax dodging from the standpoint of combating it; I shift now to the perspective of the tax practitioner. While as an informed citizen he might well feel that the artful tax dodge should be checked—although I hope he will take care that the cure is not worse than the irritation—as a practitioner he should avoid confusing ethics and common sense. Since it is the
indeterminacy of the legal rules that is at the heart of the tax avoidance problem, I see no moral or ethical inhibitions against trying out new and doubtful schemes. Practitioners need feel no guilt in sending up trial balloons. But I am convinced that frequently such experimentation represents poor judgment and sometimes verges on being foolish. I mean only that all things considered, including an assessment of the chances of success and the costs of losing, the taxpayer's interests would be better served by taking an alternative path. All too often, from the taxpayer's vantage-point, the real vice of being a tax-minimization pioneer is not that the plan ultimately fails to gain the tax advantage sought, but that in choosing the dodge, the taxpayer foregoes other tax opportunities or business or estate planning openings which are unquestionably available to him.

Permit me to add, parenthetically, that I couple the freedom of practitioners to experiment with a broad license in the administrators to shoot at the trial balloons. Furthermore, it may be that our system is deficient in not penalizing unsuccessful experiments more heavily than now in view of the costs which they impose on the whole legal apparatus.

There is one respect in which the pursuit of tax minimization does or should raise an ethical question for practitioners. All too often the willingness to take the gamble rests not alone on the cleverness of the plan but in part on the thought that the facts as stated in the tax return and accompanying documents will not flag the arrangement for the administrators. Thus it is hoped that the plan may succeed because it is passed over without a test on the merits. Even if such incomplete disclosure does not violate legal standards, I submit that it comes precariously close to being unsporting conduct and to trenching on the high ethical standards to which professional men assert they aspire.

It would produce a misleading emphasis to end on this moralistic note. Instead I prefer to remind you of what ultimately lies at the base of the tax avoidance problem. Tax dodging arises in acute form only because our tax statute, in defining taxable income, makes distinctions which depart from a comprehensive measurement of a taxpayer's actual economic enhancement. Thus our tax law distinguishes between a dollar of ordinary income and a dollar of capital gain, a dollar of realized income and a dollar of unrealized income, and so forth. All of us feel and usually act on the feeling that, in maximizing our income or our economic enhancement, a dollar is a dollar. When the tax law distinguishes between dollars, it must do so in terms which are unrelated to the real economic position of the taxpayer and which, in this sense, are arbitrary. The essence of the tax avoidance problem is found here: where the basic distinction drawn by the law is itself arbitrary, no satisfactory general principle is available for deciding when taxpayers should be defeated in their attempts to move themselves across to the favorable side of that arbitrary line.
Some Members of the Board of
the University of Chicago Law School Alumni Association

Left to right, standing, William G. Burns, JD'31, Paul R. Kitch, JD'35, Hubert L. Will, JD'37; seated, Richard F. Babcock, JD'46, Abner J. Mikva, JD'51, Richard James Stevens, JD'38.
Standing, left to right, Stuart B. Bradley, JD'30, Keith I. Parsons, JD'37, P. Newton Todhunter, JD'37; seated, Hon. Willis W. Ritter, JD'24, Hon. Walter L. Pope, JD'12, Louis H. Silver, JD'28.

Morris E. Felzwell, JD'15, Senior Vice President, American National Bank, Chicago, President of the University of Chicago Law School Alumni Association.
Among Law School Alumni in Texas

E. Karl McGinnis, JD'23, Professor Emeritus, Business Law, The University of Texas, Austin, Texas. Mr. McGinnis has served as a member of the Austin City Plan Commission and is currently Vice President and a director of the First Federal Savings and Loan Association of Austin.

Edward C. Fritz, '40, of Fritz and Vinson, Dallas. Mr. Fritz has been practicing law in Dallas since 1940, with special interest in problems of damage inflicted by harassment, and in usury law. He is active in, and a director of, several Dallas civic organizations.

J. Newton Rayzor, JD'21, of Houston, a senior member of the firm of Royston, Rayzor and Cook. Mr. Rayzor, and his firm, are specialists in admiralty and maritime work, with offices in both Houston and Galveston. He is a Trustee of Baylor University and a Life Trustee of Rice Institute.
John H. Freeman, '12, of Fulbright, Crooker, Freeman, Bates and Jaworski, Houston. Mr. Freeman is a director of, and general counsel of, Anderson, Clayton and Company, a director of the First City National Bank, of Houston, President of the M. D. Anderson Foundation and active in numerous other charitable and professional groups. He has received the honorary degree of Doctor of Laws from Baylor University.

E. Ernest Goldstein, '43, Professor of Law at the University of Texas. Mr. Goldstein has served as General Counsel to the Subcommittee on Study of Monopoly Power of the House Judiciary Committee. He is the author of a casebook on Patent, Trade-Mark and Copyright Law. In addition to that field, he also teaches international law and anti-trust. He has been chairman of the International Law Committee of the Association of American Law Schools.

Dudley K. Woodward, Jr., JD'07, of Dallas. Mr. Woodward was in private practice in Austin and later in Dallas, until 1944, at which time he began to devote all of his time to his work as Chairman of the Board of Regents of the University of Texas. Shortly after the conclusion of his service on that Board in 1955, Mr. Woodward became Chairman of the Executive Committee of the Committee of Seventy-Five, a group set up by the Regents to study the past development of the University of Texas and to chart its future progress.
Toomin—
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States of trusteeship over the islands. Under Chapter 11 of the Charter of the United Nations, provision is made for the assumption by members of the administration of territories, whose people have not yet attained full self government. Under such provisions, members agree to accept as a sacred trust, the obligation of promoting the well being of the inhabitants of such territories.

In pursuance of the national policy of maintaining these islands within our sphere of influence, Congress, on July 18, 1947, authorized assumption of the trusteeship. By the trusteeship agreement, termination of Japanese control was recognized, and the United States named as the administering authority. Under it, the United States assumed the obligation of promoting the economic advancement and self sufficiency of the inhabitants; of protecting their civil rights and fundamental freedoms, without discrimination; of fostering and developing a general system of elementary education, and the pursuit of higher and professional education as well. It also agreed to promote the self government of the people in accordance with their expressed wishes, and to give them an increasing share in the administrative services in the territory. And lastly, it agreed to provide a system of law which would give due recognition to the well recognized native customs of the inhabitants.

Upon approval of the Trust Agreement by the Security Council, the President directed the Navy Department to provide, on an interim basis, appropriate administration to implement this country's obligations under the Trusteeship Agreement. It was no longer possible to operate the machinery of government through military directives backed by Navy guns. It was now necessary to set up a government operating under civil rules of administration, with the branches of government and their powers adequately delineated, a system of laws established, and a judicial branch established in order to interpret and enforce those laws.

The administrative head of the new government named by the President, was the Commander-in-Chief of the United States Pacific Fleet, who was given the title of High Commissioner. To his subordinates was assigned the task of preparing the necessary draft of a bill of rights and constitution, as well as a new legal system, tailored to the needs of this far-flung aggregation of communities.

The sea-going lawyers proved to be as adept at initiating a formal civilian government as they had been in administering its military predecessor. In short order they hammered out a series of directives which
were adopted by the High Commissioner as the basic framework of the new system of laws. They took the shape of a bill of rights and a series of regulations covering the division of powers and duties of government and its sub-divisions, as well as a code of crimes and criminal procedure, and provisions for judicial procedures and law enforcement.

When their task was completed, they had prepared a series of interim regulations of some eighteen chapters, of which Chapter I was the Bill of Rights, setting up the framework of a system of government (its constitution), together with the statutes designed to carry into effect this constitutional system. A later chapter was added with respect to communications, so that the entire scheme of government, as well as the statutes designed to implement the powers delegated, was finally compressed into 19 chapters, divided into some 1,204 sections, and running slightly over 139 pages of text.

Before one becomes lost in admiration at this apparent example of concise draftsmanship, yet it be noted that there are a number of ready answers. First, we are dealing with a society which, though not primitive, is far below the complexity of western civilization, and up to this time has required only relatively limited application of the principles and practices incidental to modern business, finance, and government.

Second, it is possible to adopt other legal systems by a few apt words, thus dispensing with the requisite detail where each provision is to be set forth with particularity. As will be seen, such is the case here.

And, third, where not restricted by constitutional limitations, as here, broad powers may be delegated to administrators, and considerable discretion allowed in the exercise of these powers. Although this pattern is not to be described as markedly democratic, it is nevertheless completely workable.

These interim regulations adopted by the Navy, and as amended from time to time, continued as the sole body of law applicable in the Trust Territory from July 18, 1947, until December 22, 1952, approximately a year after administration of the Territory had passed from Navy, and become vested in the Department of the Interior. That Department appointed a civilian as High Commissioner, who, in 1952, by proclamation adopted these interim regulations as the official Trust Territory Code of Laws.

In a foreword to the printed code which accompanied the proclamation, the then High Commissioner, former Senator Elbert D. Thomas, had this to say:

"On this wisdom of our two American judges to appreciate law as a growing organism, and on the ability of our more than 100 Micronesian judges to overcome the forces of the past and rule in accordance with law, will depend the ultimate success of attaining our objectives."

It may be of interest to take a quick look at this code to see why its successful administration depends so largely on the wisdom of the two American judges. As above stated, Chapter 1 consists of a Bill of Rights. There are 14 sections, 10 of which are adapted without significant change from the first 10 amendments to the Federal Constitution. Of the 4 additional, one guarantees freedom of migration and movement within the Trust Territory; a second assures free elementary education throughout the Territory; a third permits the High Commissioner to restrict ownership of real property and business enterprises to citizens of the Trust Territory; and the last requires due recognition of local custom in providing a system of laws.

Chapter 2 undertakes to designate the laws and legal systems applicable in the Trust Territory. It repealed all the Spanish, German, and Japanese laws theretofore adopted, and provided that the following were to have the effect of law: (a) The Trusteeship Agreement; (b) such laws of the United States as shall by their own force be in effect in the Trust Territory; (c) The Trust Territory Code; (d) District Orders promulgated by the District Administrators of Trust Territory, with the approval of the High Commissioner; and (e) duly enacted Municipal Ordinances.

Recognition of local custom was assured in a section providing that customary laws not in conflict with the laws of the Trust Territory, or those laws of the United States in effect therein, were to have the force of law in matters to which they were held by the courts to be applicable.

The further proviso was made that the common law of England, as it existed on July 3, 1776, and as interpreted by American decisions, was to be in effect in the Territory, except where local land law was in conflict therewith. An express provision also appears that the laws governing ownership, use, inheritance, and transfer of land, in effect in the Territory December 1, 1941, were to remain in full force and effect, except where changed by written enactment under the authority of the Trust Territory Government.

Due recognition was given to the desirability of amending the Code from time to time, by a provision that such could be done through Executive Order promulgated by the High Commissioner. Thus, it can be seen that the legislative power is lodged primarily in the High Commissioner, secondarily in the District Administrators, and finally in the municipalities created under the authority of the Code. It can also be seen that there has been created a hybrid legal system in which there has been engrafted on the common
This review provision of the Code was inserted in order to expose the trial practice of the lower courts to the scrutiny of the High Court for the purpose of assuring that substantial justice was done. Though the Code authorizes the reviewing Justice to reverse and remand any judgment believed by him to have been entered erroneously, even though no appeal has been taken therefrom, in practice the review procedure is utilized by the reviewing Justice to point out palpable error and suggest appropriate change.

In addition to this review procedure which though onerous, serves a highly useful purpose, further appellate jurisdiction inheres in the Appellate Division of the High Court, to review on appeal, all decisions in cases tried by the Trial Division and in certain cases heard by that division on appeal or review of decisions of the lower courts.

District Court judges are named by the High Commissioner, usually upon recommendation of the Chief Justice of the High Court, but are removable by the High Court for cause and after hearing. The number of judges assigned is based on the amount of judicial business in the particular district. District Courts have original jurisdiction over civil causes involving claims of property not exceeding $1,000.00 in value, excepting admiralty and maritime matters, and adjudication of title to real estate; and jurisdiction over criminal cases where the maximum punishment does not exceed a fine of $1,000.00, or imprisonment for one year, or both. Each District Court has appellate jurisdiction over all decisions of the Community Courts, civil and criminal.

Community Court judges are appointable by the respective District Administrators, and removable by the High Court for cause and after hearing. Jurisdiction is limited to civil cases where the values involved do not exceed $100.00, except admiralty and maritime matters, and adjudication of title to land, and criminal cases where the maximum punishment does not exceed a fine of $100.00, or imprisonment for 6 months, or both.

Further provisions appear whereby the High Court may require any case pending in the inferior courts to be transferred to it for further proceedings; also delegating to the Chief Justice administrative supervision over all the courts of the Trust Territory and their officers, with the power to make rules regulating pleading, practice, and procedure in the various courts, and the conduct of business therein. The Chief Justice is also empowered to appoint and remove the Clerks of Courts for the various districts, as well as all other court employees, provided that native inhabitants are to be employed as judges, clerks, and employees to the maximum extent consistent with good administration.

Provisions appear with respect to judicial procedures...
in the enforcement of extra ordinary remedies, such as attachment, execution, and levy on property, habeas corpus, and the commitment of insane persons; also with respect to criminal procedures in the matter of process, search and seizure, bail, and the protection of fundamental rights of the accused. These are similar to procedures set up by the statutes of the several states. They are supplemented by a series of rules of civil and criminal procedure promulgated by the Chief Justice, adopting certain portions of the Federal Rules of Civil and Criminal Procedure.

Accordingly, it can be seen that insofar as is apparent from the provisions of the Trust Territory Code, and of the Rules of Civil and Criminal Procedure, the courts of the Territory have to same basic legal background, are called upon to enforce, in general, the same civil rights, and use, on the whole, pretty much the same techniques and procedures as are employed in similar situations within the United States. There are, however, several basic differences, which result in imposition on the judges of the High Court, of responsibilities, duties, and discretion more demanding than those required of conventional Federal judges.

In the first place, territorial trials are not held before juries. The standard of general education in Micronesia, though constantly improving, is still far below the level needed to assure adequate deliberation by the ordinary resident on issues of fact. Local influences are particularly strong where the clan and lineage system operates, and the impact of foreign cultures too recent to permit of even a moderate use of this trial method. Accordingly, a judge has the burden initially of acting as his own jury, and after determining the facts, of applying to them the relevant legal principles.

Second, in nearly all civil cases the parties are without the aid of a professional bar in the drafting of pleadings, motions, and other documents, and during the trial. Customarily they appear with some trusted advisor, who undertakes to present the testimony and such argument as his understanding of the issues will permit. This imposes on the High Court the necessity of questioning each witness for both sides rather extensively in order to be sure that the record contains all the essential facts. The court has great latitude—and exercises it—in adjourning trials until some essential testimony may be forthcoming which the parties have neglected, or for the purpose of examining the site where land or other disputes are involved. But the most important weapon in the judicial arsenal is the pre-trial conference, and its usually resultant order. This conference is set by the court early in its sitting, and the parties and their advisors are invited to present their respective theories of the case. The court then strives to obtain the necessary background of the case and agreement on matters not in controversy. In an order there is then stated the contentions of the parties, the agreements reached between them, and the issues remaining to be resolved by evidence at the trial.

In this manner the court is able to eliminate all but the essential evidence and to center the parties' attention on the real matter at issue. A vast amount of court time and effort is thus saved, and the handling of judicial business expedited. However, the burden thus imposed on the court is substantial, as the drafting of the pre-trial order is frequently onerous; and convincing the parties that the order adequately protects their interest, involves a considerable amount of salesmanship, particularly in the light of the language barrier. It may then be stated that the lack of a trained professional bar adds enormously to the duties and responsibilities of judges of the High Court, and in this respect their lot is far less happy than that of their brethren with the heavier robes.
It is an axiom of human conduct that everyone espouses a just solution to controversy, provided it is in his favor. Since the court ex hypothesi desires in each case to achieve substantial justice, and since the parties are mainly interested in achieving their own ends, the parties have developed the practice of using what are known as Trial Assistants. These assistants are usually present or former Assistant Public Defenders, who have become somewhat familiar with the court rules and procedure, and have acquired some understanding of basic legal principles. By court rule, these trial assistants have been given status before the courts and have become amenable to court disciplinary action. It is hoped the use of trial assistants will increase until the advent of a trained professional bar, of which there is as yet but the faintest glimmer on the horizon. How comforting it will be to High Court judges of the post atomic age to doze gently in their courtrooms while pretending to listen to the learned argument of counsel. And how pleasant to be able to examine with practiced eye the orders prepared by counsel, noting merely whether they contain the essential facts and judicial prerequisites.

This leads to the third point of difference between practice in the Trust Territory and in stateside courts. It follows from what has been said hereinabove that in all civil cases, all orders, and much of the record of the proceedings, are prepared by or under the supervision of the trial judge. In addition to the pretrial order, there is the final judgment order containing findings of fact and conclusions of law. If there is an appeal, the record of proceedings is typed by the court reporter and submitted for examination to the trial judge, who makes any necessary revisions, then certifies it, and sends it on to the appellate tribunal with the exhibits and the common law record. All that the party, or his trial assistant, customarily does is to present a brief and argument, although this is not essential to a consideration of the appeal by the appellate court.

What has been said above does not apply in its entirety to criminal trials. Here we have a territory-wide District Attorney, who presents all felony cases to the High Court in the districts of their origin. These cases are defended by a Public Defender, he and the District Attorney being professional lawyers recruited from the American bar. They have assistants in each district, who are qualified to present and defend misdemeanors before the District Court judges, and to prepare the necessary complaints in all cases in the absence of the District Attorney.

However, all orders in criminal cases, the report of proceedings, and the record on appeal, are prepared under the direction of the trial judge. He does not take such a dominant part in the conduct of criminal trials, as there is adequate representation of both parties to assure presentation of essential evidence. However, he frequently examines witnesses and takes upon himself the responsibility of determining that the fundamental constitutional rights of the accused have not been violated, particularly where the introduction of a confession is sought by the prosecution. Great pains are taken by the trial judge in pronouncing sentence to make sure the defendant understands the purpose of the punishment, as well as the factors considered by the court in determining sentence. It is a cardinal principle of the High Court that it is not only essential to do substantial justice in each case, but that the people generally, if not both litigants, recognize as such.

The final distinctive difference in practice between Stateside courts and those of the Trust Territory, is in the impact of customary law in the Territory. First in the Trusteeship Agreement, then in the Bill of Rights, and finally in the Code, it was recognized that the customary law in existence in various parts of the Trust Territory, in matters to which it was applicable as determined by the courts was to have the full force and effect of law, to the extent not in conflict with the written basic law formalized in the Code. Though the common law was made generally effective in the Trust Territory, it was provided by exception thereto, that it would yield to recognized local

Gloria P. Martinez, of El Paso, Texas, A.B., Texas Western College, Editor-in-Chief, The Student Lawyer.
custom. In addition, an express provision was inserted in the Code concerning land law as hereinabove described.

The impact of customary law upon the otherwise common law of Trust Territory can be measured when it is realized that in practically all of the districts, in addition to the customs in force governing ownership, use, inheritance, and transfer of land, there are well recognized customs having the sanction of law, in marriage, divorce, adoption, and wills.

When to the foregoing is added the further qualification that the customs differ not only from district to district, but occasionally from municipality to municipality of the same district, it becomes obvious what a headache this matter of customary law may present to the casual jurist. So important is the impact of custom on litigation generally, that by Code provision and rule of court, the courts are permitted to avail themselves of a local expert called an “assessor,” who is usually a District Court judge, and who sits alongside the trial judge and is permitted to ask questions of the witnesses to the same extent as counsel and the trial judge. While the parties are invited to present their own evidence as to custom, it may be assumed that the advice of the court’s expert shares importantly in the court’s decision.

These are the principal differences in practice between Stateside courts and those of the Trust Territory. However, let it not be assumed for a moment that they tell the whole story. There is more to the transaction of judicial business in the Trust Territory than conducting a pre-trial conference, or presiding at trials. It is quite different here from the occasional peril of travelling by taxi from a federal judge’s comfortable apartment on the near-north side, to his well-equipped chambers and imposing courtroom in the United States courthouse.

Our High Court justices travel from district to district as often as judicial business requires, in amphibious planes carrying not over 15 passengers, and up to several thousand pounds of freight. Water landings are made in three of the districts, and on land in the other three. In two of the districts where the plane comes to rest on the surface of the lagoon, it taxies to a sea ramp up which it waddles and then comes to rest for discharge of passengers and freight and refueling. The passengers then leave for their hotel, either by launch through the tricky three mile channel at Ponape, or by jeep several miles across the causeway to Koror Island in the Palau group. In the third district which requires water landings, Yap, there is no sea ramp, so that the plane must tie up to a buoy in the harbor and discharge passengers and freight onto a waiting barge, which transports them a half-mile or so to the pier. In all of the districts where water landings are employed, it is necessary for a launch to sweep the ‘runway’ to be utilized by the oncoming plane, of any debris which might become a peril to its fast approach or departure. It is a thrill, which is never dulled by constant repetition, to take off in these comparatively small planes, fly from 500 to 800 miles of ocean, and unerringly find one’s way into the relatively calm waters of the target lagoon.

Where these planes land on an airstrip, their ex-bomber pilots usually waste no time in preliminaries, such as circling the air field or banking to reduce speed. One of them comes in exactly as he used to do on the deck of a carrier, with a sudden descent and no apparent slackening of speed. Nor is the take-off at daybreak on a rough coral runway entirely conducive to pleasant digestion and peaceful slumber.

Added to these perils is another from which stateside judges are relatively free, namely the malevolent use of magic. In criminal cases, High Court judges are unfortunately subject to an occasional “hex” which is used to ward off an adverse decision. In a recent trial at Yap, the accused employed a “sure” method of inserting such confusion and uncertainty into the judicial mind as to preclude an unfavorable decision. This he did by tearing leaves into small bits and scattering them along the road from the judge’s quarters to the
courthouse. Unfortunately for the accused, this jurist had been in such a chronic state of confusion induced by a study of some involved native customs, that the "hex" had relatively little effect. Accordingly this magician now sits in a cool cell wondering what could have gone wrong, as he serves the sentence imposed on him by the confused jurist.

When he travels to the various districts, the High Court Justice is usually met by a delegation consisting of District Judges, the Clerk of Courts, and local prosecutors and public defenders, from whom he will get the latest news concerning readiness of cases on the trial call. Later in the day he will visit the courthouse and groan over the inadequate facilities, for it is a deplorable fact that construction or renovation of courthouses is on the public works agenda far behind the necessary expansion of hospital facilities and construction of schools. This is why it is such a pleasure to sit in the new courthouse at Koror, where the almost completed building is so attractive as to have earned the sobriquet, "Taj Mahal."

However, conditions are constantly improving, and as funds are made available by Congress, serious deficiencies are being alleviated. In its operation of the Trust Territory the United States has amply demonstrated that it has taken to heart the objectives of the Trusteeship Agreement. Signs abound that the native populations are showing a marked advance in health, education and civilization, and a steady improvement in economic well-being. In all this the United States can take a justified pride, as can the many dedicated staff members who man the necessary facilities.

Americans coming to Micronesia and rendering significant service in the fields of medicine, law, education, and public health, are deservedly held in high esteem by the native populations. Those having the appropriate professional background and the stimulus towards the experience of living among and working with the eager natives, will find their lives in Trust Territory rich in reward. They will be disappointed, however, if they expect this reward to come in the shape of a beautiful hand maiden sent by her tribe to grace the home of the altruistic worker. The writer is constrained to sadly admit, that though he has toiled for some time on the outlying islands in a position of responsibility and power, no such experience has as yet befallen him.