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FEDERAL PRACTICE AND PROCEDURE

I. FEDERAL ABSTENTION IN LAND USE CASES

A. INTRODUCTION

In two recent cases,[1] the Ninth Circuit Court of Appeals held that district courts had acted within their discretion in abstaining from the exercise of federal question jurisdiction in two inverse condemnation suits. In each case a California city had declared a moratorium on development in an area that included plantiff's property, and plaintiff complained that the property was "taken" in violation of the fifth and fourteenth amendments of the United States Constitution. In *Sederquist v. City of Tiburon,*[2] plaintiffs alleged that the city had included a road over which they claimed an easement in the open space element of the city's general plan and had imposed unreasonable conditions upon the right to pave that road. In *Sante Fe Land Development Company v. City of Chula Vista*[3] plaintiff alleged that the city had down zoned an area containing plaintiff's industrial property to include commercial, residential, and open space elements. Both complaints alleged that the cities had converted private property into public lands without paying just compensation.[4] In each case the district court abstained from exercising jurisdiction. However, in *Sederquist* the federal action was stayed while in *Sante Fe* the action was dismissed. Relying heavily on the three-pronged abstention test announced in *Canton v. Spokane School District* #81[5] the Court of Appeals concluded that the courts had not

1. Sante Fe Land Improvement Co. v. City of Chula Vista, 596 F.2d 838 (9th Cir. Mar., 1979) (per Wallace, J.; the other panel members were Curtis, D.J. and Goodwin, J.); and Sederquist v. City of Tiburon, 590 F.2d 278 (9th Cir. Sept., 1978) (per Wallace, J.; the other panel members were Smith, D.J. and Hug, J.).

2. *Id.*

3. 596 F.2d 838.

4. While the Sederquists predicated their complaint solely on the federal Constitution, the Sante Fe Land Improvement Co. based its complaint on both federal and state constitutional proscriptions against uncompensated"takings."

5. 498 F.2d 840 (9th Cir. 1974). In *Canton,* the Ninth Circuit applied and catalogued the abstention requirements announced in Railroad Comm'n v. Pullman Co., 312 U.S. 496 (1941). *See* note 12 *supra. Pullman* abstention should be ordered only where:

> (1) The complaint "touches a sensitive area of social policy upon which the federal government ought not to enter unless no alternative to its adjudication is open."
> (2) "Such constitutional adjudication plainly can be avoided if a definitive ruling on the state issue would terminate the controversy."

abused their discretion by refusing to exercise jurisdiction. The court held that the lower court erred in dismissing the action in *Santa Fe* and that the action should have been stayed.

B. Background: The Abstention Doctrines

If a case is properly within a federal court's jurisdiction, that court generally has an affirmative duty to exercise its jurisdiction without discretion to decline.[6] Normally, the court may not refuse to hear a case arbitrarily,[7] merely because another forum is available to plaintiff,[8] or because a case involves state issues that are difficult[9] or for which there is no precedent.[10]

However, there are certain contravening interests and principles that form the bases for narrow exceptions to a court's duty to decide a case properly before it.[11] The most firmly established exception is generally referred to as the "*Pullman* doctrine."[12] In

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(3) The possibly determinative issue of state law is doubtful.

Sederquist v. City of Tiburon, 590 F.2d at 281, *citing* Canton v. Spokane School Dist. #81, 498 F.2d at 845; Santa Fe Land Improvement Co. v. City of Chula Vista, 596 F.2d at 839-40.

6. Cohens v. Virginia, 19 U.S. 264, 403 (1821).

7. United States v. Hofsteen Tse-Kesi, 191 F.2d 518, 520 (10th Cir. 1951).

8. Lake Carriers' Ass'n v. MacMullan, 406 U.S. 498, 510 (1972).

9. Williams v. Green Bay and W. R. Co., 326 U.S. 549, 556-57 (1946); Meredith v. City of Winter Haven, 320 U.S. 228, 234-35 (1943), *cert. denied*, 323 U.S. 738 (1943), *mandate conformed to* 141 F.2d 348 (1944), *rehearing denied*, 141 F.2d 1019 (1944). *But see* County of Allegheny v. Frank Mashuda Co., 360 U.S. 185, 187 (1959) and Louisiana Power & Light Co. v. City of Thibodaux, 360 U.S. 25, 27-28 (1959). For a discussion of abstention in cases involving difficult state law issues, *see* note 22 *infra*.

10. *E.g.*, Martin v. State Farm Mut. Auto. Ins. Co., 375 F.2d 720, 722 (4th Cir. 1967).

11. Some of these considerations are: (1) that decisions of constitutional law should be avoided where a case can be disposed of on the basis of state law, Ashwander v. Tennessee Valley Authority, 297 U.S. 288 (1936); (2) that conflicts between the state and federal systems should be avoided wherever possible, Railroad Comm'n v. Pullman Co., 312 U.S. 496, 500 (1941); (3) that where a case involves state law that is unsettled or possibly violative of the federal Constitution, it should be reserved to the state courts wherever posssible, Harris County Comm'rs Court v. Moore, 420 U.S. 77, 87-88 (1975); American Trial Lawyers Ass'n v. New Jersey Supreme Court, 409 U.S. 467, 468 (1973); Spector Motor Serv. Inc. v. McLaughlin, 323 U.S. 101, 105 (1944); and (4) that congestion of the federal court dockets should be relieved where feasible, Railroad Comm'n v. Pullman Co., 312 U.S. 496, 501 (1941).

12. Named for the leading case on the subject, Railroad Comm'n v. Pullman Co., 312 U.S. 496 (1941), where plaintiffs sought to enjoin as invalid an order of a state railroad commission requiring Pullman conductors to supervise all sleeper cars on passenger trains. Before the order was issued, many sleeper cars were staffed only by porters (most of whom were black). Pullman porters joined with the railroad company as plaintiffs, complaining that the rule would deprive blacks of their jobs and was violative of the fourteenth amendment as well as state law. The Supreme Court ordered the district court to abstain from assuming jurisdiction pending a state court ruling because the state court could invalidate

this form of abstention, the district court postpones its exercise of jurisdiction when a federal constitutional issue may be rendered moot or substantially modified by a state court decision involving the same parties and controversy. When a court abstains under *Pullman,* it retains jurisdiction over any federal issues which may remain after the state ruling.[13] Another exception to the court's duty to hear a case over which it has jurisdiction is frequently referred to as "*Burford* abstention."[14] This type of abstention is appropriate when a suit involves issues that are of

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the order and thus render the constitutional issue moot. The Court based its decision largely on a "scrupulous regard for the rightful independence of the state governments." *Id.* at 501.

13. The litigant has the option of submitting all issues, state and federal, to the state court for a final adjudication, or of reserving the federal issues for final adjudication in the federal court after all state issues have been decided. England v. Louisiana State Bd. of Medical Examiners, 375 U.S. 411, 421 (1964).

14. Named after Burford v. Sun Oil Co., 319 U.S. 315 (1943), a case involving a state regulatory commission's grant of permission to drill oil wells in a certain Texas oil field. The Supreme Court ruled that a district court had properly dismissed the federal action where the state had established a complex regulatory scheme to deal with such cases. Because the issues were complex and of particular importance to the state, and because previous federal intervention had already resulted in significant friction between the state and federal governments, the Court held that the federal courts should allow the state to form its own policy in such matters of predominantly local importance. *Id.* at 331.

Burford abstention is based on comity, that is, a respect for the fact that the United States is comprised of separate state governments whose interests will best be served by allowing them to make their own policy decisions. *Burford* abstention is only justified when a case involves issues in which the state has a predominant interest. Santa Fe Land Improvement Co. v. City of Chula Vista, 596 F.2d at 842.

The Court greatly expanded *Burford* in Alabama Public Service Comm'n v. Southern Ry. Co., 341 U.S. 341 (1951). There, the Court ordered abstention in a case which did not qualify under *Pullman,* did not involve a complex state regulatory scheme, nor had a history of friction resulting from past federal intervention. Further, the record did not reflect that the state provided more complete judicial review than could be had in the federal courts, as was the case in *Burford.* The sole basis for the *Alabama* decision was that the state had a predominant interest in deciding the case because it involved distinctly local factual issues. One circuit court has taken *Alabama* to stand for the broad proposition that any time a state has an interest in the subject matter of a federal action, the federal court should abstain in order to prevent state-federal friction. Kelly Serv. Inc. v. Johnson, 542 F.2d 31, 33 (7th Cir. 1976). Such a broad reading of *Burford* has no support in the Supreme Court or Ninth Circuit opinions, and the authoritativeness of both *Kelly Services* and *Alabama* should be questioned in view of the rule that abstention should be ordered only in extraordinary circumstances.

In Colorado River Water Conservation Dist. v. United States, 424 U.S. 800, 813 (1976) the Court reiterated the exceptional nature of abstention in a case involving water rights, an issue of extreme importance to western states. Even though the state had established a complex judicial scheme for deciding questions relating to water rights, the Court declined to apply *Alabama* to find abstention proper in that case. It appears that the *Colorado River* Court properly narrowed the application of abstention to truly extraordinary circumstances, and reaffirmed the general rule that federal courts should exercise jurisdiction in cases properly before them under all but a few greatly limited circumstances.

predominantly state interest, and federal invervention would interfere with the state's efforts to deal with those complex issues. When a court abstains on the basis of *Burford*, the federal action is dismissed rather than stayed.

C. The Courts' Analyses

Pullman *Abstention*

In *Canton v. Spokane School District* #81,[15] the Ninth Circuit interpreted *Pullman* as requiring that three conditions be met before a court could properly abstain. Applying the *Canton* analysis, the *Sederquist* and *Sante Fe* panels ruled that the first requirement was met in that plaintiffs' complaints "touche[d] a sensitive area of social policy upon which the federal courts ought not to enter unless no alternative to its adjudication is open."[16] Relying on the 1976 case of *Ranchos Palos Verdes Corp. v. City of Laguna Beach*,[17] in which the court ruled that because California had recently enacted a complex web of statutes dealing with land use issues, the state had a contervailing interest in dealing with land use issues. For that reason the federal courts should not deny the state the opportunity to formulate its own policy. The *Sederquist* court expressed apprehension that federal intervention might impede the state's effort to deal with complex land use issues, adding that any conclusion a federal court might reach would only amount to a guess at what a state court might decide in the future.[18]

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15. 498 F.2d 840 (9th Cir. 1974). In *Canton*, a typical *Pullman* abstention case in which federal jurisdiction was predicated on a federal question, the Ninth Circuit applied and catalogued the abstention requirements announced in *Pullman*. For the Pullman abstention requirements *see* note 5 *supra*.

16. 590 F.2d at 281, *quoting* Canton v. Spokane School District #81, 498 F.2d at 845.

17. 547 F.2d 1092, 1094-95 (9th Cir. 1976).

18. 590 F.2d at 281-82. The question of whether eminent domain is a type of abstention unto itself has been raised by two highly similar cases which do not otherwise fall neatly within any defined abstention doctrine. While County of Allegheny v. Frank Mashuda Co., 360 U.S. 185 (1959) and Louisiana Power & Light Co. v. City of Thibodaux, 360 U.S. 25 (1959) do appear to be related to *Burford*-type abstention, neither case would qualify for abstention under a narrow reading of *Burford*.

Both *Allegheny* and *Thibodaux*, decided on the same day, involved issues of state eminent domain and were brought on diversity jurisdiction. The Supreme Court overruled the lower court's dismissal in *Allegheny* where the applicable state law was held to be clear. However, in *Thibodaux*, a stay was affirmed as the applicable state law was held to be unclear. The two heavily divided decisions are difficult to reconcile. The *Thibodaux* opinion emphasized the "special nature" of eminent domain which made it "intimately involved with sovereign prerogative." 360 U.S. at 28-29. However, in *Allegheny* the majority ruled that "[s]urely eminent domain is no more mystically involved with 'sovereign prerogative'" than a host of other concerns of state government which have been decided

The second prong of the *Canton* test was satisfied in both cases because federal constitutional issues could be avoided by applying state law[19] which prohibits zoning that amounts to an uncompensated taking of private property,[20] and which prohibits unreasonable conditions upon the right to improve private property.[21]

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by the federal courts. 360 U.S. at 192. While the two cases taken together do show that abstention may be appropriate in eminent domain cases, it is impossible to formulate any firm rule based solely on these two cases. It may be that abstention is proper where a case involves eminent domain issues coupled with unsettled state law, although if a case involves only one of these factors a federal court should not relinquish jurisdiction.

In Colorado River Water Conservation Dist., 424 U.S. 800 (1976), *Thibodaux* was interpreted as standing for the proposition that abstention is appropriate in cases where unsettled state law is presented, the importance of which outweighs the result of the case then at bar. *Id.* at 814. While both *Thibodaux* and *Pullman* require unsettled state law, the latter type of abstention is based on the policy of avoiding constitutional issues. It remains undecided if eminent domain is the only issue whose importance so overshadows the result in a given case that it merits a separate category of abstention.

19. The court ruled that the fact that the Sederquists had worded their complaint so as to raise only federal issues was not a bar to their holding. 590 F.2d at 282. The plaintiffs in Ranchos Palos Verdes Corp. v. City of Laguna Beach, 547 F.2d 1092, 1095 (1976), also drafted their complaint so as to raise only federal issues. In that case, too, the court ruled that such a ploy could not prevent a finding that constitutional issues might be avoided by applying state law.

This issue was not pertinent in *Sante Fe* because plaintiffs raised both federal and state issues in their complaint.

20. CAL. GOV'T CODE § 65912 (West Supp. 1978) (codifed CAL. CONST. art. 1, § 14, which provides that "[p]rivate property shall not be taken or damaged for public use without just compensation having first been made to . . . the owner . . . ."

The *Sederquist* panel relied on Newport Investments, Inc. v. City of Laguna Beach, 564 F.2d 893, 894 (9th Cir. 1977), in deciding that because the California constitutional proscription against uncompensated "takings" was the "mirror image" of that provision in U.S. CONST. amend. V, the state court should be afforded the first opportunity to interpret the state Constitution as a matter of policy. In *Sante Fe*, however, the court cited Stephens v. Tielsch, 502 F.2d 1360, 1362 (9th Cir. 1974) which held that abstention is not justified when state and federal constitutional provisions are such "mirror images." While the *Sante Fe* court declined to overrule *Newport Investments*, it does appear that *Stephens* is the better rule. The Supreme Court recently held that abstention is not justified by such "mirror image" provisions. Examining Bd. of Eng'rs, Architects & Surveyors v. Flores de Otero, 426 U.S. 572, 598 (1976); Harris County Comm'rs Court v. Moore, 420 U.S. 77, 84 n. 8 (1975). *But see* Askew v. Hargrave, 401 U.S. 476, 478 (1971) (distinguished in Stephens v. Tielsch, 502 F.2d at 1361-62). Other circuits have followed the *Stephens* rule. Pollard v. Cockrell, 578 F.2d 1002, 1010 (5th Cir. 1978); Connecticut State Fed'n of Teachers v. Bd. of Educ. Members, 538 F.2d 471, 485 (2d Cir. 1976) (dictum). The question of whether *Newport Investments* or *Stephens* is the correct rule in the Ninth Circuit would not affect the outcome of either of the principle cases because a state court could rule on the basis of the statutory provisions, obviating the need for a ruling on the constitutional issues.

21. The *Sederquist* court held that plaintiffs' allegation that unreasonable conditions had been attached to the granting of a permit to pave their access road could be settled under CAL. CIV. PROC. CODE § 1094.5 (Deering Supp. 1979) which permits an individual to appeal a decision of an administrative agency directly to a state court. *See* Mobil Oil Corp. v. Superior Court, 59 Cal. App. 3d 293, 130 Cal. Rptr. 814 (1976).

Finally, the Ninth Circuit held that the third prong of the *Canton* test was satisfied because the applicable state law was "manifestly unclear."[22] In the 1975 case of *HFH, Ltd. v. Superior Court,*[23] the California Supreme Court specifically reserved judgment on the question of entitlement to compensation where a zoning regulation forbade substantially all use of private lands. The *Sederquist* court also ruled that whether a city had abused its discretion by refusing to issue plaintiffs a permit to pave their access road necessarily depended upon state and local law. Therefore, the court held that it ought not attempt to anticipate a state court ruling on this issue.

In holding that the principle cases met the criteria announced in *Canton,* the court found that sufficient counterbalancing interests were present to justify an exception to a court's duty to decide a case over which it has jurisdiction. However, abstention is not justified merely because a case meets the *Canton* criteria. If equitable considerations exist which justify an

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22. Sederquist v. City of Tiburon, 590 F.2d at 282; Santa Fe Land Improvement Co. v. City of Chula Vista, 596 F.2d at 841. The degree of unclarity required has not been firmly established. The most common formulation is that the requirement has been met if the state law is "susceptible" to an interpretation that would avoid or substantially modify the constitutional challenge. Harman v. Forssenius, 380 U.S. 528, 534-35 (1965). Another standard is whether state law "may fairly be read" so as to avoid the constitutional issue. Boehning v. Indiana State Employees Ass'n Inc., 423 U.S. 6, 7-8 (1976). One commentator has suggested that no real standard exists and that the decision whether state law is sufficiently unclear depends upon the "court's view of the substantive issues that the case presents." Field, *The Abstention Doctrine Today,* 125 U. PA. L. REV. 590, 602-03 (1977).

At this time, it is unresolved whether abstention is proper in private litigation merely for the purpose of avoiding difficult state law where there is no constitutional or predominant state issue to be avoided. In Meredith v. City of Winter Haven, 320 U.S. 228, 236 (1943), the Court ruled that mere difficulty of applicable state law does not justify abstention. The later cases of *Thibodaux* and *Allegheny,* cast some doubt on the authoritativeness of *Meredith. See* note 18 *supra.* However, in McNeese v. Board of Educ. for Community School Dist. 187, 337 U.S. 668, 673 n. 5 (1963), the Court again ruled that mere difficulty of state law was not a sufficient ground for abstention. Lower federal courts have been inconsistent in their application of these cases. For a time, the Fifth Circuit ruled abstention proper simply because the state law was unclear. *See* United Services Life Ins. Co. v. Delaney, 328 F.2d 483, 484-85 (5th Cir. 1964), *cert. denied,* 377 U.S. 935. However, it appears that that holding was predicated largely on the distaste for diversity jurisdiction. *See* Bendar, *Abstention Under* Delaney: *A Current Appraisal,* 49 TEX. L. REV. 247 (1971). Recent cases indicate that *Delaney* is of questionable reliability. Imperial Enterprises, Inc. v. Fireman's Fund Ins. Co., 535 F.2d 287, 290 (5th Cir. 1976). The Ninth Circuit rejected the *Delaney* ruling in Tomiyasu v. Golden, 358 F.2d 651, 654 (9th Cir. 1966). No later case has appeared which alters this rule.

23. 15 Cal. 3d 508, 518 n. 16, 125 Cal. Rptr. 365, 372 n.16, 542 P.2d 237, 244 n. 16 (1975).

immediate adjudication by the federal court, abstention will not be ordered.[24] Abstention will necessarily result in a delay in reaching a judgment on the merits. However, the delay involved in *Sante Fe* and *Sederquist* would be minimal because both plaintiffs had already commenced an action in the state court before the running of the statute of limitations.[25] While the *Sederquist* court specifically ruled that the burden placed on the plaintiffs was small and was outweighed by the interests served by ordering abstention, the *Sante Fe* court did not consider whether additional equitable considerations justified an immediate adjudication by the federal court.

Burford *Abstention*

Having decided that *Pullman* abstention was justified, the

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24. The court will not abstain when doing so would result in undue hardship to the parties. In Griffin v. County School Bd. of Prince Edward County, 377 U.S. 218, 229 (1964), the Court refused to abstain where doing so would have increased the length of time required to implement integration of a school system. In Pike v. Bruce Church, Inc., 397 U.S. 137, 145 (1970) the Court declined to order abstention when the ensuing delay would have resulted in the economic loss plaintiffs sought to avoid by bringing suit originally.

25. There is some support for a fourth type of abstention which is ordered only for the convenience of the court and to avoid duplicative proceedings. In McClellan v. Carland, 217 U.S. 268, 282 (1910), the Supreme Court ruled that the mere pendency of an action in state court does not justify federal abstention. The lower federal courts have shown dissatisfaction with the *McClellan* requirement that both state and federal actions proceed until one of them results in a final judgment that would be res judicata as to the other. Most of the circuit courts have held that a district court may abstain when a similar action is pending in a state court. Weiner v. Shearson, Hammill & Co., Inc., 521 F.2d 817, 820 (9th Cir. 1975); PPG Industries, Inc. v. Continental Oil Co., 478 F.2d 674, 681 (5th Cir. 1973); Mottolese v. Kaufman, 176 F.2d 301, 303 (2d Cir. 1949).

In Colorado River Water Conservation Dist. v. United States, 424 U.S. 800, 809 (1976), the Supreme Court upheld a lower court abstention order where a similar suit was pending in state court. However, the Court based its order on a federal statute which the Court interpreted as giving support to the proposition that states have a countervailing interest in deciding matters pertaining to water rights. Thus, in *Colorado River*, the Court ruled that "the circumstances permitting dismissal (for purposes of judicial economy) are substantially more limited than circumstances appropriate for abstention." *Id.* at 818.

While the Supreme Court has not ruled abstention appropriate solely for the purpose of advancing judicial economy, there is considerable support among the commentators. *See*, Kurland, *Toward a Co-Operative Federalism: The Federal Court Abstention Doctrine*, 24 F.R.D. 481, 490-92 (1960); Note, *Stays of Federal Proceedings in Deference to Concurrently Pending State Court Suits*, 60 COLUM. L. REV. 684 (1960); Note, *Power to Decline the Exercise of Federal Jurisdiction*, 37 MINN. L. REV. 46 (1952); Note, *Power to Stay Federal Proceedings Pending Termination of Concurrent State Litigation*, 59 YALE L.J. 978 (1950). For a more detailed discussion of the various forms of abstention, *see* 1A, Pt. 2 MOORE'S FEDERAL PRACTICE, ¶ 0.203(2)-(4); C. WRIGHT, A. MILLER & E. COOPER, FEDERAL PRACTICE AND PROCEDURE: JURISDICTION §§ 4241-46; C. WRIGHT, HANDBOOK OF THE LAW OF FEDERAL COURTS, § 52 (3d ed. 1976).

Sante Fe court also ruled that *Burford* dismissal was inappropriate on several grounds. In *Ranchos Palos Verdes Corp. v. City of Laguna Beach,*[26] the court noted that California has not attempted to relegate land use cases to any one court or set of courts.[27] Further, even if California had established a special court to hear such cases, the facts of *Sante Fe* did not indicate that federal intervention would interfere with the state's efforts to establish its own policy in a matter of predominant state interest. Finally, and perhaps most importantly, the *Sante Fe* court held that the issues involved were not sufficiently complex or unique so as to warrant *Burford* dismissal.[28] Therefore, the *Sante Fe* panel ruled that the district court had abused its discretion in dismissing the case.

D. Conclusion

In *Sederquist* and *Sante Fe,* the *Canton* interpretation of the *Pullman* doctrine was applied in a typical and straightforward manner. As it was in 1976 when *Ranchos Palos Verdes* was decided, land use planning remains a sensitive area of intense state interest.[29] For this reason, California continues to have a predominant interest in establishing its own policies in this area. All matters raised by plaintiffs in both cases could be decided under state law. Finally, at the present time the California Supreme Court has still not ruled on entitlement to compensation where a zoning law disallows all use of plaintiff's property, and any decision a federal court might make concerning plaintiffs' complaints would amount to a mere forecast of what a state court might rule in the future. In fact, the degree of unclarity of state law in these cases surpasses any standard that has been applied by the federal courts.

Simply meeting the *Canton* requirements does not, of itself, justify abstention.[30] Ordering abstention will always result in a delay in reaching a decision on the merits, and it is the court's duty to carefully balance the costs of, against the interests served by, abstaining. While it is true that plaintiffs will have to turn to state courts for a final judgment, they are assured of a forum

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26. 547 F.2d 1092 (9th Cir. 1976).

27. *Id.* at 1096.

28. 596 F.2d at 843.

29. Isthmus Landowners Ass'n v. State of Cal., 601 F.2d 1087, 1090 (9th Cir. 1979).

30. Gibson v. Berryhill, 411 U.S. 564, 579-80 (1973); Hostetter v. Idlewild Bon Voyage Liquor Corp., 377 U.S. 324, 328-29 (1964).

by having filed complaints in the state courts before the running of the statute of limitations. The *Sederquist* court found that no other factors were involved that would justify an immediate adjudication by the federal court, the *Sante Fe* court failed to discuss this possibility. Although the facts do not indicate that such factors exist, the court was remiss in not including a discussion of this issue in its opinion. In any case, the plaintiffs retain their right to return to federal court if any federal issues remain after a state decision.[31]

The Ninth Circuit Court of Appeals did not choose to broaden the scope of abstention in these cases. Although it has been suggested that land use is an area of state law which is so sensitive that its importance outweighs the outcome of a particular case, and that whenever a case involves land use issues abstention should be ordered with no further consideration,[32] the Ninth Circuit did not so rule. Thus, *Sederquist* and *Sante Fe* represent the straightforward application of the *Pullman* abstention doctrine rather than an extension of the circumstances under which a federal court may refuse to exercise its jurisdiction.

Edward Willner

II. PLAINTIFF'S FIFTH AMENDMENT PRIVILEGE IN CIVIL SUITS

A. INTRODUCTION

In *Campbell v. Gerrans,*[1] the Ninth Circuit Court of Appeals held that a federal district court may not dismiss a civil rights action simply because a plaintiff refuses to answer specific interrogatories on fifth amendment grounds. In *Campbell,* plaintiffs sued two San Francisco police officers for assault, invasion of privacy, and unjustified seizure of property in connection with a warrantless search[2] of plaintiffs' automobile, persons, and apart-

31. England v. Louisiana State Bd. of Medical Examiners, 375 U.S. at 416.

32. *See* text accompanying notes 17 and 29 *supra.*

1. 592 F.2d 1054 (9th Cir. Mar., 1979) (per Kerr, D.J., sitting by designation; the other panel members were Choy and Sneed JJ.).

2. Plaintiff Charles Campbell had pled guilty to one count of possession of heroin. CAL. HEALTH & SAFETY CODE § 11550 (Deering 1975). For this and a subsequent violation of the same statute, he was sentenced to a term in jail and was later placed on probation.

ment.[3] In the course of that search, defendants discovered several articles that could reasonably lead to a finding that either or both of the plaintiffs were engaged in the selling of heroin.[4]

Plaintiffs brought a civil rights action in federal court.[5] During discovery proceedings, plaintiffs were served with a total of thirty-four interrogatories by the defendants. Of these questions, plaintiffs finally answered thirty and refused to answer four on the ground that the answers might contain potentially self-incriminating evidence.[6] Although ordered by the court to answer, plaintiffs refused.

The district court, relying on *Lyons v. Johnson,*[7] ruled that plaintiffs' refusal to answer the interrogatories constituted a "willful default," and dismissed the action. The court of appeals reversed, distinguishing *Lyons* from the present case, and ruled that plaintiffs' refusal to answer the interrogatories was justified.

One of the conditions of his probation was that he submit to warrantless searches of his person, premises, and automobile. 592 F.2d at 1055.

3. The other plaintiff in this action was Charles Campbell's wife, Elizabeth. Although legally married, the plaintiffs had separated and maintained separate residences since the time Charles pled guilty to possession of heroin. The search complained of took place at Elizabeth's apartment. It was not a condition of Charles' probation that his wife also submit to warrantless searches. *Id.*

4. The items seized included the following: 1,682 balloons, a container of lactose, a funnel, a strainer, spoons, a savings account passbook, a key to a safety deposit box, and a pistol. Two days after the initial search, the defendants searched the safety deposit box pursuant to a search warrant and found $2,240. *Id.*

5. Federal jurisdiction was predicated on 42 U.S.C. § 1983 (1976), which grants federal jurisdiction in civil rights actions.

6. The four questions which plaintiffs refused to answer were:

> 31. In regard to [the items seized by defendants, please state] a) Who the owner was of said items . . . d) Use to which item was to be put by the owner thereof.
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> 32. Within the two year period preceding July 9, 1973, have you ever made a sale of heroin? If so, please state: a) Date of sale; b) Name and address of person to whom sale was made; c) The quantity sold.
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> 33. In regard to [the money seized from plaintiffs' safety deposit box], please state: a) The owner of said funds; b) Date(s) said funds were acquired; d) Whether said funds acquired by gift or by exchange of consideration; e) Nature of consideration, if appropriate.
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> 34. In regard to [the money and bank book found on plaintiffs' premises], please state . . . c) Person from whom said funds were acquired; d) Whether said funds acquired by gift or by exchange of consideration; e) Nature of consideration, if appropriate.

592 F.2d at 1056.

7. 415 F.2d 540 (9th Cir. 1969), *cert. denied,* 397 U.S. 1027 (1970).

B. The Privilege Against Self-Incrimination

The scope of discovery is limited to matter that is "not privileged."[8] Thus, information that would tend to be self-incriminating is clearly not discoverable in a criminal suit.[9] Until the mid-nineteenth century, the fifth amendment was strictly construed, and the privilege against self-incrimination did not apply in civil suits.[10] Since that time, however, the privilege has been available to the parties or witnesses in a civil suit as well.[11] The only requirement has been that the answer to a given question might lead to information needed to prosecute the party or witness of a crime,[12] regardless of how remote the possibility of prosecution.[13] This privilege has been held to be applicable to discovery in general and, in particular, will justify the refusal to answer interrogatories.[14]

It has been suggested that by bringing or defending a civil suit a party waives his privilege against self-incrimination.[15] However, there is no case law holding that by exercising the constitutional right to bring or defend a lawsuit, a party must automatically waive the constitutional privilege against self-incrimination.[16] If a party has actually waived his fifth amend-

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8. Fed. R. Civ. P. 26(b)(1). What is "privileged" is defined by the rules of evidence. Hickman v. Taylor, 329 U.S. 495, 507-08 (1947), *reh. denied*, 336 U.S. 921 (1949). Federal common law governs the scope of privilege "in light of reason and experience." Fed. R. Evid. 501 (1975).

9. U.S. Const. amend. V provides: "No person . . . shall be compelled in any criminal case to be a witness against himself."

10. J. Wigmore, Evidence § 2252, at 325 (McNaughton rev. 1961).

11. *Id.* at 327 § 2257 n.19. That the privilege against self-incrimination was available to civil litigants who might be subject to a criminal action was deemed well established by 1924. McCarthy v. Arndstein, 266 U.S. 34, 40 (1924).

12. Hoffman v. United States, 341 U.S. 479, 486 (1951).

13. For example, in Antonio v. Solomon, 42 F.R.D. 320 (D. Mass. 1967), the privilege was granted where there was a "remote" possibility that the answer to the challenged question might lead to criminal liability. In *In re* Master Key Litigation, 507 F.2d 292 (9th Cir. 1974), the court held that the right to object to questions depended on the *possibility* that criminal liability might result, not the likelihood that such an action would be brought.

14. United States v. 47 Bottles, etc., 26 F.R.D. 4 (D.N.J. 1960), *cert. denied*, 375 U.S. 953 (1963).

15. *E.g.*, Independent Productions Corp. v. Loew's, Inc., 22 F.R.D. 266, 276-78 (D.C.N.Y. 1958) where the court cited J. Moore, Federal Rules and Official Forms 164 (1956) as suggesting that "plaintiffs must be deemed to have waived their assumed privileges by bringing [an] action." 22 F.R.D. at 276. The court cited no supporting law, however, and the court's discussion of waiver was not necessary to the decision.

16. Jones v. B.C. Christopher & Co., 466 F. Supp. 213, 223 (D. Kan. 1979), *citing* Mitchell v. Roma, 265 F.2d 633 (3d Cir. 1959).

ment privilege, however, he may be compelled to answer all relevant questions on pain of contempt.[17]

The fifth amendment privilege will not excuse a litigant from submitting to all discovery. Rather, the party must answer any questions which do not raise fifth amendment issues and make a proper objection to those questions which do raise such issues.[18] If the discovering party believes that the claim of privilege is an improper one, he may then move to compel discovery.[19] If the court rules that no fifth amendment privilege applies to a specific question, then an order compelling discovery should be issued.

In the great majority of cases where the issue arises, the party claiming the fifth amendment privilege is the defendant. Because the plaintiff is a voluntary litigant while the defendant is not, courts have often treated the parties differently in terms of the right to plead the fifth amendment.[20] Although no court has ruled that a plaintiff automatically waives the fifth amendment privilege merely by bringing suit, many courts have held that absent one narrow exception, plaintiff must either answer all relevant questions or face dismissal.[21] While the two concepts may appear similar at first blush, they are substantially different. If it were held that a party waived the privilege by bringing or defending a suit, then that party would be forced to answer all questions or be held in contempt. On the other hand, the rule that has been established by some courts is that a plaintiff cannot be forced to provide self-incriminating evidence. That is, a plaintiff has a clear choice between maintaining an action and providing self-incriminating information.

C. The Court's Analysis

Relying on Supreme Court precedent,[22] the court of appeals held that the privilege against self-incrimination can be asserted in any proceeding, civil or criminal. Without discussion or support for the assertion, the court further held that those cases in which sanctions have been imposed for the refusal to answer in-

17. *E.g.*, Brown v. United States, 356 U.S. 148, 156, *reh. denied*, 356 U.S. 948 (1958).
18. Fed. R. Civ. P. 37(a)(2).
19. Fed. R. Civ. P. 37(b)(2).
20. *See* Jones v. B.C. Christopher & Co., 466 F. Supp. 213 (D. Kan. 1979), and note 27 *infra* and accompanying text.
21. *Id.*
22. Kastigar v. United States, 406 U.S. 441, 444 (1972).

terrogatories were distinguishable on their facts. The court distinguished its prior holding in *Lyons v. Johnson,*[23] upon which the lower court based its dismissal, from the present case. In *Lyons,* the plaintiff refused to answer *all* interrogatories, including those questions asking for mere background information. In the present case, however, plaintiffs refused to answer only those particular questions that obviously raised fifth amendment issues. The court failed to draw any other distinctions between the two cases.

The court decided that whenever a party responds to interrogatories with a fifth amendment plea, a court must determine whether the answer to a particular question could provide evidence that could be used in a criminal suit against the objecting party. A fifth amendment objection would be proper only if the answer to a particular question leads to criminal liability. The court made no reference to any possible differences between a plaintiff's and defendant's right to refuse to answer interrogatories. The court concluded that because plaintiff's assertion of the privilege was proper, no sanction could be imposed.[24]

D. SIGNIFICANCE

The Ninth Circuit stands alone in advancing the foregoing analysis of plaintiff's right to invoke the fifth amendment privilege in respone to interrogatories. The most obvious difference between the rule set forth in *Campbell* and that established by the other circuits is that the *Campbell* court did not draw any distinction between a plaintiff's right to assert the privilege and a defendant's right to do so.[25]

The court cited four federal cases purportedly standing for the proposition that *a party* has the right to refuse to answer

23. 415 F.2d 540 (9th Cir. 1969), *cert. denied,* 397 U.S. 1027 (1970).

24. The court based this holding on Griffin v. California, 380 U.S. 609, *reh. denied,* 381 U.S. 957 (1965), which held that dismissal of a suit in which a proper fifth amendment objection has been made is not permissible because that sanction makes the assertion of a constitutional privilege "costly." *See* Spevack v. Klein, 385 U.S. 511, 515 (1967). The court relied on cases from the Second Circuit which held that a party's day in court should not be denied unless there is a showing of "willful default." Trans World Airlines v. Hughes, 332 F.2d 602 (2d Cir. 1964); Gill v. Stolow, 240 F.2d 669 (2d Cir. 1957). In each of these cases, the party claiming the Fifth Amendment privilege was the defendant. The *Campbell* court did not acknowledge this fact.

25. For a thorough analysis of the distinction between plaintiff's and defendant's fifth amendment privilege, *see* Jones v. B.C. Christopher & Co., 466 F. Supp. 213 (D. Kan. 1979).

interrogatories on fifth amendment grounds without the possibility of dismissal.[26] Each of these cases, however, involved a *defendant's* refusal to answer questions during discovery. While it is well established that a defendant has the right to assert his fifth amendment privilege in refusing to answer questions during discovery, virtually every court which has considered the matter has refused to grant this right to a *plaintiff.*[27] At first glance, this may seem to be an unjust view since the two parties are treated differently. Since on its face the fifth amendment applies to anyone who might be made subject to criminal prosecution, the denial of a plaintiff's right to refuse to answer so long as he maintains an action may appear to some to be an automatic waiver of the privilege. However, no court which has considered the matter has construed the privilege in that light.

In *Independent Productions Corp. v. Loew's, Inc.*,[28] a New York district court drew the distinction between a plaintiff and a defendant in a civil suit stating: "It would be uneven justice to permit plaintiffs to invoke the powers of this court for the purpose of seeking redress and, at the same time, to permit plaintiffs to fend off questions, the answers to which may constitute a valid defense or materially aid in the defense."[29] While plaintiffs are voluntary litigants, defendants are not, and to allow plaintiffs to use the court both to redress a grievance and to shield itself from discovery is substantially unfair.[30] The universal rule is that a

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26. Bowles v. Trowbridge, 60 F. Supp. 48 (C.D. Cal. 1945); United States v. 47 Bottles, etc., 26 F.R.D. 4 (D.N.J. 1960), *cert. denied*, 375 U.S. 953 (1963); United States v. Fishman, 15 F.R.D. 151 (C.D.N.Y. 1953); Hope v. Burns, 6 F.R.D. 556 (E.D. Ky. 1947).

27. DeVita v. Sills, 422 F.2d 1172, 1183 (3d Cir. 1970); Lyons v. Johnson, 415 F.2d 540 (9th Cir. 1969), *cert. denied*, 397 U.S. 1027 (1970); Penn Communications Specialties, Inc. v. Hess, 65 F.R.D. 510 (E.D. Pa. 1975); Brown v. Ames, 346 F. Supp. 1176 (D. Minn. 1972); Duffy v. Currier, 291 F. Supp. 810 (D. Minn. 1968); Independent Productions Corp., v. Loew's, Inc., 22 F.R.D. 266 (S.D.N.Y. 1958); Lund v. Lund, 161 So.2d 873 (1964); Stockham v. Stockham, 168 So.2d 320 (1964); Franklin v. Franklin, 365 Mo. 442, 283 S.W.2d 483 (1955); Levine v. Bornstein, 13 Misc.2d 161, 174 N.Y.S.2d 574, aff'd, 7 App. Div. 2d 995, 183 N.Y.S.2d 868 (2d Dept.), *aff'd*, 6 N.Y.2d 892, 160 N.E.2d 921, 190 N.Y.S.2d 702 (1959); Annot., 4 A.L.R.3d 545 (1965).

The *Campbell* court relied on Buzard v. Griffin, 89 Ariz. 42, 358 P.2d 155 (1960) in holding that a party is sometimes justified in refusing to answer questions propounded during discovery proceedings. In *Buzard*, the party objecting to the questions on fifth amendment grounds was a defendant.

Only one case has held that a plaintiff is generally allowed to refuse to answer discovery on fifth amendment grounds and it has since been overruled. Simkins v. Simkins, 219 So.2d 724 (1969), *rev'd*, Minor v. Minor, 240 So.2d 301 (1970).

28. 22 F.R.D. 266 (S.D.N.Y. 1958).

29. *Id.* at 276.

30. Courts have used various images to illustrate this idea: for example, in Indepen-

plaintiff may not refuse to answer discovery questions and continue to maintain the action. If a plaintiff does persist in asserting the privilege, his action will be dismissed. The courts distinguish this from a true waiver because plaintiff is never prevented from asserting the privilege by the threat of contempt.

Although the court failed to draw the essential distinction between a plaintiff's and a defendant's right to plead the fifth amendment, it must be admitted that if plaintiffs' civil rights were violated by the search and seizure, dismissal is too harsh a sanction. It does appear, however, that the court's ruling could have been justified on other, better established grounds.

There is an exception by which some circuits allow a plaintiff to assert the privilege while maintaining a civil action.[31] In these cases, there was an identity of interest between the civil defendants and the potential prosecuting party in the anticipated criminal action. This situation frequently occurs when a taxpayer sues the Internal Revenue Service for a refund and the United States serves interrogatories seeking the source of the income. If the income was derived from illegal sources, then the United States will have gained information it will need to prosecute the civil plaintiff in a related criminal action.[32] In *Campbell,* there was not a complete identity between the civil defendant and the potential criminal plaintiff only because the government was immune from suit when this action was brought.[33] It is reasonable

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dent Productions Corp., the court refused to allow plaintiffs to use the privilege as both a "shield and a sword." *Id.* at 267. *Accord,* Kisting v. Westchester Fire Ins. Co., 290 F. Supp. 141 (W.D (W.D. Wisc. 1968), *aff'd,* 416 F.2d 967 (7th Cir. 1969). In Jones v. B.C. Christopher & Co., 466 F. Supp. 213 (D. Kan. 1979), the court refused to allow plaintiff to "have his cake and eat it too."

31. *See* Thomas v. United States, 531 F.2d 746 (5th Cir. 1976); Shaffer v. United States, 528 F.2d 920 (4th Cir. 1975); Ianelli v. Long, 487 F.2d 317 (3d Cir.), *cert. denied,* 414 U.S. 1040 (1973). Although no circuit has specifically rejected this exception to the general rule that a civil plaintiff must answer questions propounded during discovery or face dismissal, not all circuits have considered the matter. In one case that is factually similar to *Campbell,* a district court dismissed an action when the civil plaintiff refused to answer specific questions that raised fifth amendment issues. The court did not consider whether that case came within the exception. Brown v. Ames, 346 F. Supp. 1176 (D. Minn. 1972).

32. *See* Shaffer v. United States, 528 F.2d 920 (4th Cir. 1975), where the civil plaintiff was allowed to refuse to answer discovery questions on the ground that the collection procedure was instituted in order to coerce the taxpayer to incriminate himself.

33. At the time the present suit was instituted in district court, a municipality was not considered a "person" under 42 U.S.C. § 1983 (1976). Thus, plaintiffs could not have named the City and County of San Francisco as a co-defendant. Moor v. County of Alameda, 411 U.S. 693 (1973); Monroe v. Pape, 365 U.S. 167 (1961). Between the time

to expect that any information defendant police officers obtain concerning plaintiffs' use or possession of heroin would be immediately turned over to the prosecutor. Thus, a reasonable analogy may be made between the present case and those cases in which the civil defendant and the potential criminal plaintiff are identical. Had the court followed this line of reasoning, the result that was reached could have been based on established case law.

E. Conclusion

In *Campbell*, the Ninth Circuit has carved out its own rule concerning the right of plaintiff to refuse to answer interrogatories on fifth amendment grounds. Only the Ninth Circuit has ruled that this right exists whenever a plaintiff makes a valid assertion of the privilege to a specific question. If the court had intended to create its own rule on this issue, an explicit rejection of the overwhelming majority rule would have been appropriate. The court's failure to recognize the essential distinction between plaintiff's and defendant's right to rely on the fifth amendment in refusing to answer interrogatories appears to be a major flaw in the court's reasoning. Furthermore, if the court had adopted the majority view, the same result could have been reached by recognizing that the present case falls within an established exception to that majority rule.

Edward Willner

III. IMPLYING PRIVATE RIGHTS OF ACTION IN AREAS OF INDIVIDUAL RIGHTS

A. Introduction

In *Keaukaha-Panaewa Community Association v. Hawaiian Homes Commission,*[1] the Ninth Circuit considered the implica-

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the suit was brought and the appeal, the Supreme Court overruled that portion of *Monroe* granting absolute immunity to municipalities. Monell v. Department of Social Services, 436 U.S. 658, 663 (1978). Under present law, therefore, San Francisco could have been named a co-defendant, thus making the identity between the civil defendant and the criminal plaintiff complete. Even if the immunity rule were still followed, the resulting lack of identity of parties should not alter plaintiffs' fifth amendment rights. The possibility of criminal prosecution is as great as it would be if the government were presently a co-defendant.

For a further discussion of a municipality's liabblity in civil rights actions, see Note, *Municipal Liability for Civil Rights Violations, Ninth Circuit Survey,* 10 Golden Gate U. L. Rev. 27 (1979).

1. 588 F.2d 1216 (9th Cir. Sept., 1978) (per Wallace, J.; the other panel members were

tion of a private right of action and the extension of federal subject matter jurisdiction. The action was brought by a group of native Hawaiians seeking declaratory and injunctive relief for the construction of a flood control project, which was allegedly in violation of the Hawaiian Admission Act of 1959[2] (Admission Act) and the Hawaiian Homes Commission Act of 1921[3] (Commission Act).

The Commission Act originally designated 200,000 acres of Hawaiian land for the welfare and rehabilitation of native Hawaiians. The Admission Act transferred responsibility for the home lands to the State of Hawaii. Under section 5(f) of the Admission Act, Hawaii is to hold the lands in public trust. The United States may sue for any breach of that trust. Since the proposed project was to be constructed on twelve acres of native home lands, the County of Hawaii turned to the Hawaiian Homes Commission, which had the power to lease the land in question. The Commission agreed to exchange an amount of home lands for equivalent acreage in county land.[4]

Chambers and Anderson, JJ.), *cert. denied*, 100 S.Ct. 49 (1979).

2. Hawaii Admission Act, 48 U.S.C. Prec. § 491 (Supp. 1979). Section 4 provides, in pertinent part, that "as a compact with the United States relating to the management and disposition of the Hawaiian home lands, the Hawaiian Homes Commission Act, 1920, as amended, shall be adopted as a provision of the Constitution of said State. . . ." *Id.* Section 5(f) provides, in pertinent part:

> [A]ny such lands and the income therefrom, shall be held by said State as a public trust for the support of the public schools and other public educational institutions, for the betterment of the conditions of native Hawaiians, as defined in the Hawaiian Homes Commission Act, 1920, as amended, for the development of farm and home ownership on as widespread a basis as possible for the making of public improvements, and for the provision of lands for public use. Such lands, proceeds, and income shall be managed and disposed of for one or more of the foregoing purposes in such manner as the constitution and laws of said State may provide, and their use for any other object shall constitute a breach of trust for which suit may be brought by the United States.

Id. The court accepted the validity of the assertion that the home lands may still be used lawfully only in the manner set forth in the Commission Act. 588 F.2d at 1218 n.2.

3. The 1920 Hawaiian Homes Commission Act, 48 U.S.C. §§ 691-716 (1952). (The current version was incorporated into the Hawaiian Constitution by the Hawaii Admission Act, 48 U.S.C. Prec. § 481 (Supp. 1979)).

4. The amount of land was increased to 25 acres. In 1954, Congress amended § 204(4) of the Commission Act to permit the Commission, under certain circumstances, to exchange property under its jurisdiction for lands of equal value. Act of June 18, 1954, ch. 319, 68 Stat. 262 (1954).

The plaintiffs asserted five causes of action in an attempt to block the project and to ascertain their rights.[5] The Commission moved to dismiss the action for lack of federal subject matter jurisdiction.[6] The district court denied the motion to dismiss and held that federal jurisdiction existed since both acts were federal statutes. The district court further granted plaintiffs' motion for summary judgment on four of the five claims.[7]

On appeal, the Ninth Circuit reversed, holding that there was no implied private cause of action under the Admission Act. The court therefore, found it unnecessary to determine if jurisdiction existed under that Act.[8] The court further held that there was no federal jurisdiction to consider claims brought under the Commission Act and, therefore, it chose not to confront the issue of an implied private cause of action under that Act.[9]

B. Background: Implication of a Private Cause of Action

In instances where legislation has not explicitly granted an individual the right to bring suit, the courts have been faced with the task of either denying a private action or deciding under what circumstances to imply such a right. The early cases which considered this issue adopted a liberal stance.[10] In 1916, the Supreme

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5. The court described the claims as follows:

> First, plaintiffs claim that the Commission has violated § 204(4) of the Commission Act by agreeing to exchange lands for a purpose other than those permitted by the Act. Second, the plaintiffs claim that the Commission has violated § 204(4) by permitting the County to render home lands useless for their designated purpose without first receiving title to lands received in compensation. Third, plaintiffs claim that the Commission violated § 204(4) by failing to obtain the consent of the Governor and the Secretary of Interior for the proposed exchange. Fourth, plaintiffs allege the project is "illegal" because it will consume twice the amount of home lands originally approved by the Commission. Finally, plaintiffs claim that the Commission has violated fiduciary obligations imposed upon it by §§ 4 and 5 of the Admission Act.

588 F.2d at 1219. Plaintiff's first, second and third claims were premised on the Commission Act; the fourth claim was based on both the Admission and Commission Acts; and the fifth claim was based on the Admission Act. *Id.*

6. *Id.* at 1220. The Commission relied on 28 U.S.C. § 1331(a).

7. Summary judgment was denied on plaintiff's first claim, which alleged a violation of the Commission Act by agreeing to exchange lands for a purpose other than those permitted by the Act.

8. 588 F.2d at 1220. Jurisdiction is a primary requirement. Any order given without proper jurisdiction is invalid. *See* D. Dobbs, Remedies § 2.7 at 83-84 (1973).

9. 588 F.2d at 1220.

10. *See generally* Note, *Analytical Framework for Implied Causes of Action: Section*

Court in *Texas Pacific Railway v. Rigsby*[11] stated, "in every case, where a statute enacts, or prohibits a thing for the benefit of a person, he shall have a remedy upon the same statute for the thing enacted for his advantage . . .." Years later, in *J.I. Case Co. v. Borak,*[12] the Court modified the broad guidelines of *Rigsby* by considering whether the chief purpose of the legislation was to benefit the plaintiff and whether the implication of a remedy was necessary to carry out the congressional purpose.[13]

In 1974, however, the Supreme Court shifted away from its liberal policy of implying private remedies to a more strict constructionist viewpoint. The two leading cases to expound this viewpoint were *National Railroad Passenger Corp. v. National Association of Railroad Passengers (Amtrak)*[14] and *Securities Investor Protection Corp. v. Barbour (SIPC).*[15]

The Court in *Amtrak* held that no remedy would lie beyond that which was expressly stated in the statute.[16] Thus, only the Attorney General could maintain a cause of action to enforce the terms of the Rail Passenger Service Act of 1970. Since the National Association of Railroad Passengers had not *explicitly* been granted the right to sue, it was precluded from bringing suit under that Act.

Analytically, the importance of the *Amtrak* decision was its dependence upon the old Latin maxim—*expressio unius est ex-*

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17 of the Securities Exchange Act and Redington v. Touche Ross & Co., 59 B.U.L. REV. 157 (1979); Note, *Implication of Private Causes of Action from Federal Statutes*, 1 J. CORP. L. 371 (1976); Note, *Implied Civil Remedies from Federal Regulatory Statutes*, 77 HARV. L. REV. 285 (1963).

11. 241 U.S. 33 (1916) (an employee sought relief in a tort action under criminal provisions of the Federal Safety Appliance Act against an interstate railroad).

12. 377 U.S. 426 (1964) (the Court dealt with remedies under § 14(a) of the 1934 Securities Exchange Act, regarding circulation of misleading proxy materials which deprived a stockholder of his preemptive rights).

13. The Court implied a private remedy even though the legislative history was silent on the issue. *Id.* at 431-32. *See* Wyandotte Transportation Co. v. United States, 389 U.S. 191 (1967) where the Court found an implied right to sue by the Government under § 15 of the Rivers and Harbors Act, 33 U.S.C. § 409 (1970). The Act provided for express criminal sanctions which the Court felt were inadequate as a remedy.

14. 414 U.S. 453 (1974), *reh. denied*, 415 U.S. 952 (1975). The Court refused to imply a private right of action for railroad passengers. The Court took the opposite approach from the *Borak* Court, creating a presumption against implication.

15. 421 U.S. 412 (1975). The Court refused to allow private actions under the Securities Investor Protection Act of 1970, which was enforceable by administrative proceedings and government suits.

16. 414 U.S. at 464.

clusio alterus—expression of one remedy is the exclusion of others. This principle dictates a narrow statutory application of federal legislation and greatly reduces the number of potential plaintiffs under any act which does not specify precisely who can sue to enforce its terms. This principle was followed in *SIPC* where the Court found that an implied private right of action did not exist in favor of customers of a failing brokerage house to compel SIPC "to exercise its statutory authority for their benefit."[17] In so deciding, the Court relied heavily upon *Amtrak*'s use of the *expressio unius* rule.

In the midst of this conflict between liberal application and strict statutory reading, the Supreme Court in *Cort v. Ash*,[18] set forth a four-factor test for determining when an implied private right of action should be found:

> [F]irst, is the plaintiff "one of the class for whose *especial* benefit the statute was enacted,"—that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely in federal law?[19]

The *Cort* Court concluded that under its test, which had been drawn from elements of both previous theories, there was no implied private action for damages in favor of stockholders of a corporation for corporate violations of a criminal statute which prohibited contributions to presidential campaigns. The Supreme Court maintained that the *expressio unius* rule is permissible when it is supported by legislative history. Silence may be

17. 421 U.S. at 414.

18. 422 U.S. 66 (1975). The Court refused to imply a private cause of action for stockholders against corporate directors for violations of a criminal statute which prohibited contributions to presidential campaigns. Fed. Corrupt Practices Act, 18 U.S.C. § 610 (1970).

19. 422 U.S. at 78 (citation omitted). The Court held that when it is clear that federal law has created rights for a class of persons, "it is not necessary to show an intention to create a private cause of action. . . ." *Id.*

used as an indication of legislative intent, but it is not determinative.[20]

In the Supreme Court decision in *Cannon v. University of Chicago,* after applying the four *Cort* factors, a private right of action was implied under Title IX of the Education Amendments of 1972.[21] However, more recently in *Transamerica Mortgage Advisors, Inc. v. Lewis (TAMA),*[22] the Supreme Court held that under the Investment Advisors Act of 1940[23] a limited private right of action was implied for injunctive relief or recission of advisory contracts, but no right was implied for damages under the Act. The Court did not apply the *Cort* test but held that the ultimate issue was the determination of Congressional intent. No further guidelines were given. Both *Canon* and *TAMA* were decided after *Keaukaha* and therefore, are not the focus of this note. Nonetheless these decisions indicate a continuing split in the Supreme Court on the issue of implying a private right of action.

C. Ninth Circuit's Analysis in Refusing to Imply a Private Cause of Action

The decision in *Keaukaha* not to imply a private cause of action was based primarily upon *Amtrak*'s use of the *expressio unius* rule. The Ninth Circuit acknowledged the *Cort* test but used it as after-the-fact support rather than as an initial determinative tool.

The Ninth Circuit in *Keaukaha* has interpreted *Cort* as rejecting the *Amtrak* approach "requir[ing] the inference of legislative intent not to provide a private remedy."[24] However, *Cort* distinguished *Amtrak* on the ground that its use of the *expressio unius* principle was permissible when specifically supported by legislative history. To the *Keaukaha* court, this distinction con-

20. 441 U.S. 677 (1979) (Powell, J. and White J. filed separate dissents), *reversing,* Cannon v. University of Chicago, 559 F.2d 1063 (7th Cir. 1976).

21. 20 U.S.C. §§ 1681 *et seq. See* text accompanying notes 28 to 31 *infra.*

22. No. 77-1645 (Nov. 13, 1979) *rev'd,* 575 F.2d 237 (9th Cir. 1978) (White, J., filed a dissenting opinion and was joined by Brennan, Marshall and Stevens, JJ.). The dissent strongly relies on use of the *Cort* analysis and would have applied a private right of action in this instance. *See* Touche Ross v. Reddington, No. 78-309 [1979] Fed. Sec. L. Rep. (CCH) ¶ 96,894 (June 18, 1979), *rev'd,* 592 F.2d 617 (2d Cir. 1978), in which the Court refused to imply a private cause of action for damages under § 17(a) of the Securities Exchange Act of 1934.

23. 15 U.S.C. § 806-1 *et. seq.* (1971).

24. 588 F.2d at 1222.

flicted with "Amtrak's teaching that this inference [*expressio unius*] is operative unless contradicted by 'clear contrary evidence of legislative intent.'"[25] Thus, apparently in cases where there is some legislative comment, the *Cort* test should be applied. When there is silence, *Amtrak* "remains controlling precedent." The Ninth Circuit, however, does not provide support for this conclusionary interpretation.

After holding *Amtrak* controlling, the court applied the *Cort* test. It agreed that plaintiffs met the first criterion of "being members of the class for whose especial benefit the statute was enacted." In regard to the second criterion—express or implied legislative intent—the Ninth Circuit found only legislative silence. Therefore, it applied *expressio unius* to deny implication.

The Ninth Circuit saw the third criterion of "being consonant with the general scheme and purposes of the statute" as a close question. However, it felt the issue involved purely Hawaiian officials and lands. Thus, no federal purpose would be served "by reading a private cause of action into the Admission Act." Using the same reasoning, the court held the final criterion of "being a concern of the States" dictated against implying a private right of action in this factual situation.[26]

D. Ninth Circuit's Reasoning in Denying a Private Cause of Action Under the Admission Act

Native Hawaiians are in an analogous position to American Indians and logically, therefore, they should be afforded the same legal treatment regarding private causes of action.[27] A review of pertinent Ninth Circuit decisions regarding implication of private rights of action in general and to Indians, in particular, puts *Keaukaha* in sharp contrast with recent trends in federal law.

Generally, the Ninth Circuit has rejected the use of *expressio unius*. Rather, it has held the initial question to be whether the

25. *Id.* (emphasis in original).

26. *Id.* at 1224.

27. *See generally* Levy, *Native Hawaiian Land Rights*, 63 Cal. L. Rev. 848 (1975), in which the author states, "[a]lthough Native Hawaiians cannot properly be called American Indians in an anthropological sense, the plight of both groups as indigenous peoples within the United States calls for analogous legal treatment." *Id.* at 875. The author comments in footnote that "[t]he United States Supreme Court has never defined the term 'Indian' but has implicitly expanded its meaning to include Alaskan Aleuts and Eskimos, non Indians under an 'anthropological' meaning." *Id.*, n.215 (citation omitted).

statute might be insured fuller effectiveness by allowing a private remedy. This kind of reasoning dictates the use of a logical balancing approach, i.e. the *Cort* test rather than blind application of an outdated Latin maxim. Additionally, the Ninth Circuit has been especially sensitive to protecting the rights of native Americans, specifically American Indians.

In *Agua Caliente Band of Mission Indians v. County of Riverside*[29] (*Agua Caliente*), the Ninth Circuit held that "an Indian, as the beneficial owner of lands held by the United States in trust has a right acting independently of the United States to sue to protect his property interests."[30] This applicaiton of a "co-plaintiff" rule was based on a unanimous opinion delivered by Chief Justice Earl Warren in *Poafpybitty v. Skelly Oil Co.*[31]

In *Poafpybitty,* Chief Justice Warren stated that "the allotment system was created with the Indians receiving ownership rights in the land while the United States retained the power to scrutinize the various transactions by which the Indian might be separated from that property."[32] It would, in the opinion of the Chief Justice, frustrate that purpose to disallow Indians a right to bring suit.

In the present case, the Admission Act provides that the home lands are to be held in trust by Hawaii "for the betterment of the conditions of native Hawaiians" by the "development of farm and home ownership." Any other use would constitute "a breach of trust for which suit may be brought by the United States."[33] Except that in *Poafpybitty* and *Agua Caliente,* the

28. *See, e.g.,* Stewart v. Travelers Corp., 503 F.2d 108 (9th Cir. 1974); Burke v. Compania Mexicana de Aviacion, 433 F.2d 1031 (9th Cir. 1970); Matheson v. Armbrust, 284 F.2d 670 (9th Cir. 1960).

In *Stewart,* the Ninth Circuit implied a private right of action under the Consumer Protection Act, 15 U.S.C. § 167(a), which forbids the discharge of an employee due to garnishment of wages for one indebtedness. Use of *expressio unius* was strictly limited to ensuring the full effectiveness of the statute. In *Burke,* a private civil right was implied from a statute containing criminal penalties. The court held that in the absence of clear intent to the contrary, courts are free to fashion appropriate remedies. In *Matehson,* the court expressly refused to apply *expressio unius* and implied a private right of action under § 10(b) of the Securities Exchange Act of 1934.

29. 442 F.2d 1184 (9th Cir. 1971) *cert. denied,* 405 U.S. 933 (1972). *See also* Moses v. Kinnear, 490 F.2d 21, 25 (9th Cir. 1973).

30. 442 F.2d at 1186.

31. 390 U.S. 365 (1968).

32. *Id.* at 369.

33. 588 F.2d at 1218.

trustor was the United States and in *Keaukaha* it is the State of Hawaii, the schemes appear analogous.[34] Yet, the outcome is opposite.

In the recent Supreme Court case of *Cannon v. University of Chicago*,[35] the Court affirmed the use of the *Cort* test rather than mere application of the *Amtrak* approach.[36] Justice Stevens, writing for the majority, signalled the underlying thrust when he stated:

> This Court has never refused to imply a cause of action where the language of the statute explicitly conferred a right directly on a class of persons that included the plaintiff in the case. Conversely, the Court has been especially reluctant to imply causes of action under statutes that create duties on the part of persons for the benefit of the public at large.[37]

The *Cannon* Court, quoting from *Cort*, noted "that the legislative history of a statute that does not expressly create or deny a private remedy will typically be silent or ambiguous on the question."[38] This was precisely the situation in *Keaukaha*.

E. Conclusion: Denial of an Implied Private Cause of Action

The Ninth Circuit has based its decision on *Amtrak*'s use of *expressio unius*. This reliance appears misguided. In its decision, the court admits that *Cort* may be read as rejecting the *Amtrak* analysis.[39] Within the space of a few paragraphs, the weight afforded the *Amtrak* analysis shifts from "a controlling precedent" to "at least one factor" to a "relevant factor" which cannot be given heavy reliance.[40] Further, the Ninth Circuit apparently

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34. *See* Amicus Brief at 4, Keaukaha-Panaewa Community Ass'n. v. Hawaiian Homes Comm'n, 588 F.2d 1216 (9th Cir. 1978), in which the United States Justice Department agreed that the present case is analogous to *Poafpybitty*.

Similarly, the Ninth Circuit in Capitan Grande Band of Mission Indians v. Helix Irrigation Dist., 514 F.2d 465, 470 (9th Cir. 1975), *cert. denied*, 423 U.S. 874 (1974) stated: "Indian bands and tribes have no assurance that all their claims or even all their plainly reasonable claims, with respect to trust lands will be pursued in a timely fashion by the United States."

35. 441 U.S. 677 (1979).

36. Justice Powell wrote a strong dissent as to overuse of the test. 99 S. Ct. at 1974.

37. 99 S. Ct. at 1954 n.13 (citations omitted).

38. 99 S. Ct. at 1956.

39. 588 F.2d at 1222.

40. *Id.* at 1222-1223.

feels that courts may choose either *Cort* or *Amtrak*. Yet, nowhere in *Keaukaha* or in *Cort* is there any support for the notion that *Amtrak* remains a controlling precedent when legislation is silent on rights of action.

Cort logically stands as stronger authority. It was *Cort* which expanded and set forth principles for determining when a private right of action is available. Under this test, *Amtrak* can be used for support *if* there is legislative comment. *Cort* is the test and *Amtrak* is only available for support—not the reverse, as *Keaukaha* purports.

Assuming that *Cort* is the appropriate test, an application of its factors leads to a conclusion opposite to that reached by the Ninth Circuit. First, there is no debate that plaintiffs are members of the class for whose benefit the legislation was enacted. Second, regarding legislative intent, the legislative history here is silent. It should be noted that the Ninth Circuit stated this silence was to be expected considering the nature of the Admission Act. Yet, the court insisted upon applying *expressio unius*. The only logical conclusion which can be drawn from legislative silence is ambiguity or neutrality. Thus, this factor neither supports implication nor denial of a private right. Third, regarding consonance with the general scheme of the legislation, implication is clearly favored here. The Ninth Circuit has decided the issue based on some notion of the rights and laws of Hawaii. Yet, the purpose of the legislation is the rehabilitation of native Hawaiians, not support of Hawaiian laws.

Finally, consideration was given to whetherr this area is basically the concern of the states, *as a group*. In its opinion, the Ninth Circuit asked whether the issue is a concern of Hawaii. This substitution of words misdirects attention away from the underlying nature of the concern. It is obvious Hawaii as a state has concerns in the litigation, yet, the underlying nature of the concern is the assurance of the rights of a specific minority. This essential concern is not particular to Hawaii. It is a truly national concern and should be dealt with by a federal court.

Additionally, support can be found in Justice Stevens' comment in *Cannon* regarding implying private causes of action when

the rights of a class are involved.[41] Cases which have dealt with the issue of implying private rights of action divide roughly into those which have revolved around financial concerns and those which have revolved around issues of class discrimination. In the former, for example, *Amtrak, SIPC,* and *TAMA*, courts have been reluctant to imply private rights of action. In the latter, for example, *Cannon, Poafpybitty* and *Agua Caliente*, courts have been more willing to imply such rights of action.

Therefore, *Keaukaha* should be examined both under the *Cort* test and as a case which clearly revolves around class discrimination. Thus, a private right of action should be implied to protect the purposes of the legislation and the rights of the native Hawaiians.

F. Federal Subject Matter Jurisdiction

The court in *Keaukaha* held that those claims which were based on the Commission Act could not be decided because the district court was without jurisdiction.[42] The court noted that in determining whether federal jurisdiction existed it must determine whether the claims "arise under" the laws of the United States. To determine this, the court relied upon the "commonsense" advice of Justice Cardozo[43] where he stated that the federal *nature* of the right to be established is decisive—not the source of the authority establishing it. This is basically the approach used by the Ninth Circuit in *League to Save Lake Tahoe v. B.J.K. Corporation*,[44] a ruling prior to *Keaukaha.*

The court's denial of federal jurisdiction under the Commission Act appears correct. One danger in determining federal "nature" is that a court may look too narrowly at the face of the complaint. However, in *Keaukaha,* the court pragmatically looked well beyond the pleadings.[45] Additionally, the Commission Act has not formally been repealed and an argument could be

41. 441 U.S. at 690-93 n.13.

42. 588 F.2d at 1224.

43. Gully v. First National Bank, 299 U.S. 109, 116 (1936), *quoting* Puerto Rico v. Russell & Co., 288 U.S. 476, 483 (1932).

44. 547 F.2d 1072 (9th Cir. 1976). For a discussion of determining jurisdiction *see* Cohen, *The Broken Compass: The Requirement That A Case Arise 'Directly' Under Federal Law,* 115 U. Pa. L. Rev. 890 (1967); Miskin, *The Federal Question in the District Courts,* 53 Col. L. Rev. 157 (1953).

45. The court examined the history and nature of the Commission Act and Admission Act as well as requesting an Amicus Brief from the Justice Department.

made to justify jurisdiction on that basis. However, for all intents and purposes, the Commission Act has been subsumed by the Admission Act.[46] To grant jurisdiction under this argument would be an unwise affirmation of technicalities.[47]

G. Conclusion

It appears that native Hawaiians may still raise claims based on the Commission Act in a state court. However, they will still face the obstacle of showing that a private cause of action is implied under that Act. It is unclear why the Hawaiians chose to litigate in federal court. Past treatment of native Hawaiians, plus ever-encroaching progress may suggest that a federal court would have been a more neutral forum. Hawaii is a state plagued by rising land costs. Its dependence upon tourism multiplies this problem. Faced with Hawaii's need to make land available for state income and the decision in *Agua Caliente,* which appeared to recommend a federal forum for native Americans, petitioners may have seen the federal forum as more receptive.

It is difficult for the practitioner to draw guidelines from *Keaukaha.* It is unclear why, in examining the Admission Act, the threshold question was whether a private right of action was implied and why, in examining the Commission Act, the threshold question was the existence of federal jurisdiction. One possible lesson is that, even though *Canon* is a subsequent decision, the Ninth Circuit may justifiably imply private rights of action more frequently when issues of discrimination are involved. However, the recent Ninth Circuit decision in *Town of Greenhorn v. Baker County, Oregon*[48] may indicate that instead of reaching a decision on implication of a private right of action, the court may simply refuse to find federal jurisdiction.

Edmund Scott

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46. Section 4 of the Admission Act provides that the Commission "shall be adopted as a provision of the Constitution of said State. . . ."

47. If the court were to allow jurisdiction on this ground, it could open a flood gate of litigation based upon obscure law. This is contrary to modern federal civil procedure.

48. 596 F.2d 349 (9th Cir. Apr., 1979). The court held that although asserted rights originated under an act of Congress, there was no federal jurisdiction to hear the claims brought by beneficiaries of a trust established by the Townsite Act, 43 U.S.C. § 718 (1964) (repealed prospectively, 1976). The claims revolved around title to land within the county.

IV. ATTORNEY'S FEES: SURVIVAL OF THE "COMMON FUND" EXCEPTION

A. INTRODUCTION

In *City of Klawock v. Gustafson,*[1] the Ninth Circuit considered the application of the "common fund" exception[2] to the general rule denying the award of attorney's fees to a prevailing party in the absence of a statutory or valid contractual provision.

The City of Klawock, located on Prince of Wales Island in Southeastern Alaska, commenced an action to obtain title to certain vacant lots within its boundaries. The land had been reserved for territorial townsites under the Native Townsite Act of 1926 and the general Alaska townsite legislation.[3] A statutory trustee[4] was appointed to administer the property. For a number of years, the townsite had undergone a series of subdivisions and, in 1974, all subdivision plans for the townsite were completed. The trustee issued deeds to the occupants of the newly subdivided lots. Thereafter, the City of Klawock sued the trustee, the Secretary of Interior and the non-native occupants of fourteen lots claiming that (1) non-natives could not occupy the lots in question, and (2) the trustee failed to deed the vacant lots to the city.[5]

The trustee's actions were consistent with a 1959 Deputy Solicitor's opinion issued by the Interior Department, involving another townsite, which required the trustee to retain title to all

1. 585 F.2d 428 (9th Cir. Nov., 1978) (per Goodwin, J.; the other panel members were Wright, and Anderson, JJ.).

2. For a discussion of the general rule and its exception, see Dawson, *Lawyers and Involuntary Clients: Attorney Fees from Funds,* 87 HARV. L. REV. 1597 (1974); Note, *Attorney Fees: Exception to the American Rule,* 25 DRAKE L. REV. 717 (1976); Note, *Reimbursement for Attorneys' Fees from the Beneficiaries of Representative Litigation,* 58 MINN. L. REV. 933 (1974); Comment, *Court Awarded Attorney's Fees and Equal Access to the Courts,* 122 U. PA. L. REV. 636 (1974).

3. The Native Townsite Act of 1926, 43 U.S.C. § 735 (1969), and the general Alaska Townsite Legislation, 48 U.S.C. § 355 (1969), were both subsequently repealed by Federal Land Policy and Management Act of 1976, Pub. L. 94-579, 90 Stat. 2789 (1976).

4. George Gustafson, the trustee, had argued that the fees could not be awarded because the other native townsites were indispensable parties and had not been joined. The Ninth Circuit rejected this argument noting that the claim was not against the other cities but the common fund in the trustee's hands. The trustee was, therefore, held to be an indispensable party because he controlled the fund. The other cities, not being liable for fees, were not indispensable. 585 F.2d at 432.

5. *Id.* at 429.

lots until they were occupied.[6] The city, however, claimed that these actions were contrary to actions of trustees in other states where municipalities were held entitled to all unoccupied lots or to their economic benefit.[7]

The parties allowed litigation to rest pending administrative review by the Interior Department's Board of Land Appeal (BLA). The BLA upheld the trustee's position with respect to the lots occupied by non-natives; it did not decide the status of the unoccupied lots. The district court upheld the BLA ruling concerning the occupied lots and further held the trustee *had* authority to deed the 333 vacant lots to the city.[8]

The city appealed that part of the district court's decision denying it title to the fourteen occupied lots. At the same time, the Regional Solicitor issued an opinion allowing the trustee to deed the vacant lots directly to the city rather than requiring the trustee to put them up for auction.[9] Having prevailed with regard to the 333 vacant lots, the city stipulated to dismissal of its appeal.[10]

The attorneys for Klawock, on their own behalf, then petitioned the district court for an award of attorneys' fees, maintaining that the vacant lots deeded to the city constituted a common fund from which their fees could be paid.[11] The district court denied the petition, emphasizing the part of its decision denying title to the fourteen occupied lots.[12] In addition, since conveyance of the *vacant* lots in Klawock and other townsites was the result of an administrative opinion, the court held that the trustee was without authority to pay the fees.[13] The attorneys for Klawock appealed.

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6. *Id.* The 1959 Deputy Solicitor's opinion concerned the townsite of Saxon.

7. *Id.* Without citing the Deputy Solicitor's opinion, the court noted that the Deputy Solicitor had taken the position that special rules applied to native townsites in Alaska. No discussion of those rules was undertaken by the district court.

8. *Id.* at 430.

9. *Id.*

10. *Id.*

11. The vacant lots which comprise the fund are not just the 333 lots in *Klawock*, but all vacant lots which are or could be conveyed to all other cities as a result of the *Klawock* action. *Id.* at 432.

12. *Id.* at 430. The district court's reason not to hold the city as the prevailing party was based on the fact that the city had not prevailed in its action to gain title to the fourteen occupied lots. *Id.*

13. *Id.*

B. BACKGROUND

The "American" rule against the allowance of attorney's fees provides that a prevailing party cannot recover costs against a losing party, in the absence of a statute or contractual provision.[14] Recently, the United States Supreme Court in *Alyeska Pipeline Service Co. v. Wilderness Society*[15] reaffirmed the viability of the American rule. However, it recognized several equitability nonstatutory exceptions, notably the century-old common fund doctrine.[16]

The doctrine provides that "a private plaintiff, or his attorney, whose efforts create, discover, increase or preserve a fund to which others also have a claim is entitled to recover from the fund the costs of his litigation, *including attorney's fees.*"[17] The concept is based in equity and seeks to prevent unjust enrichment of persons who did not participate in litigation.

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14. 6 J. MOORE'S FEDERAL PRACTICE, ¶ 54.77[2], at 1705-6 (2d ed. 1976). For a general discussion of the American rule and its exceptions, see authorities cited at note 2 *supra*.

15. 421 U.S. 240 (1975). In *Alyeska*, the Supreme Court denied the award of fees under a "private attorney general" theory, which in effect compensates plaintiffs who incur expenses in litigation to vindicate a public right. The Court, however, reaffirmed the use of common benefit doctrine and bad faith exception. *Id.* at 257-58.

Attorneys for the City of Klawock did not present their claims under a substantial benefit (common benefit) theory, an extension of the common fund exception. This exception operates under the same equitable rationale as the common fund doctrine. It was devised to permit award of fees in cases not covered by the common fund doctrine because of the lack of a monetary fund but "yet involving interests of broad public importance, interests that Congress sought to vindicate at least in part through private litigation." Vincent v. Hughes Airwest, Inc., 557 F.2d at 768-69 n.7 (1977). *See* Hall v. Cole, 412 U.S. 1 (1973) where a union member who had been expelled by his union for criticizing union activities sued and the Court found attorneys' fees to be justified because not only had the plaintiff vindicated his own free speech rights, but he had "necessarily rendered a substantial service to his union as an institution and to all of its members." *Id.* at 8. *See* Mills v. Electric Auto-Lite Co., 396 U.S. 375 (1970), where stockholders brought a derivative suit on behalf of minority stockholders to set aside a merger on the grounds of misleading proxy statements. Attorney's fees were granted. *Id.* at 390. The Court held the actual existence of a monetary fund was unnecessary if litigation conferred a "substantial benefit on the members of an ascertainable class." *Id.* at 394. The Court held the benefit conferred was the vindication of the "fair and informed corporate sufferage. . . ." *Id.* at 396.

See generally Lipson, *Beyond Alyeska—Judicial Response to the Civil Rights Attorneys' Fees Act*, 22 ST. LOUIS U.L.J. 243 (1978); Malson, *In Response to* Alyeska—*The Civil Rights Attorney's Fees Awards Act of 1976*, 430 (1977); Note, Alyeska Pipeline Service co. v. Wilderness Society: *The Demise of the Private Attorney General Theory as a Basis for Awarding Attorneys Fees in Public Interest Litigation*, 11 TULSA L.J. 420 (1976).

16. The first case to establish the common fund doctrine was Trustees v. Greenough, 105 U.S. 527 (1881). *See* note 18 *infra* and accompanying text.

17. Vincent v. Hughes Air West, Inc., 557 F.2d 759, 769 (9th Cir. 1977) (emphasis added).

In the landmark case of *Trustees v. Greenough,*[18] the Supreme Court allowed a bondholder, who was successful in a suit brought against the trustees of a bond-guarantee fund, to recover his expenditures for attorney's fees from the trust property. The court reasoned that if the trustee had performed his duties, *his* charges would have been levied against the trust. Therefore, since the bondholder merely performed the duties of the trustee, to deny the bondholder his attorney's fees would have been unfair and would have resulted in a windfall to the other beneficiaries.[19]

The Court has expanded the common fund doctrine, approving not only the claims of a client to reimbursement of attorney's fees, as in *Greenough,* but also, to the claims of an attorney to a share of the wealth.[20] Equity is central to an understanding of the doctrine; it thereby attempts to spread litigation costs among all beneficiaries of an action on a theory that those who share the benefit should also share the burden.[21]

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18. 105 U.S. 527 (1881).

19. *Id.* at 532.

20. Central Railroad & Banking Co. v. Pettus, 113 U.S. 116 (1884). In *Pettus,* several unsecured creditors of a railroad company sued to establish a lien upon railroad property. The suit was successful and the attorneys were allowed fees derived from benefits conferred upon all creditors as well as from their own clients.

One commentator, criticizing *Pettus* as "leaping a gulf" and creating an independent right of a lawyer to share in the wealth of a stranger, stated:

> The *Pettus* case totally transformed [the claim of a client for contribution to the litigation costs that he had incurred, as recognized in *Greenough,*] into an independent right of the lawyer, reinforced by lien, to an extra reward so that he might share the wealth of strangers. The lawyer was suddenly thought of as producer of this wealth, though he did nothing more than perform his contract with his own client, and furthermore had been paid by his client in full the sum he had agreed to accept.

Dawson, *supra* note 2, at 1603-04.

The principals of the *Greenough* and *Pettus* cases were extended by the Supreme Court in Sprague v. Ticonic Nat'l Bank, 307 U.S. 161 (1939). In *Sprague,* the Court dealt with a situation in which a prevailing party did *not* purport to sue as a class representative. A trustor brought suit to establish a lien on funds she had deposited in a bank which had become bankrupt. Her successful suit established by stare decisis the rights of fourteen other trusts pertaining to the same bonds. In allowing attorney fees to be awarded out of the proceeds of the bonds, the Supreme Court stressed the trial court's power of equity to act in this situation regardless of litigation formalities.

21. Vincent v. Hughes Air West, Inc., 557 F.2d 759, 769 (9th Cir. 1977). *See also In re* Air Crash Disaster at Florida Everglades, 549 F.2d 1006 (5th Cir. 1977). For a discussion of California law relating to the common fund doctrine, see Quinn v. California, 15 Cal. 3d 162, 539 P.2d 761, 124 Cal. Rptr. 1 (1975), while ostensibly based upon CAL. LAB. CODE § 3856 (1971), laid out the equitable foundation of the doctrine.

C. NINTH CIRCUIT HOLDING

The Ninth Circuit held that the policy change represented by the Regional Solicitor's 1977 opinion, allowing the 333 vacant lots to be directly deeded to the city, was the direct result of "litigation commenced and prosecuted by the [city] attorneys in this case"[22] The court noted that due to the efforts of the city attorneys, other native townsites will receive similar economic benefits; and therefore, attorney's fees could properly be awarded under the common fund doctrine even though the change was accomplished administratively rather than judicially, Despite the facts, that the case ended in a settlement, and that the attorneys represented municipal, not private litigants, the Ninth Circuit felt the common fund doctrine still applied.

In reversing the district court, the Ninth Circuit relied heavily upon *Vincent v. Hughes Air West, Inc.*,[23] in determining that the necessary elements for the common fund doctrine were present.[24] It noted with approval the doctrine's equitable rationale, as expressed in *Vincent,* that those who share the benefit should share the cost.[25] While *Vincent* indicated fees could be awarded

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22. 585 F.2d at 430.

23. 557 F.2d 759 (9th Cir. 1977).

24. The *Vincent* court listed the following elements:

> (1) the original client's attorney's fees were not shifted to—or the attorney's personal claim for an extra fee was not lodged against—the adversary losing party; rather, fees were shifted to third parties who were beneficiaries of the fund in some way;
> (2) no contractual relationship existed between the original attorneys and the third parties;
> (3) the beneficiaries were required to pay litigation costs in proportion to the benefits that the litigation produced for them;
> (4) where the third parties had hired their own attorneys and appeared in the litigation, the original claimant could not shift to them his attorney's fees;
> (5) the third parties were not personally liable for the litigation costs and any claim was to be satisfied out of the fund;
> (6) there must exist some identifiable assets on which a court could impose a charge, although the concept of "fund" was flexible and it was settled that a money judgment or even a settlement could serve as a fund; and
> (7) the court could legitimately exercise authority or control over the asset.

Id. at 770. Of importance to the *Vincent* court was the presence of certain factors, specifically that there be a shift of fees to all beneficiaries and that there is an identifiable fund upon which the court can exercise legitimate control.

25. 585 F.2d at 431.

after settlements,[26] the *Klawock* court firmly established rule in the Ninth Circuit[27] allowing an award of attorney's fees in such situations. To insist upon total adjudication would result in unnecessary litigation.[28]

The *Klawock* court, analogizing to the effect of stare decisis in *Sprague v. Ticonic Nat'l. Bank*,[29] took the next step and held that change in administrative policy justified award of fees when a benefit was clearly bestowed upon others who had not actively sought that change.[30] Fees are to come from the fund established by the attorney's efforts, but "it is not necessary for the beneficiaries to be parties to the proceedings at all."[31] Attorney's fees could, therefore, be awarded from "those lots actually in the trustee's hands at the time of the court's decision."[32]

By allowing attorney's fees in this situation, the Ninth Circuit has *implicitly* allowed those who are eligible to receive fees to include attorneys representing governmental bodies as well as private parties.

D. Discussion

In deciding whether an award of attorney's fees is proper in the Ninth Circuit, the *Klawock* decision maintains that the focus of inquiry shall be on general principles of equity; in other words, has a benefit been conferred due to the efforts of the petitioning attorneys. In support of this reasoning, *Klawock* relies upon *Sprague* and *Vincent*.

In both *Sprague* and *Klawock*, persons or entities had benefited due to the efforts of another party. In neither case did the active party sue as a representative of the non-participating ben-

26. 557 F.2d 759, 771 (9th Cir. 1977).

27. 585 F.2d at 428. *See also In re* Air Crash Disaster at Fla. Everglades, 529 F.2d 1006 (5th Cir. 1977) where that circuit independently concurred with *Vincent* and awarded attorney's fees to lead counsel. *See* text accompanying notes 33 and 34 *supra*.

28. 585 F.2d at 431. *Cf.* Prandini v. National Tea Co., 557 F.2d 1015, 1021 (3d Cir. 1977) (noted with approval the desirability of settlements as opposed to litigation).

29. 307 U.S. 161 (1939). *See* note 20 *supra*.

30. 585 F.2d at 431. The court held that the situation in *Sprague* was precisely on point and, therefore, *Sprague* was controlling. The court notes possible undesirable effects may result from award of attorney's fees in these situations but that, in this case, the effect is carefully limited because recovery is only from lots in the trustee's hands. *Id.*

31. *Id.*

32. *Id.*

eficiaries who received the benefit. While in *Sprague* the nature of the doctrine was set out by Justice Frankfurter regarding award from a fund already in existence, *Klawock* faced the dilemma that there was no fund yet in existence. However, by relying on the broad application of the doctrine in *Vincent*, where the court faced a similar seemingly lack of a fund *Klawock* was able to "discover" such a fund and focus on the nature of the doctrine in awarding fees.

The situation in *Vincent* was somewhat different. In *Vincent*, more than sixty actions were brought against Hughes Air West by the next-of-kin of victims of an air crash. The actions were consolidated and fees were awarded to four law firms which, at the direction of the district court, had comprised a "committee of lead counsel." This committee conducted discovery, pretrial motions and settlement negotiations. Fees were awarded, not from the existing fund, as in *Sprague*, but from a awarded percentage of the negotiated settlements.

The *Vincent* court noted that a crucial element of the common fund doctrine is the existence of a fund. However, applying a broad view, existence of the fund may arise *after* the action as well as prior to it. The focus of *Vincent* is clearly on the equitable nature of the claim. In affirming the district court, *Vincent* stated that the district court clearly "proceeded on concepts of quasi-contract and restitution . . . ."[33] and that lead counsel "engaged in substantial work after their appointment that benefitted all claimants."[34]

While other elements of the doctrine would be considered, it is the purpose of the doctrine which is to prevail.[35] Applying this reasoning, the *Klawock* court announced its rule that fees may be awarded even if litigation has not been fully concluded. Affirming *Vincent*, it firmly established that fees may be awarded after settlements[36] and that fees may be awarded in

33. 557 F.2d at 770.

34. *Id.* at 772.

35. *Id.*

36. *See* Kahan v. Rosenstiel, 424 F.2d 161, (3d Cir.), *cert. denied sub nom.* Glen Alden Corp. v. Kahan, 398 U.S. 950 (1970), where the court held that in order to recover legal fees, it is not necessary that suit be brought to a successful completion, since such a requirement might discourage prompt settlements. The court maintained that it is only necessary to determine that the suit was meritorious and that plaintiff's efforts resulted in benefit to others. In Kaufman v. Shoenberg, 33 Del. Ch. 282, 92 A.2d 295 (1952), the

cases which result in purely administrative decisions.[37] This holding is clearly consistent with the underlying rationale of the doctrine. If one party's efforts have created a benefit for others, the principles of unjust enrichment dictate that the non-participating party should not receive that benefit at the expense of the active party. The focus is on avoidance of unjust enrichment, not on maintenance of legal formlaities. Therefore, the type of proceeding in which the change occurred should not determine the line between granting and not granting fees.[38]

The class of persons who could recover has been expanded from *private* parties acting as their own attorneys, to attorneys for private parties whose actions resulted in benefits to *others* and, now, to attorneys who represent public bodies. Given the underlying rationale of the doctrine, there is no reason not to award attorneys' fees to such plaintiffs. In *Lafferty v. Humphrey*[39] the attorneys for Clackamas County, Oregon successfully sued to have certain land grant funds distributed to several counties. The District of Columbia Circuit held that the attorneys for the County of Clackamas were entitled to recover fees regardless of the fact that they represented government entities. The factual situation and reasoning in *Lafferty* is sufficiently similar to hold that municipalities may recover reasona-

plaintiff stockholder was awarded reasonable investigation fees, including attorney's fees. The court stressed the same benefit was accrued whether it was produced as a result of the demand or by successful litigation.

37. This is not to be confused with situations in which fees are awarded by a particular administrative agency. This practice has generally been denied to such bodies, absent statutory authority. *See* Greene County Planning Bd. v. Federal Power Comm'n 559 F.2d 1227 (2d Cir. 1976), *rev'd en banc,* 559 F.2d 1237 (2d Cir. 1977), *cert. denied,* 434 U.S. 1086 (1978), which held that absent statutory authority, the Federal Power Commission had no *inherent* authority to award costs. *See also* Turner v. FCC, 514 F.2d 1354 (D.C. Cir. 1975).

But see Comment, *Funding Public Participation in Agency Proceedings,* 27 AMER. U.L. REV. 981 (1978), noting support given by the Comptroller General of the United States that federal agencies have inherent statutory authority to reimburse public participants. *See also* Comment, *Inducement of Public Participation in Administrative Proceedings Through the Award of Attorney's Fees,* 30 BAYLOR L. REV. 785 (1978).

38. In D'Amico v. Board of Medical Examiners, 11 Cal. 3d 1, 520 P.2d 10, 112 Cal. Rptr. 786 (1974), the California Supreme Court, while denying award of fees, acknowledged the existence of the substantial benefit theory as an exception to the American Rule. *See also* Mandel v. Hodge, 54 Cal. App. 3d 596, 127 Cal. Rptr. 244 (1976), permitting award of fees under a substantial benefit theory in a state employee's successful suit against his employer.

39. 248 F.2d 82 (D.C. Cir.), *cert. denied,* 355 U.S. 869 (1957). *See also* National Ass'n of Regional Medical Programs, Inc. v. Weinberger, 396 F. Supp. 842 (D.D.C. 1975).

ble attorney's fees under the common fund doctrine. This is logical since municipalities have the capacity to sue and be sued,[40] and therefore possess the "usual incidents of suits in relation to the payments of costs and allowances."[41]

E. CONCLUSION

The *Klawock* court reaffirmed the viability of the common fund doctrine in the Ninth Circuit. The decision has also extended the situations in which recovery can be made and the classes of persons who may be entitled to such recovery. This is a clear indication to the practitioner that courts in this circuit will favorably[42] consider claims for fees by attorneys whose work may have benefited persons other than their own clients.

Edmund Scott

V. THE STANDARD OF LIABILITY OF AN ACCOUNTANT UNDER THE FEDERAL SECURITIES LAW IN AN SEC INJUNCTIVE ACTION

In *Securities and Exchange Commission v. Arthur Young & Co.*,[1] the Ninth Circuit Court of Appeals refused to apply the Securities and Exchange Commission's (SEC or the Commission) proposed standard for evaluating the conduct of accountants. The Commission urged the acceptance of a standard whereby accountants would be liable for violation of the federal securities law if their audit, as reflected in financial statements, failed to present a reasonably accurate picture of present and future risks that would face the potential ordinary investor.[2]

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40. *See* 6 J. MOORE'S FEDERAL PRACTICE, ¶¶ 17.23, 54.75(5) (2d ed. 1976). In East Peoria v. Tazewell County, 60 Ill.2d 263, 327 N.E.2d 331 (1975), two municipalities and two school districts filed a declaratory judgment action challenging the constitutionality of a county ordinance imposing a service charge on all municipal corporations over tax assessing, billing, etc. The lower court held the ordinance unconstitutional but denied award of fees. On appeal, it was held that plaintiff's attorneys successfully prevented the unlawful diversion of funds and that they were entitled to an allowance of fees.

41. Reconstruction Fin. Corp. v. J.G. Menihan Corp., 312 U.S. 81, 85 (1941).

42. *See* Reiser v. Del Monte, 605 F.2d 1135 (9th Cir. Oct. 4, 1979), in which the court recognized the common benefit doctrine for attorney's fees award in a class action derivative suit where the attorneys had not sued as a representative of a class.

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1. 590 F.2d 785 (9th Cir. Feb., 1979) (per Sneed, J.; the other panel members were Choy, J., and Waters, D. J.).

2. *Id.* at 787.

The Arthur Young accounting firm (Arthur Young) was named as a party defendant in a trial court action due to its association with its client, Jack Burke. During the 1960's, Burke formed investment programs, and promoted and sold interests in these programs as a means to finance exploration for oil and gas.[3] The accounting firm was hired in 1966 to audit the programs and certify their financial statements.[4] The firm continued in its capacity as auditor for the various investment programs for about five years.

The Commission alleged that the Arthur Young accounting examination, a necessary prerequisite to the firm's certification of financial statements, was faulty.[5] The claimed defect concerned an "inadequate audit" of Fundamental, a Burke-controlled corporation that was integrally connected to the investment programs.[6] The Commission further contended that Arthur Young knew or should have known of "improper practices" and material misstatements and omissions by Burke in connection with the investment programs he promoted.[7] There-

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3. Sec. & Exch. Comm'n v. Geotek, 426 F. Supp. 715, 722 (N.D. Cal. 1976). Burke formed the JB and Geotek investment programs.

4. *Id.* at 729.

5. *Id.* at 730-31. An extensive accounting examination was undertaken. Following this examination, Arthur Young certified the financial statements. The certifications stated that: 1) Arthur Young examined the programs' receipts and disbursements in accordance with generally accepted auditing standards (GAAS); 2) the examination included the necessary tests and procedures prescribed under those standards; and 3) in their opinion, there was a fair presentation according to generally accepted accounting principles (GAAP). *Id.* at 730.

The GAAS and GAAP standards are promulgated by the American Institute of Certified Public Accountants. *Id.* at 730 n.10. For a discussion of these standards, *see* Strother, *The Establishment of Generally Accepted Accounting Principles and Generally Accepted Auditing Standards*, 28 VAND. L. REV. 201 (1975).

6. 426 F. Supp. at 731. The funds of all the programs were channeled through Fundamental. The Commission stated that Fundamental was engaging in Geotek program activities which were inconsistent with its role as represented in the prospectus. The Commission's position was that Arthur Young knew or should have known that Burke did not disclose the significance of the role played by Fundamental. Specifically, the Commission alleged that Burke misstated:

> i) that Fundamental was acting as "operator" for the Geotek programs,
> ii) that Fundamental was holding legal title to the Geotek program properties,
> iii) that Fundamental was receiving and holding "advance" disbursements . . .,
> iv) that Fundamental was pledging program properties as collateral for bank loans.

Id. at 732.

7. *Id.* at 730. The Commission alleged in their brief that Arthur Young knew of the

fore, according to the Commission, Arthur Young misstated in the audit report certifications that it complied with generally accepted accounting principles and generally accepted auditing standards.[8] This misstatement, as well as the "inadequate audit," constituted a violation of the federal securities laws.[9]

The trial court found that Arthur Young neither violated the securities laws nor aided and abetted violation of those laws,[10] thus denying the remedy of an injunction against future viola-

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following "improper practices":

> 1. Burke backdated checks to mislead investors as to tax deductions.
> 2. Burke commingled money and property of the programs with his own.
> 3. Burke sold property he knew was worthless to the programs.
> 4. Burke failed to disclose management expenses.

Brief for Appellee at 6, Sec. & Exch. Comm'n v. Geotek, 426 F. Supp. 715 (N.D. Cal. 1976).

8. 426 F. Supp. at 730. *See* note 5 *supra*.

9. 590 F.2d at 786. Specifically, Arthur Young was charged with violating sections 17(a), 10(b), 15(d), and 13(a) of the Securities and Exchange Act and rule 10b-5, promulgated under section 10(b) of the Act.

Section 17(a) of the Securities Exchange Act of 1933, 15 U.S.C. § 77q(a) (1978), applies to the offer or sale of securities and makes it unlawful

> (1) to employ any device, scheme, or artifice to defraud, or
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact . . . or
> (3) to engage in any transaction, practice or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(1978), makes it unlawful

> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for protection of investors.

Rule 10b-5, promulgated under 10(b), 17 C.F.R. § 240.10b-5(1979), makes it unlawful to omit or misstate a material fact "in connection with the purchase or sale of any security."

Section 13(a), 15 U.S.C. § 78m(a)(1978), requires an issuer of a registered security to file information and documents as the Commission prescribes, which may include the filing of reports certified by independent public accountants.

Section 15(d), 15 U.S.C. § 78o(d)(1978), concerns the filing of registration statements and supplemental reports in accordance with rules and regulations the Commission may prescribe.

10. 426 F. Supp. at 730.

tions which the Commission sought.[11] The Ninth Circuit affirmed, stating that the trial court did not abuse its discretion by refusing to enjoin the defendants.[12] The court based its affirmance on the ground that the trial court's failure to adopt the Commission's standard, whereby the audit statements must reflect the present and future risks of investment, did not constitute error.[13]

A. The Court's Analysis

The Ninth Circuit dealt primarily with the appropriate legal standard against which to measure the performance of an auditor under the federal securities laws. If the trial court imposed too low a standard, then failure to enjoin the defendants *might* have been an abuse of discretion. However, the appellate court emphasized that even if there was a past violation of the securities laws, this factor alone did not mean that an injunction must follow.[14] In order for the Commission to prevail on appeal, the court stated, the Commission must show "no reasonable basis for the district judge's decision."[15]

The court assumed that a finding of mere negligence, rather than scienter, could justify the issuance of an injunction.[16] The issue thus presented on appeal was whether the trial court applied too low a standard in evaluating the accountants' conduct to determine if they negligently violated the securities laws.[17]

The court noted that it was not exactly clear what standard the trial court applied when it concluded that Arthur Young was not negligent.[18] However, it was clear that the lower court did not

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11. *Id.* at 731.

12. 590 F.2d at 789.

13. *Id.*

14. *Id.* An injunction is appropriate when there is a reasonable likelihood of future violation. In Sec. & Exch. Comm'n v. Bausch & Lomb, Inc., 565 F.2d 8 (2d Cir. 1977), although the defendant violated the securities laws, the Second Circuit found he was unlikely to repeat the violation and upheld the trial judge's denial of injunctive relief. *Id.* at 18.

15. 590 F.2d at 787.

16. *Id.* In Ernst v. Hochfelder, 425 U.S. 185 (1976), the Supreme Court held that scienter was necessary for liability to be imposed in a private action for damages under § 10(b) of the securities laws. The Court left open the question of whether scienter is necessary in an injunctive action.

17. 590 F.2d at 787.

18. *Id.* at 788. The evidence at trial included expert testimony that Arthur Young complied with professional standards (GAAS and GAAP). Basically, the Commission's position was, that Arthur Young should have done something more than it did. 426 F.

use the standard suggested by the Commission during oral argument,[19] which is described as follows:

> [W]hether the accountant performed his audit function in a manner that would have revealed to an ordinary prudent investor, who examined the accountant's audits or other financial statements, a reasonably accurate reflection of the financial risks such an investor presently bears or might bear in the future if he invested in the audited endeavor.[20]

The Ninth Circuit found this statement too demanding. To accept such a standard, the court stated, would push an accountant toward guaranteeing the honesty of his client.[21] The court recognized that this standard appealed to the Commission because it would enable them, with the help of accountants, to detect fraud earlier, stop the fraud, and then "bag the game."[22] However, the court concluded that attractive as the standard may seem to the Commission, the standard must be rejected since Congress never enacted a law to draft accountants into service as "[a]n enforcement arm of the SEC."[23]

The court stated that a lower standard for determining liability, proposed by Arthur Young, was sufficient under the circumstances of this case.[24] This standard was good faith compliance with generally accepted auditing standards.[25] The court found

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Supp. at 759. The trial court, relying on the expert testimony, found that either "more" was not required under GAAS or GAAP, or, at most as to one allegation, the expert testimony was evenly balanced that Arthur Young did all that was professionally required. *Id.* at 742.

19. 590 F.2d at 788.

20. *Id.* at 787-88.

21. *Id.* at 788. Recently, the SEC has issued several releases in their efforts to gain tighter control over oil and gas programs, thereby suggesting to the court that had the Commission promulgated more explicit requirements earlier, this would have remedied many of the Commission's concerns in the present case. *Id.* at 788 n.3, discussing and *citing* Releases Nos. 33-6006, 33-6007, 33-6008, 43 Fed. Reg. 60404, 60413, 60418 (1978).

22. *Id.* at 788. The court stated that presently, the Commission is hampered because it can only act after a securities violation; whereas if they were there earlier they could see the fraud and stop it. But, according to the Commission's viewpoint, since they cannot be there earlier and accountants are there, the accountants should take on the Commission's role.

23. *Id.* "The difficulty with this is that Congress has not enacted the conscription bill that the SEC seeks to have us fashion and fix as an interpretive gloss on existing securities laws." *Id.*

24. *Id.*

25. *Id.* The court concluded that the findings of fact demonstrated Arthur Young's good faith compliance with professional auditing standards.

support in *Securities and Exchange Commission v. Republic National Life Insurance Co.*[26] In that case, the court noted that an accountant's only duty is to act honestly, with good faith, and use due care. If fraud is alleged, it must be "pleaded with particularity."[27]

The Ninth Circuit also found that *United States v. Simon*[28] was not applicable to the facts of this case. In *Simon,* the Second Circuit found an accountant liable under the securities laws, although he complied with generally accepted accounting principles. This was based on a finding that the accountant consciously chose not to disclose facts that he knew were material on a financial statement.[29] The Ninth Circuit distinguished the present case from *Simon* since the facts of *Arthur Young* did not indicate deliberate concealment by the accountants.[30]

The court reasoned that denial of an injunction was proper, given that the lower court did not err when it refused to apply the Commission's standard and since the findings of fact were not clearly erroneous.[31] Even if the trial court erred in concluding that the defendants did not negligently violate the securites laws, the appellate court stated that it would uphold the judge's exercise of discretion in deciding not to enjoin Arthur Young.[32] This was based on the fact that the lower court could still have found no reasonable likelihood of future violation, in which case an injunction would not have been an appropriate remedy.

B. SIGNIFICANCE

The Ninth Circuit, in *Securities and Exchange Commission v. Arthur Young,* makes it clear that the Commission's proposed standard for evaluating an accountant's performance under the federal securities laws was too high. The court's language emphasizes its disapproval of what it views as the Commission's attempt to use the court to enlist an auditor into service as an active

26. 378 F. Supp. 430 (S.D.N.Y. 1974).

27. *Id.* at 440.

28. 425 F.2d 796 (2d Cir. 1969), *cert. denied,* 397 U.S. 1006 (1970).

29. *Id.* at 809.

30. 590 F.2d at 789.

31. *Id.*

32. *Id.* The court was careful to point out that it made no finding that Arthur Young violated the securities laws.

enforcer of the securities laws.[33] Yet the court did not clearly establish an alternative standard upon which accountants can rely. Instead, the court limited itself to stating that good faith compliance with generally accepted auditing standards was sufficient in this case.[34]

Accountants would prefer the courts to define the standard as good faith compliance with generally accepted auditing standards without qualification, and then to hold that compliance with this standard precludes liability.[35] The *Arthur Young* court, by narrowing its finding to the circumstances of this case, in effect refused to set good faith compliance with a generally accepted auditing standard as the standard for accountants under the federal securities law.[36] Other courts have also been reluctant to adopt such a standard,[37] due in part to a fear that a profession allowed to set its own standards on which to base legal liability will inevitably be influenced by motives inconsistent with the securities law, enacted to protect the public interest.[38]

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33. *Id.* at 788. "To accept the SEC's position would go far toward making the accountant both the insurer of his client's honesty and an enforcement arm of the SEC." *Id.* Also, the court states in reference to the Commission, "[w]hat it cannot do, the thought goes, the accountant can and should." *Id.* The court then faults the Commission for trying to get the court to put an "interpretive gloss" on the securities laws. *Id.*

34. *Id.* The court concluded that "under the circumstances of this case" the trial court "did not err as a matter of law" in the standard it chose to evaluate Arthur Young's conduct. *Id.* at 787. Yet the court never directly states what standard the trial court used, other than to say it was not the SEC standard. The Ninth Circuit simply looked at the facts of the case and concluded that Arthur Young's compliance with GAAS in good faith was sufficient to discharge its obligations.

35. *See* Metzger & Heintz, *Hochfelder's Progeny: Implications for the Auditor*, 63 MINN. L. REV. 79, 113 (1978). *See also* Earle, *The Fairness Myth*, 28 VAND. L. REV. 147 (1975).

36. 590 F.2d at 787. The court repeatedly uses limiting language such as "under the circumstances of this case," or, "[b]ecause the only sanction sought to be imposed on AY [Arthur Young] and its auditors was an injunction . . . ." *Id.*

37. *See, e.g.*, Herzfeld v. Laventhol, Krekstein, Horwaith & Horwaith, 540 F.2d 27 (2d Cir. 1976) (duty of accountants beyond complying with GAAP to report fairly to the public); United States v. Simon, 425 F.2d 796 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970) (refusal of judge in a criminal trial to give jury instruction that the defendant will only be guilty for willful departure from GAAP).

38. Commentators have noted that the courts are not receptive to such a standard because it will be influenced by "the profession's natural tendency toward self-protection." Metzger & Heintz, *supra* note 35, at 113. *See also* Briloff, *We Often Paint Fakes*, 28 VAND. L. REV. 165 (1975), in which the author criticizes accounting professional organizations for failure to adequately police and censure its own members. He perceives the American Institute of Certified Public Accounts who set professional standards as being preoccupied with "projecting the profession's image, thereby protecting its economic interests. . . ." *Id.* at 195.

As a result, compliance with professional auditing standards is more of a threshhold test than an absolute guarantee of finding no liability. An accountant who fails to meet this threshhold test will most likely be held liable.[39] An accountant who does meet this threshhold test is, of course, in a better position, but may still be liable under the securities laws.[40]

What more is required of accountants than compliance with professional standards is an issue not directly dealt with by the *Arthur Young* court. The court does stress that the Arthur Young firm acted in good faith when it complied with the auditing standards, yet the panel never defines good faith.[41] Perhaps an accountant who lacked good faith but met professional standards would be liable in the Ninth Circuit. The *Arthur Young* court delineated one circumstance where even good faith compliance with professional auditing standards might be insufficient: when an accountant deliberately conceals a known material fact, or suspects fraud but looks the other way.[42] Other circumstances, where good faith compliance with professional auditing standards might not be enough, are not addressed by the *Arthur Young* court.[43] The opinion only gives one a sense of the outer perimeters of what constitutes an acceptable or unacceptable standard for

39. *See, e.g.*, McLean v. Alexander, 420 F. Supp. 1057 (D. Del. 1976); Escott v. Barchris Constr. Corp., 283 F. Supp. 643 (S.D.N.Y. 1968).

40. *See* United States v. Simon, 425 F.2d 796 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970) where compliance with GAAP did not insulate the defendant from criminal liability.

41. 590 F.2d at 788. In the United States v. Simon, 425 F.2d 796 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970), the test involved in determining criminal liability of an accountant included "good faith." If the financial statement did not fairly present the financial position of the firm, "the basic issue became whether the defendants acted in good faith." *Id.* at 805. The court said compliance with professional standards was persuasive evidence, but *not* determinative of the good faith issue. Good faith was a jury question of whether an honest judgment had been made when the accountants failed to reveal on the financial statement known looting by a corporate officer.

42. 590 F.2d at 789.

43. One such circumstance might be when a particular standard is shown to be unreasonable. This parallels general negligence law, where following customary practices will not insulate the defendant from a finding of negligence if the custom is shown to be unreasonable. *See* Morris, *Custom and Negligence*, 42 COLUM. L. REV. 1147 (1942).

Another circumstance considered by several courts is whether the financial statement fails to fairly present the financial position of the audited firm. *See, e.g.*, Herzfeld v. Laventhol, Krekstein, Horwaith & Horwaith, 540 F.2d 27 (2d Cir. 1976); United States v. Simon, 425 F.2d 796 (2d Cir. 1969), *cert. denied*, 397 U.S. 1006 (1970). *See also* Metzger & Heintz, *supra* note 35, at 113, where the authors state: "Liability will hinge, however, upon whether the statement 'fairly presents' the financial position of the audited firm, and not upon whether there is compliance with GAAP and GAAS."

accountants under the securities laws. How much more than good faith compliance with professional standards is necessary or how much less than showing present and future risks will suffice are questions that remain unanswered by the *Arthur Young* court.

Arthur Young further indicates the Ninth Circuit's choice not to join the negligence - scienter debate.[44] Rather, it will *assume* negligence is the degree of culpability required in an injunctive action. Therefore, the plaintiff need not allege scienter as part of the prima facie case.[45] However, if fraud is alleged, it will have to be alleged "with particularity."[46] This requirement is based on fairness to the defendant.[47]

The opinion reaffirms the Ninth Circuit's position as to when

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44. Since Ernst v. Hochfelder, 425 U.S. 185 (1976), the question of whether a finding of scienter is necessary for an injunction under the securities laws has been a much debated issue. The circuits are split in their conclusions. In Securities & Exch. Comm'n v. World Radio Mission, Inc., 544 F.2d 535 (1st Cir. 1976), the court held that negligence was sufficient for injunctive relief under §§ 17(a) and 10(b) and rule 10b-5. *Id.* at 540-41; *see* note 9 *supra*. The Second Circuit also appeared to use a negligence standard for a § 5 (of the 1933 Act) violation, in Securities & Exch. Comm'n v. Universal Major Indus. Corp., 546 F.2d 1044, 1047 (2d Cir. 1976), though in a later Second Circuit opinion, the court treated the issue as yet unresolved and found it unnecessary to decide the issue, Securities & Exch. Comm'n v. Commonwealth Chem. Sec., Inc., 574 F.2d 90, 102 (2d Cir. 1978). In the Fourth Circuit, a district court found that scienter was necessary for injunctive relief under § 17(a) of the Securities Act of 1933 in Securities & Exch. Comm'n v. American Realty Trust, 429 F. Supp. 1148, 1171 (E.D. Va. 1977). Prior to *Ernst,* the Sixth Circuit required more than negligence for an injunction in Securities & Exch. Comm'n v. Coffrey, 493 F.2d 1304, 1314 (6th Cir. 1974), *cert. denied,* 420 U.S. 908 (1975).

For a discussion of this issue and the position of different circuits, *see* Notes and Comments, *SEC Enforcement Actions to Enjoin Violations of Section 10(b) and Rule 10b-5: The Scienter Question,* 5 HOFSTRA L. REV. 831 (1977); Note, *The Scienter Requirement in SEC Injunctive Enforcement of Section 10(b) after* Ernst v. Hochfelder, 77 COLUM. L. REV. 419 (1977); Case Comments, *Scienter and SEC Injunction Suits,* 90 HARV. L. REV. 1018 (1975); Comment, *Injunctive Relief in SEC Civil Actions: The Scope of Judicial Discretion,* 10 COLUM. J.L. & SOC. PROB. 328 (1974).

45. The trial court indicated that had scienter been necessary, the action against Arthur Young would have been dismissed. 426 F. Supp. at 730. Since the action was brought under both §§ 10(b) and 17(a), *see* note 9 *supra*, it is not entirely clear whether scienter might be a necessary element if an injunctive action was brought under just one of those sections. However, it appears that the Ninth Circuit would probably assume negligence was sufficient if the action was brought under either § 10(b) or § 17(a), 15 U.S.C. §§ 78j, 77q(a)(1978).

46. Sec. & Exch. Comm'n v. Republic Nat'l Life Ins. Co., 378 F. Supp. 430, 440 (S.D.N.Y. 1974).

47. In Rich v. Touche Ross & Co., 68 F.R.D. 243 (1975), the court stated the "particularity requirement" is necessary to shield defendants from lightly made claims, especially when one's professional reputation can easily be damaged. Also, the court recognized that the defendant needs specific information to adequately prepare a defense. *Id.* at 245.

an injunction is an appropriate remedy under the federal securities laws. While a past violation continues to be probative, it is not the only criteria the court will examine; evidence of a reasonable likelihood of future violation by the defendant is necessary for injunctive relief.[48]

C. Conclusion

Arthur Young is part of a growing trend of accountants litigating claims brought against them by the SEC, rather than simply entering into consent decrees.[49] The decision demonstrates that an action to enjoin accountants can be successfully defended in the courts. It further shows the heavy burden the Commission must overcome to reverse a lower court's denial of injunctive relief.[50]

Reassurring for accountants is the fact that the Ninth Circuit will not require compliance with a standard under which they must present risks to investors in the present and future. Exactly what is required of auditors for compliance with the federal secur-

48. The Ninth Circuit stated this position in SEC v. Koracorp Indus., Inc., 575 F.2d 692, 701 (9th Cir. 1978). The court concluded that the likelihood of repetition of the wrong was a critical factor and the district court was free to exercise its discretion and deny an injunction if the accountant negligently violated the securities laws. For a treatment of the *Koracorp* case, *see* Note, *Standards for Summary Judgment and Injunctions in Securities Violations*, 9 Golden Gate U.L. Rev. 287 (1979). This is consistent with the position taken by the Second Circuit in Sec. & Exch. Comm'n v. Bausch & Lomb, Inc., 565 F.2d 8 (2d Cir. 1977), where the court concluded that one instance of misconduct did not necessitate the issuance of an injunction when other factors indicated that the defendants "are not likely to need the prophylactic of an injunction to prevent recidivism." *Id.* at 19.

It is important to examine the appropriateness of an injunction on a case by case basis, for it can have serious consequences. For a discussion of the effects an injunction might have on an accountant, *see* SEC v. American Realty Trust, 429 F. Supp. 1148, 1175-76 (E.D. Va. 1977); Mathews, *Program of the Committee on Fed. Reg. of Sec. SEC Civil Injunctive Actions*, 30 Bus. Law. 1305, 1307-09 (1975); Earle, *Program of the Committee on Fed. Reg. of Sec. SEC Civil Injunctive Actions*, 30 Bus. Law. 1319, 1321-23 (1975).

49. Wall St. J., July 16, 1979, at 1, col. 6. The article points out that more firms are going to court for many reasons, amongst which are the protection of their professional reputations and the courts' increasing refusal to enjoin SEC targets. One commentator, recognizing the growing trend in SEC litigation describes Sec. & Exch. Comm'n v. Republic Nat'l Life Ins. Co., 375 F. Supp. 430 (S.D.N.Y. 1974) as "the first trial *on the merits* of an SEC injunction against a major accounting firm." Earle, *supra* note 48, at 1323 (emphasis added).

50. For a discussion of why the courts should *not* shift from the abuse of discretion standard when the SEC appeals from a denial of an injunction, *see* Comment, *Injunctive Relief in SEC Civil Actions: The Scope of Judicial Discretion*, 10 Colum. J.L. & Soc. Prob. 328, 367 (1974).

ities laws beyond the threshold test of good faith compliance with professional standards remains, however, less clearly defined.[51]

Susan J. Adler

VI. A FINANCIAL COLUMNIST'S LIABILITY UNDER SEC RULE 10b-5

A. INTRODUCTION

In *Zweig v. Hearst Corporation,*[1] the Ninth Circuit Court of Appeals held that in certain circumstances, a financial columnist has a duty to disclose material information.[2] The plaintiffs in *Zweig* alleged that the defendant intentionally used his position as a columnist to inflate the market for a particular stock in violation of rule 10b-5.[3] The court concluded that this defendant's duty to disclose his intent to manipulate the market and reap a

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51. For suggestions of how an auditor can comply with the securities laws, *see* Metzger & Heintz, *supra* note 35, at 116-18. For several viewpoints on this topic, *see generally Symposium on Accountants and the Federal Securities Laws,* 28 VAND. L. REV. 1 (1975).

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1. 594 F.2d 1261 (9th Cir. Apr., 1979) (per Goodwin, J.; Ely, J., dissenting; the other panel member was Solomon, D.J.)

2. *Id.* at 1268.

3. 17 C.F.R. § 240.10b-5 (1978) (hereinafter rule 10b-5). Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) to employ any device, scheme or artifice to defraud,
>
> (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Rule 10b-5 was promulgated under 15 U.S.C. § 78j (1978) (hereinafter § 10(b)), which provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

profit extended to anyone who would foreseeably rely on the market.[4]

The defendant wrote a favorable column about a small company, American Systems, Inc. (ASI), located in Southern California. On June 2, 1969, he purchased ASI stock at a discount[5] from the corporation. His column was published on June 4, 1969 in the *Los Angeles Herald Examiner*. Furthermore, his column was reproduced as a paid advertisement for ASI in a journal in which he had a financial interest. The price of ASI stock rose after publication of defendant's column. On June 5, 1969, the defendant sold a portion of his ASI stock at a profit.[6] The evidence showed that defendant had engaged in "strikingly similar" behavior in the past.[7]

Plaintiffs alleged that the defendant omitted the following facts from his column: (1) defendant invested in ASI stock at a discount before the column was published and intended to sell the stock after publication; (2) defendant had a practice of "scalping" in the past; and (3) defendant's columns were often used as advertisements in his journal.[8] Plaintiffs never actually read defendant's column. Prior to publication of the column, Reading Guidance Center (RGC), a corporation in which plaintiffs each owned one third of the shares, entered into a reorganization agreement with ASI. Under the agreement, ASI was to pay RGC shareholders ASI stock worth $1,800,000 on the market. The market value of the stock, according to their contract, was to be determined by the average closing bid for ASI stock from June 5, 1969 to June 10, 1969.[9]

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4. 594 F.2d at 1269.

5. *Id.* at 1264. The price defendant paid was two dollars per share; the bid price was 3 ⅝. The court did not decide the issue of whether this bargain price constituted receipt of consideration for defendant's column, in violation of 15 U.S.C. § 77q(b) (1978). *Id.* at 1264 n. 5.

6. *Id.* at 1265. Defendant sold 2,000 shares at $5.00 each, thus making a $3.00 profit per share.

7. *Id.* at 1264 n. 4. Defendant had bought stock, wrote a column, and then sold the stock for a profit within five days after publication of the column 21 times within a two year period.

8. *Id.* at 1265.

9. *Id.* This means that the higher the market price of ASI stock during this period, the fewer shares RGC shareholders (the plaintiffs) would receive as part of the reorganization. Since defendant's column was published on June 4, it had great potential to effect the market price of ASI stock during the critical period from June 5 to June 10, assuming readers were influenced by the column to purchase ASI stock.

After an offer of proof by the plaintiffs, the district court concluded that the plaintiffs failed to show a right to relief and granted the defendant's motion to dismiss.[10] The court stated that it found nothing wrong with a columnist's "making a nickel" after recommending a particular stock.[11]

On appeal, the Ninth Circuit panel reversed and remanded,[12] characterizing the lower court's treatment of the defendant's motion to dismiss as a ruling on a motion for summary judgment.[13] The appellate court determined that the defendant was not allowed to prevail as a matter of law, stating:

> We hold that these . . . [federal security laws] also require a financial columnist, in recommending a security that he or she owns, to provide the public with all material information he or she has on that security, including his or her ownership, and any intent he or she may have (a) to score a quick profit on the recommendation, or (b) to allow or encourage the recommendation to be published as an advertisement in his or her own periodical.[14]

B. The Court's Analysis

The court dealt with each element of a cause of action under section 10(b) and rule 10b-5. It stressed the elements of material

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10. 407 F. Supp. 763, 764 (C.D. Cal. 1976). The court granted the motion to dismiss under Fed. R. Civ. P. 41(b), which provides:

> After the plaintiff, in an action tried by the court without a jury, has completed presentation of his evidence, the defendant . . . may move for a dismissal on the ground that upon the facts and the law the plaintiff has shown no right to relief. The court as trier of the facts may then determine them and render judgment against the plaintiff . . . .

11. 594 F.2d at 1271.

12. *Id.* at 1263.

13. *Id.* at 1264. Based on the transcript, the appellate court determined that the parties intended only to test the legal sufficiency of the plaintiff's claim. Therefore, the motion to dismiss functioned as a motion for summary judgment pursuant to Fed. R. Civ. P. 56, which provides:

> (c) The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

Therefore, in keeping with the standard of review on a motion for summary judgment, the court of appeal viewed the facts in the light most favorable to the plaintiffs.

14. 594 F.2d at 1271.

omission and duty to disclose and gave lighter emphasis to the elements of scienter, reliance and causation.

The court of appeals determined that defendant's failure to include in his column the facts of his stock ownership, his journal interest, and his intent to profit, were material omissions. Since these facts could have effected his objectivity, the court concluded that they would be significant to a reasonable investor in evaluating defendant's investment advice and deciding whether or not to follow the column's recommendation to invest in ASI stock.[15] The court emphasized that stock ownership by a newspaper reporter might not be material in all situations.[16] It expressed why it was significant in this instance: "given the column's style and tone, with its glowing praise of ASI and conclusion that the firm was a worthy investment despite its risks, the effect of [defendant's] stock ownership on his objectivity would be important to his readers."[17]

Defendant's Duty to Disclose I: To Readers

The court found defendant's behavior analogous to that of a corporate insider who withholds material information while trading corporate stock.[18] Usually the information withheld by the insider relates directly to the company's value. The court recognized that the information defendant withheld was of a different sort; it related to his motivations and objectivity in recommending purchase of ASI stock. Yet, the court reasoned, this difference in the type of information withheld is not determinative of the duty to disclose.[19] Disclosure of both types of material information is necessary, so that investors will not be misled in making their investment decisions. For this reason, the court concluded that failure to disclose either type of material information while trading in the stock constituted a violation of section 10(b) and rule 10b-5.[20]

15. *Id.* at 1266.

16. *Id.* "[I]f [the column] objectively reported an undisputed fact or news event," stock ownership might not be material.

17. *Id.*

18. *Id.* at 1266. *See, e.g.*, Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228 (2d Cir. 1974); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968) (en banc), *cert. denied*, 394 U.S. 976 (1969).

19. 594 F.2d at 1271. *See* ALI FED. SEC. CODE § 1603, Revised Comment 3(d) (Mar. 1978 Draft), which states that there is no reason to distinguish between the two types of material information.

20. 594 F.2d at 1267.

The court rejected *SEC v. Capital Gains Research Bureau*[21] as controlling in this case. In *Capital Gains*, an investment advisory service engaged in a scheme similar to that of the defendant in *Zweig*. The Supreme Court held that the SEC could get an injunction under the Investment Adviser's Act (the Act), compelling the advisory service's disclosure to subscribers of its practice of profiting on its recommendations.[22] Since the *Zweig* plaintiffs did not show that defendant was an investment adviser, as defined in the Act, the court concluded that the duties imposed on investment advisers under the Act did not pertain to the defendant.[23] However, the court stated its belief that the rule (10(b), 10b-5) and the Investment Advisers Act are complementary so that failure to bring the defendant within the latter was not fatal to the claim under rule 10b-5.[24]

The court relied on *Chasins v. Smith, Barney & Co.*[25] and *Affiliated Ute Citizens of Utah v. United States*[26] in concluding that defendant had a duty to disclose to his readers under rule 10b-5. In *Chasins*, the broker-dealer defendant recommended securities to his client, but failed to inform him of his market-making activities in those securities. The Second Circuit Court of Appeals found the defendant liable under rule 10b-5 for failure to disclose this conflict of interest.[27] While *Chasins* could be read as applicable only in a broker-client context, the court in *Zweig* rejected this reading of the case.[28] It read *Chasins* more broadly,

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21. 375 U.S. 180 (1963).

22. *Id.* at 180. The defendant in *Capital Gains* was liable under the 1940 Investment Advisers Act, 15 U.S.C. § 80b-1 *et seq.* (1970). 15 U.S.C. § 80b-2(a) states:

> "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities; but does not include . . . (D) the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation . . . .

23. 594 F.2d at 1267. The court specifically left open the question whether a columnist such as defendant could ever come within the Investment Advisers Act. *Id.* at 1267 n.10.

24. *Id.* For a discussion of the legislative history of each, *see* Peskind, *Regulation of the Financial Press: A New Dimension to Section 10(b) and Rule 10b-5*, 14 ST. LOUIS U. L. J. 80, 84-88 (1969).

25. 438 F.2d 1167 (2d Cir. 1970).

26. 406 U.S. 128 (1972).

27. 438 F.2d at 1167.

28. 594 F.2d at 1268.

based on the Supreme Court's opinion in *Ute.*[29]

In *Ute,* the bank employee defendants acted as stock transfer agent for a corporation in which plaintiffs were former shareholders. Stock transfer agents usually have no duty to disclose.[30] However, the Supreme Court held that the bank employees assumed this duty because they were active in encouraging a market for the corporation's stock and were in a position to profit from their sales.[31] The *Zweig* court reasoned that the defendant's activities were so similar to the bank employees' activities in *Ute,* that he, too, assumed a duty to disclose under rule 10b-5.[32]

The court found additional support for its conclusion that the defendant had a duty to disclose to his readers his stock ownership, journal interest, and intent to profit, in *White v. Abrams.*[33] In *White,* the court stated five factors which it considered relevant to the scope of the duty to disclose under rule 10b-5.[34] Applying the factors to the defendant in *Zweig,* the court determined that although there was no fiduciary relationship, his duty extended to his readers because (1) defendant was in control of the material information and the only one with access to it; (2) defendant benefitted from his relationship with his readers, in that his employment depended on them; and (3) defendant's column initiated stock transactions by his readers and the resultant rise in the price of ASI stock.[35]

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29. *Id., citing* Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128 (1972).

30. 406 U.S. 128, 152 (1972).

31. *Id.* at 153.

32. 594 F.2d at 1268. "Here, as in Affiliated Ute Citizens, the defendant assumed those duties when, with knowledge of the stock's market and an intent to gain personally, he encouraged purchases of the securities in the market." *Id.*

33. 495 F.2d 724 (9th Cir. 1974).

34. The factors are:

> 1. The relationship of the defendant to the plaintiff;
> 2. Defendant's access to the information as compared to that of the plaintiff;
> 3. Defendant's benefit derived from the relationship;
> 4. Defendant's awareness of whether plaintiff was relying on their relationship in making his or her investment decision; and
> 5. Defendant's activity in initiating the transaction in question.

Id. at 735-36.

35. 594 F.2d at 1269.

Duty to Disclose II: To Nonreaders

The court further analyzed defendant's duty to disclose to determine if it extended to RGC and its shareholders. If the duty did not extend this far, the shareholder plaintiffs could not recover damages from the defendant.[36] The *Zweig* court concluded that defendant's duty to disclose did extend to the plaintiffs. Given that both the plaintiffs and readers were in similar positions, the court reasoned that the plaintiffs' relationship to the defendant was similar to the reader's relationship to him.[37] The similarity of their positions arose from the fact that both the readers and the plaintiffs relied on an "honest" and "fully informed market." Thus, "RGC and the readers had strikingly similar stakes in the processes of the market."[38]

The court discussed RGC's expectation of an honest market when it entered in the reorganization contract with ASI. RGC relied on an honest market when it agreed to accept ASI stock worth $1,800,000, based on the average market price for ASI stock from June 5 to June 10. In an honest market, demand is generated by fully informed investors. However, investors were not fully informed by the column. Assuming investors relied on the column, causing the market to be distorted, the court concluded RGC was forced to deal in a "manipulated market" contrary to RGC's expectations when it entered into the reorganization agreement.[39] The court took this analysis one step further, concluding that it was foreseeable to the defendant that RGC would rely on the market and be effected by any manipulations in that market.[40]

Other Elements: Scienter, Reliance, Causation

Scienter was dealt with briefly by the court, which found that the defendant knew the facts he failed to disclose and, therefore, concluded that there was a triable issue of fact as to defen-

36. *Id.*
37. *Id.*
38. *Id.*
39. *Id.*
40. *Id.* "If . . . [the defendant] was unaware of RGC's reliance on the market, he could have discovered it with minimal effort by asking ASI or RGC about the terms of the merger, or by checking the reorganization agreement . . . ." *Id.* The court demonstrated how the more successful the column was in influencing readers to buy ASI stock, the greater the discrepancy between what ASI stock was worth in a free market as opposed to its worth in a manipulated market.

dant's intent to benefit from his column.[41]

The court dealt summarily with reliance and causation. It applied the *Ute* test of causation, which is satisfied by a showing of materiality in an action based on nondisclosure.[42] Since the court previously determined that the omission was material, it concluded that on remand, the lower court should presume ASI stock was purchased in reliance on the column.[43]

Though plaintiffs never read the column, the court found this did not defeat liability under section 10b and rule 10b-5. The court reasoned that since RGC did rely on the natural processes of the market, and the market included defendant's reader who relied on full disclosure, this would suffice to establish liability.[44] The dissenting opinion, however, rejected this analysis. It reasoned that since the merger agreement took place months before publication of the column, there was clear evidence of nonreliance.[45]

Fairness and the Policy Behind the Federal Securities Laws

The *Zweig* court expressed its belief that imposing liability, given the circumstances of this case, is within the "spirit" of the federal securities laws.[46] It stated that these laws aim to protect investors and the public from abuses effecting the market and foster the expectation that the market is free from manipulation.[47] Therefore, the court concluded, to deny plaintiffs, who relied on an honest market, a cause of action under rule 10b-5 would be contrary to the policy behind the federal security laws.[48]

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41. *Id.* at 1271. *See also* Ross v. A.H. Robins Co., Inc., 607 F.2d 545, 555-56 (2d Cir. 1979).

42. 406 U.S. 128 (1972). The Supreme Court concluded that the appellate court erred when it held that the plaintiffs could not recover unless the evidence showed reliance. *Id.* at 152. "Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material . . . ." *Id.* at 153.

43. 594 F.2d at 1271.

44. *Id.* at 1271. "We hold that these two legitimate expectations constitute sufficient reliance to establish liability in this case." *Id.*

45. *Id.* at 1272 (Ely, J., dissenting). Circuit Judge Ely concluded that nonreliance by the plaintiff defeated any implication of reliance. Also, he viewed the fact that the agreement predated the column as fatal to the "in connection with" requirement of rule 10b-5. Therefore, he concluded the defendant was not liable.

46. *Id.* at 1270.

47. *Id.* at 1270 n. 16.

48. *Id.* at 1270. *See* note 68 *infra* and accompanying text.

In addition, the court focused on the fairness of imposing liability when a financial columnist uses his position to manipulate the market and profit by it, stating:

> As we have illustrated, to extend the obligation of disclosure to the readers but to bar RGC from recovery under the rubrics of reliance or duty would lead to a wholly incongruous result: the more effective [defendant] was in elevating the price of the stock for his own benefit, the greater the losses an innocent third party [RGC] would have to absorb.[49]

C. Analysis of the Court's Reasoning

The Ninth Circuit's holding in *Zweig v. Hearst Corporation* is noteworthy because it extends a duty to disclose material information under section 10(b) and rule 10b-5 to a nontraditional defendant, a financial columnist. Though the defendant in *Zweig* had access to material information, he was clearly not an insider.[50] Nor was his information the result of a tip.[51] Furthermore, the defendant was not in any sort of special relationship with the plaintiff.[52] In the absence of insider or tippee status, or a special

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49. *Id.* at 1270-71.

50. *See* 2 A. Bromberg, Securities Law: Fraud SEC Rule 10b-5 § 7.46(b) (1969). The author isolates "access" as the crucial criterion in determining who is an insider. "This means something more than possession of the information, but how much more is not yet clear. Probably it means possession intended to fit a corporate purpose (of the company to which the information relates)." *Id.* at 180. Furthermore,

> Analytically, the obligation [of insiders] (to disclose) rests on two principle elements; first, the existence of a relationship giving access, directly or indirectly to information intended . . . for a corporate purpose and not for the personal benefit of anyone, and second, the inherent unfairness involved where a party takes advantage of such information knowing it is unavailable to those with whom he is dealing.

Id. at 179, *citing* Cady, Roberts & Co., 40 S.E.C. 907, 912 (1961).

In plaintiff's brief, the plaintiff referred to the defendant as an insider. Brief for Appellee at 66, Zweig v. Hearst Corp., 594 F.2d 1261 (9th Cir. 1979). However, the Court never accepted this characterization. *Cf.* ALI Fed. Sec. Code § 1603, Revised Comment 3(d) (Mar. 1978 Draft) (suggesting a new category of "quasi-insider," for one who has information that will affect the market, such as a financial columnist).

51. A tippee is one who receives material inside information from an insider and acts on this information without disclosing it to the public. One who receives information as a result of a tip is under a duty to disclose or abstain from trading; this duty is based on the same rationale as the duty of an insider. Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228, 236-37 (2d Cir. 1974).

52. *See* Peskind, *supra* note 24, at 90, where the author states: "[T]here is no judicial authority holding that the financial press owes a fiduciary duty to a potentially unlimited class of investors."

relationship between the parties, courts are often reluctant to extend an affirmative duty to disclose material information,[53] perhaps for fear of the potentially limitless thrust of section 10(b) and rule 10b-5.

However, the extension of an affirmative duty to disclose to a financial columnist seems reasonable owing to the special relationship to the market, and the ability to influence that market,[54] created by that position. It is also a practical extension of the duty to disclose because a columnist's duty is only activated in certain limited situations, which reduces the prospect of endless liability under section 10(b) and rule 10b-5.

According to the court, one will only assume this duty if he or she has knowledge of the market and an intention to gain personally.[55] An individual possessing these characteristics will then only be liable if he or she actively encourages purchase of stock on that market.[56] A further possible restriction on the potential class of plaintiffs that the defendant owes a duty to is that the plaintiff's conduct be reasonably foreseeable.[57]

Applying these factors to the defendant in *Zweig*, it seems fairly straightforward to conclude that he did owe a duty to disclose to readers of his column. It seems fair to hold the defendant liable to the plaintiffs, since they absorbed the damages he would have had to pay readers. But fairness alone is not enough; the

53. For a discussion of an affirmative duty to disclose, *see* United States v. Chiarella, 588 F.2d 1358, 1373 (2d Cir. 1978) (Meskill, J., dissenting).

54. *See* SEC REPORT OF THE SECURITIES MARKETS, H.R. Doc. No. 95, 88th Cong., 1st Sess. 70-78 (1963) where the SEC found that the potential impact of financial news on the securities market is great. *See also* Note, *Stock Scalping by the Investment Advisor: Fraud or Legitimate Business Practice?*, 51 CAL. L. REV. 232, 233-35 (1963) (emphasizing that if a particular stock has a thin market, even a small increase in demand may significantly influence price).

55. 594 F.2d at 1268.

56. *Id.*

57. *Id.* at 1269. From the *Zweig* decision, it is not clear whether "foreseeability" is an essential requirement. The *Zweig* court concluded that the plaintiffs were foreseeable, but this seems debatable. It might be a heavy burden to a columnist who writes several columns a week to investigate those columns. The *Zweig* court imposed this duty to investigate when it noted the defendant could have easily discovered the terms of the merger. Perhaps the court suspected that the defendant really did know the terms of the upcoming reorganization. However, it does seem fair to impose a duty to investigate when one with knowledge of the market manipulates it with the intent to gain. *See In Re* Republic Nat'l Life Ins. Co. and Reality Equities Corp., 387 F. Supp. 902 (S.D.N.Y. 1975) (defendant who engaged in statistical reporting and expressed as his opinion a recommendation of a security, had no duty to investigate the truth of what was published).

court must also find that the defendant owed a duty to the plaintiffs to establish liability under section 10(b) and rule 10b-5.[58]

While the court applied the *White* flexible duty factors and concluded that the defendant owed a duty to his readers,[59] it never applied the *White* factors in analyzing whether the defendant owed a duty to the non-reader plaintiffs. If the *White* factors were applied, it is questionable whether the defendant owed a duty to the plaintiffs.[60] However, application of these factors makes more sense where a duty is owed to a special personal relationship, rather than in a "special relationship to the market" situation, as in *Zweig*.

The court's application of *Ute* to the facts in *Zweig* forms a stronger basis for its conclusion that the defendant owed a duty to disclose to the plaintiffs. The defendants in each case were normally under no duty to disclose; yet each assumed this duty because of his conduct. However, the *Zweig* court took the *Ute* holding one step further: in *Ute,* the defendant bank employees assumed affirmative obligations to disclose to parties they knew were relying on them as transfer agents;[61] in contrast, in *Zweig,* there was no question of reliance on the defendant by the plaintiffs.

The *Zweig* dissent correctly points out that it would have been impossible for reliance on the defendant's column to induce the plaintiffs behavior since the reorganization agreement was made in February, while the column was released in June.[62] However, the timing of the manipulation and the plaintiffs purchase

58. 594 F.2d at 1269. For other cases that discuss a duty to disclose, *see* Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128 (1972); United States v. Chiarella, 588 F.2d 1358 (2d Cir. 1978); Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228 (2d Cir. 1974); Chasins v. Smith, Barney & Co., 438 F.2d 1167 (2d Cir. 1970); Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787 (2d Cir. 1969); Tucker v. Arthur Anderson & Co., 67 F.R.D. 468 (S.D.N.Y. 1975).

59. *See* note 34 *supra.*

60. There was no relationship between the plaintiffs and defendant, the defendant derived no benefit from the relationship, the defendant could not have been aware that the plaintiffs would rely on the relationship (since it was impossible for them to rely), and the defendant did not initiate the transaction in question. This suggests a very weak duty, if a duty existed at all.

61. 406 U.S. 128, 153-54. The *Ute* Court stated: "The mixed blood sellers 'considered these defendants to be familiar with the market for the shares of stock and relied upon them when they desired to sell their shares.' " *Id.* at 152.

62. 594 F.2d at 1272 (Ely, J., dissenting).

or sale of securities does not seem to be as crucial as the dissent asserts, particularly in the Ninth Circuit.[63] After *Ute*, it was generally agreed that proof of reliance is not necessary in an omissions case; only the materiality of the omission is relevant.[64] There is some disagreement as to whether proof of nonreliance will defeat recovery.[65] Some cases have held a defendant liable to

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63. In Lewelling v. First Cal. Co., 564 F.2d 1277 (9th Cir. 1977), the court stated: "[N]either 10(b) nor or Rule 10b-5 require[s] that the fraud occur *before* the transaction. In accordance with this pronouncement, the trial court below ruled that there is no 'mechanical test such as the clock or the calendar or the metronome' that governs the disposition." *Id.* at 1279 n.4, *citing* Lanning v. Serwold, 474 F.2d 716, 718-19 (9th Cir. 1973) (emphasis in original).

Because the merger agreement predated the defendant's column, the dissent in *Zweig* was concerned that the "in connection with" requirement of rule 10b-5 was not met. However, this requirement has been broadly interpreted. *See, e.g.*, Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co., 404 U.S. 6, 12-13 (1971) ("in connection with" requires that the plaintiff shall have suffered injury due to a deceptive practice "touching" its purchase or sale of securities as an investor); Frigitemp Corp. v. Financial Dynamics Fund, Inc. 524 F.2d 275, 280 (2d Cir. 1975) (the "in connection with" requirement "may apply to a security different from the security whose sale originated the fraudulent scheme"); Vine v. Beneficial Finance Co., 374 F.2d 627 (2d Cir. 1967), (stating, in the context of a short form merger, that fraud on Class A shareholders was "in connection with" the forced sale by B). *Contra*, Raschio v. Sinclair, 486 F.2d 1029 (9th Cir. 1973) (the "in connection with" requirement was not met when the plaintiffs purchased stock prior to the misleading prospectus). However, *Raschio* differs from *Zweig* in that the purchases were actually consummated before the nondisclosure.

64. *See* note 51 *supra*. For cases following *Ute, see* Blackie v. Barrack, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976); Competitive Associates, Inc. v. Laventhol, Krekstein, Horwath & Horwath, 516 F.2d 811 (2d Cir. 1975); Titan Group Inc. v. Faggen, 513 F.2d 234 (2d Cir. 1975); Shapiro v. Merrill Lynch, Pierce, Fenner, & Smith, Inc., 495 F.2d 228 (2d Cir. 1974); Chasins v. Smith Barney & Co., 438 F.2d 1167 (2d Cir. 1970); Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787 (2d Cir. 1969); Tucker v. Arthur Anderson & Co., 67 F.R.D. 468 (S.D.N.Y. 1975); Wolfson v. Solomon, 54 F.R.D. 584 (S.D.N.Y. 1972).

65. In Crocker Citizens Nat'l Bank v. Control Metals Corp., 566 F.2d 631 (9th Cir. 1977), the court suggests that evidence of nonreliance may defeat the inference of reliance. "There was sufficient evidence that the bank did not rely on the alleged misrepresentations, but instead made its own investigation, albeit inadequate, into the marketability of the stock." *Id.* at 636 n.3.

However, in *Zweig*, the evidence of nonreliance was somewhat different. Presumably, if the plaintiffs could have foreseen the future, they would not have relied on the market to set the exchange rate for ASI stock. The fact that they did not rely on the defendant's column specifically does not defeat causation, as the nonreliance in *Crocker* did.

In Blackie v. Barrack, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976), the court stated two ways the defendant could disprove causation: "(1) by disproving materiality or by proving that despite materiality, an insufficient number of traders relied to inflate the price, and (2) by proving that an individual purchased despite knowledge of the falsity of a representation, or that he would have, had he known of it." *Id.* at 906.

For a discussion of reliance, nonreliance, and rule 10b-5, *See* Note, *The Reliance Requirement in Rule 10b-5 Class Actions*, 7 GOLDEN GATE U.L. REV. 373 (1976); Note, *The Reliance Requirement in Private Actions Under SEC Rule 10b-5*, 88 HARV. L. REV. 584 (1975); Note, *Two Different Standards of Reliance Applied in Individual Private Damage Actions Under SEC Rule 10b-5 by the Second Circuit*, 49 TEMP. L.Q. 183 (1975).

a third party when the defendant induces another party to act to the detriment of that third party.[66] Reliance may not be a realistic prerequisite for recovery in an open market context.[67] The court's holding that the reliance requirement was met in *Zweig* is, therefore, not without support.

Also, the Ninth Circuit's extension of this affirmative duty to disclose is logical in terms of the purposes behind the securities laws[68] and the courts' "flexible" interpretation of them to carry out these purposes.[69] Scalping is recognized as a manipulative device that can have a pronounced impact on the market.[70] The

66. In Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787 (2d Cir. 1969), the court concluded that plaintiff had a cause of action when an insider defendant created an extraordinary demand for the stock of a company so that shareholder chose not to tender to plaintiff, which operated to defeat the success of plaintiff's tender offer. Instead of reliance, "[w]hat must be shown is that there was deception which misled [other] stockholders and that this was in fact the cause of plaintiff's claimed injury." *Id.* at 797, *quoting* Vine v. Beneficial Finance Co., 374 F.2d 627, 635 (2d Cir. 1967). *See also* Walsh v. Butcher & Sherrerd, 452 F. Supp. 80, 84 (E.D. Pa. 1978), where the court stated, "[w]hile we can find no authority directly discussing the issue of 'third-party reliance,' our understanding . . . reveals that reliance of this kind cannot be deemed insufficient as a matter of law."

67. One commentator suggests that since a person can be harmed by a deception that effects the prices in the market without having heard the deception, reliance is irrelevant. 3 A. BROMBERG, *supra* note 50, § 8.6. *See also* Tucker v. Arthur Anderson & Co., 67 F.R.D. 468 (S.D.N.Y. 1975) (the focus should be on causation, rather than on reliance); Wolfson v. Solomon, 54 F.R.D. 584 (S.D.N.Y. 1972) (market impact arising from nondisclosure, not reliance on the nondisclosure, causes the injury).

68. *See* SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968) (en banc), *cert. denied*, 394 U.S. 976 (1969) in which the court states: "Rule 10b-5 is based in policy on the justifiable expectation of the securities marketplace that all investors trading on impersonal exchanges have relatively equal access to material information . . ." 401 F.2d at 848. For a discussion of Congressional intent to subject all investors to the same market risks and promote free and open markets, *see* United States v. Charnay, 537 F.2d 341 (9th Cir. 1976), where the court states: "The bill seeks to give investors markets where prices may be established by the free and honest balancing of investment demand with investment supply." *Id.* at 347, *quoting* H.R. REP. No. 1383, 73rd Cong., 2d Sess., at 10 (1934).

69. *See* SEC v. Capital Gains Research Bureau Inc., 375 U.S. 180 (1963). The Supreme Court stated that Congress intended securities legislation designed to avoid fraud to be construed, "not technically and restrictively, but flexibly to effectuate its remedial purposes." *Id.* at 195. *See also,* Peskind, *supra* note 24, at 88, where the author notes that "[c]ourts have emphasized that Rule 10b-5 is intended to be a flexible, general provision to cover all species of fraud."

70. "Scalping involves the purchase of securities by a person in a position to influence others by his recommendation or favorable commentary on that security, the recommendation of that security to investors, and the sale of that security after capital appreciation." Peskind, *supra* note 24, at 81. Scalping was categorized as a manipulative device in SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180 (1963). The success of scalping depends on whether the advice given will be followed and if this will significantly effect the market. For a discussion of the economic impact of scalping, *see* Note, *supra* note 54, at 233-35. *See also* SEC REPORT OF THE SECURITIES MARKETS, H.R. Doc. No. 95,

remedy to prevent abuse is full disclosure.[71] This remedy would work in the present context since it would effectively stop a financial columnist from using his or her position to manipulate the market for a quick profit because the columnist would have to disclose an intention to do just that.[72] Furthermore, "With judicial approval of . . . [defendant's] operation, the integrity and reliability of the financial press would be destroyed."[73] Financial columnists engaging in manipulative conduct should beware of conflicts of interest which must be disclosed, for the Ninth Circuit will extend rule 10b-5 to encompass them.

D. Conclusion

After *Zweig v. Hearst Corporation*, it is clear that the Ninth Circuit will extend an affirmative duty to disclose under section 10(b) and rule 10b-5 to a defendant who is not an insider, tippee, or in a special relationship with the plaintiff. The fact that a financial columnist, such as the defendant in *Zweig*, may not come within the Investment Advisors Act will not insulate the columnist from liability under the federal securities law. Rather, the columnist who intends to engage in stock scalping or who writes from a perspective other than disinterested objectivity, must disclose his or her position to readers, or suffer potential liability under section 10b and rule 10b-5.

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88th Cong. 1st Sess. 70-78 (1963), which discusses the impact even a single newspaper column or magazine article may have on the market.

71. *See* 2 A. Bromberg, *supra* note 50, § 7.4(b). *See also* Fleischer, Mundheim, & Murphy, *An Initial Inquiry Into the Responsibility to Disclose Market Information*, 121 U. Pa. L. Rev. 798, 831 (1973).

72. *See* Fleischer, Mundheim, & Murphy, *supra* note 71, at 827, where the authors state: "Although disclosure is the regulatory technique applied by the cases, it would normally be so embarrassing or impractical to make the required disclosures that, as a practical matter, in most instances scalping and sneaking to the head of the line can be viewed as prohibited."

73. Appellant's Brief at 68, Zweig v. Hearst Corp., 594 F.2d 1261 (9th Cir. 1979). *See also* SEC Report of the Securities Markets, H.R. Doc. No. 95, 88th Cong., 1st Sess. 70-78 (1963), which states that some publications such as Time Magazine and the Wall Street Journal, have policies against writing about a company in which the author owns stock. This suggests a similar concern for the integrity of the press.

VII. IMPROPER REMOVAL: *CALIFORNIA v. C & H SUGAR*

A. INTRODUCTION

In 1975, a large multidistrict antitrust case was filed in the Northern District of California. Designated as *In re Sugar Industry Antitrust Litigation,*[1] it involved several hundred plaintiffs, scores of attorneys and fourteen defendants in approximately one hundred consolidated cases.[2] The State of California filed one case, alleging violation of the Sherman and Clayton Acts.[3] The state sought to represent a consumer class of indirect purchasers composed of its citizens and residents. Shortly after the district

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1. 395 F. Supp. 1271 (J.P.M.D.L. 1975).

2. On December 19, 1974, the government instituted two criminal actions and three injunction lawsuits against several refiners of sugar, charging them with violations of section one of the Sherman Act, 15 U.S.C. § 1 (1979). In the first criminal indictment, United States v. Great Western Sugar Co. Crim. No. CR 74 830 (N.D. Cal. Dec. 19, 1974), *cited in* In re Sugar Industry Antitrust Litigation, 1977-1 TRADE REG. REP. (CCH) ¶ 61,373, at 71,325, the government alleged that defendants unlawfully combined and conspired to fix the price of refined sugar in the Chicago-West Territory. The second criminal indictment and companion civil suit United States v. California & Hawaiian Sugar Co., No. CR 74 2675, *id.*, made similar allegations regarding the California-Arizona Territory.

Thereafter, private parties filed civil antitrust lawsuits in four district courts in California, Illinois, Washington and Minnesota. On June 2, 1975, the Judicial Panel on Multidistrict Litigation transferred the pending cases to the Northern District of California pursuant to 28 U.S.C. § 1407 (1976) for coordinated or consolidated pretrial proceedings. For a discussion of the complex multi-district litigation procedures, *see* note 16 *infra.*

The complaints alleged that the defendants conspired and combined to: (1) establish and raise the basic prices for molasses and refined sugar, (2) establish prepaid freight applications, (3) eliminate, reduce and restrain the providing of allowances to customers for molasses and refined sugar, (4) establish, raise, maintain and stabilize the effective selling prices for molasses and refined sugar, (5) refuse to sell or to limit the sale of private label sugar, (6) threaten to employ price discrimination and sales below cost to force agreement on the non-utilization of private label sugar and on establishing, raising, maintaining and stabilizing the effective selling prices for molasses and refined sugar, (7) discourage customers from entering into any commitments for the purchase of private label sugar, (8) use the monopoly power enjoyed by various of the defendants and their co-conspirators in certain markets to finance and support the previously described practices, and (9) maintain prior agreed upon market shares within the various markets for molasses and refined sugar sales.

As a result of the allegations, every separate sugar product, every method of marketing refined sugar and molasses and every level and method of distribution was before the court. 1977-1 TRADE REG. REP. (CCH) ¶ 61,373.

3. The Sherman Act, 15 U.S.C. §§ 1-7 (1979), provides in pertinent part: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. . . ." *Id.* § 1.

The Clayton Act, 15 U.S.C. §§ 12-17 (1973), provides in pertinent part: "Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor . . . and shall recover three fold the damages by him sustained . . . ." *Id.* § 15.

court denied class certification,[4] *California v. California & Hawaiian Sugar Company (C & H Sugar)*[5] commenced in state court, alleging violation of state antitrust law. The case was removed by the sugar companies to federal district court to be consolidated in the multi-district litigation in process.[6] California moved for an order to remand the case to state court alleging lack of removal jurisdiction. The district court denied the petition for remand.[7]

On appeal, the Ninth Circuit held that federal law does not pre-empt state law and therefore indirect purchasers could file consumer class claims against sugar refiners under California antitrust law in state court.[8] By filing a state claim, such purchasers avoid the problems posed by the United States Supreme Court's controversial *Illinois Brick Co. v. Illinois*[9] decision which held that under federal law indirect purchasers could not re-

4. For a discussion of the issue of class certification in this litigation *see* the district court's opinion in *In re* Sugar Industry Antitrust Litigation, 1977-1 TRADE REG. REP. (CCH) ¶ 61, 373 at 71, 327.

5. 588 F.2d 1270 (9th Cir. Nov., 1978) (per Merrill, J.; the other panel members were Sneed and Lindberg, JJ.) (as modified on denial of rehearing and rehearing en banc).

6. *Id.* at 1271. On removal jurisdiction, one commentator states, "The right to remove an action, properly brought by a plaintiff in one set of courts, into another court system for trial has no roots in common law." 7B J. MOORE, FEDERAL PRACTICE ¶ 89-3, at JC-660 (2d ed. 1979). "If there is to be a removal of action because it is one 'arising under the . . . laws of the United States' the federal claim must be substantial and normally appear in the complaint well pleaded and without anticipation of defenses." *Id.* § 1441, at JC-701.

7. *In re* Sugar Antitrust Litigation, 1976-2 TRADE REG. REP. (CCH) ¶ 61,004. It should be noted that an order granting remand is not appealable except in very limited circumstances inapplicable here. 28 U.S.C. § 1447 (d) (1973). That factor seemed to weigh heavily on the district court when it issued the above order certifying the interlocutory appeal under 28 U.S.C. § 1292(b). *Id.* at 69,443.

8. 588 F.2d at 1274. The consumer claims alleged violations of The California Cartwright Act, CAL. BUS. & PROF. CODE § 16600 *et seq.* (West 1964) relating directly to restraints on competition. The statutory definition of trust is located at CAL. BUS. & PROF. Code § 16720 (West 1964). For the allegations of the complaint which parallel § 16720, *see* note 2 *supra.*

Under § 16750, consumers have standing to sue:

> (a) Any person who is injured in his business or property by reason of anything forbidden or declared unlawful by this chapter, may sue therefor in court having jurisdiction in the county where the defendant resides or is found, or any agent resides or is found, or where service may be obtained, without respect to the amount in controversy, and to recover three times the damages sustained by him, and shall be awarded a reasonable attorney's fee together with the costs of the suit.

CAL. BUS. & PROF. CODE § 16750 (West 1979).

9. 431 U.S. 720 (1977).

cover.[10] The court of appeals noted that the action did not *arise* under federal law and therefore the case should have been remanded to state court for construction under California law.[11]

B. Background

In 1922, the Supreme Court in *Lambert Run Coal Co. v. Baltimore & Ohio Railroad*[12] developed the rule of derivative action. The rule states that if a state court lacks jurisdiction over the subject matter of an action, that defect cannot be cured by removal.[13] Thus, a removed action must be dismissed by the federal court if it has acquired no jurisdiction from the state court. While this rule was developed nearly six decades ago, it was not until 1972 that it was expanded by the Ninth Circuit to include the complex field of anti-trust litigation.

In *State of Washington v. American League of Professional Baseball Clubs (Baseball),*[14] the Ninth Circuit first concluded that under the *Lambert Run* doctrine it was without jurisdiction to proceed on the federal anti-trust claims commenced in state court and second, remanded the case for disposition of the remaining state claims.[15] Although *Baseball* was an extension into the complex field of anti-trust litigation, neither *Baseball* nor *Lambert Run* was a case involving the intricacy of multidistrict litigation.[16]

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10. *Id.* at 729.

11. 588 F.2d at 1274.

12. 258 U.S. 377 (1922).

13. "The jurisdiction of the federal court on removal is, in a limited sense, a derivative jurisdiction. If the state court lacks jurisdiction of the subject matter or of the parties, the federal court acquires none, although it might in a like suit originally brought there have had jurisdiction." Lambert Run Coal Co. v. Baltimore and Ohio R.R., 258 U.S. at 382.

This rule has been vigorously criticized:

> With some logic, but indefensible from the standpoint of practical judicial administration, the principle of derivative jurisdiction, as it pertains to subject matter jurisdiction of the sate court, has been applied so that any action commenced in state court, involving a matter over which the federal courts have exclusive jurisdiction, is subject to dismissal, after removal, for want of jurisdiction even though the federal court would have jurisdiction of a similar case brought originally therein.

1A J. Moore, *supra* note 6, ¶ 157[3] at 46-47; 1976-2 Trade Reg. Rep. ¶ 61,004, at 69,444. For a critical discussion attacking this rule, *see* H. Hart & H. Wechsler, The Federal Courts and the Federal System 1200 (2d ed. 1973).

14. 460 F.2d 654 (9th Cir. 1972).

15. *Id.* at 660.

16. The statutory provisions on multi-district litigation are found at 28 U.S.C. § 1407

The multidistrict litigation laws vested the district courts with broad authority. Developed at a time when federal courts were faced with "massive calendars and mandated speed-up provisions,"[17] the multidistrict litigation vehicle allows preparation and trial of multiple cases that are substantially identical or closely similar, filed in various district courts. This procedure was designed to avoid most of the duplicative and often contradictory practices encouraged by separate cases proceeding in several courts at the same time.[18] This type of litigation seems to have principally arisen in antitrust cases.[19] The Ninth Circuit first extended the *Lambert Run* doctrine only to antitrust cases in *Baseball,* but now extends it to multidistrict litigation as well. Thus *C & H Sugar*[20] is significant since it revives a sixty year old rule in the context of the most complex area of litigation.

Not only was the *C & H Sugar* panel faced with the issue of derivative jurisdiction, but it was also presented with the problems created by *Illinois Brick Co. v. Illinois.*[21] This case has serious implications for the fair and effective enforcement of federal antitrust laws.[22] The majority in *Illinois* held that "the overcharged direct purchaser, and not others in the chain of manufacture or distribution, is the party 'injured in his business or property' within the meaning of Section [4 of the Clayton Act]."[23] Thus in federal antitrust cases, with rare exceptions, only persons who have dealt directly with an antitrust violator can recover damages for injuries suffered as a result of a violation.

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and foll. § 1407 (1976). For discussions of multi-district litigation procedures *see* Levy, *Complex Multi-district Litigation and the Federal Courts,* 40 FORDHAM L. REV. 41 (1971); Grossman, *Class Actions: Manageability and the Fluid Recovery Doctrine,* 47 L.A.B. Bull. 415 (1972); 1 B. GARFINKEL, CURRENT PROBLEMS IN FEDERAL CIVIL PRACTICE 1979 at 521-53 (1978).

17. 1976-1 TRADE REG. REP. (CCH) ¶ 61,004, at 69,445. *See generally* Peterson and McDermott, *Multidistrict Litigation: New Forms of Judicial Administration,* 56 A. B. A. J. 737 (1970); Neal and Golbert, *The Electrical Equipment Antitrust Cases: Novel Judicial Administration,* 50 A.B.A.J. 621 (1964).

18. This argument was the basis of the district court's opinion when the motion for remand was denied. 1976-2 TRADE REG. REP. (CCH) ¶ 61,004, at 69,444-46.

19. B. GARFINKEL, *supra* note 16, at 521.

20. 588 F.2d 1270 (9th Cir. 1978).

21. 431 U.S. 720 (1977).

22. For a discussion of *Illinois Brick, see* Note, *Recovery by Indirect Purchasers and the Functions of Antitrust Treble Damages,* 55 TEX. L. REV. 1445 (1977); S. REP. No. 96-239, 96th Cong., 1st Sess. (1979), *reprinted in* TRADE REG. REP., No. 393 (July 16, 1979), concerning the 1979 Antitrust Enforcement Act, the purpose of which is to legislate away the *Illinois Brick* decision.

23. 431 U.S. at 729. For the text of § 4 of the Clayton Act, *see* note 3 *supra.*

C. State Antitrust Claim

The *C & H Sugar* complaint filed in state court charged that the sugar companies engaged in a conspiracy to restrain trade by the fixing and raising of the price of refined sugar and prepaid freight applications in violation of California's Cartwright Act.[24] Plaintiffs also sought to represent a class of retail purchasers of sugar, but once the case had been removed, the district court denied their motion for class certification.[25]

The plaintiffs moved for remand contending that removal jurisdiction did not exist since the cause of action was based purely on state law. They argued that the facts demonstrating an antitrust violation arose under state, not federal, law and, therefore, there was no basis for removal jurisdiction. The defendant sugar companies argued that the facts alleged in both federal and state actions were identical and should be heard together.[26] District Judge Boldt found that plaintiffs' attempt to seek relief in state court was an improper attempt to circumvent the district court's denial of consumer class certification.[27] The Ninth Circuit rejected these findings, holding that the claims were asserted under California's antitrust laws on facts that did *not* state a federal claim.[28]

Under *Illinois Brick*, a consumer class composed of indirect purchasers cannot claim injury under section four of the Clayton Act.[29] Thus, the court observed that if the consumer class action claims of the plaintiffs were construed under federal law, the holding in *Illinois Brick* would require that the action be dismissed in federal court. While the process of removal of state actions "looks forward to trial of the removed cause in a more appropriate forum,"[30] in this situation, removal would assure that the cause would never be tried at all. The court found it illogical to construe the state law claims as arising under federal law, when, under the federal law of *Illinois Brick*, indirect purchasers

24. Cal. Bus. & Prof. Code § 16,660 *et seq.* (West 1964). *See* note 2 *supra.*

25. 588 F.2d at 1272-73.

26. 588 F.2d at 1272.

27. 1976-2 Trade Reg. Rep. (CCH) ¶ 61,004, at 69,445; 588 F.2d at 1272.

28. *Id.* at 1274.

29. 431 U.S. at 729.

30. 588 F.2d at 1273.

"The right of removal being statutory, a suit commenced in a state court must remain there until cause is shown for its transfer under some act of Congress." Great Northern Ry. Co. v. Alexander, 246 U.S. 276, 280 (1918).

have no standing to assert their claims. On the other hand, under California law indirect purchasers may have standing.[31]

Since the freedom to settle these issues is best left to the state, to deny remand under the circumstances of this case would actually amount to federal pre-emption of the state antitrust laws by judicial act.[32] The state would have no power other than to legislate consistent with the Clayton Act as it was construed in *Illinois Brick.*

The Ninth Circuit further rejected the sugar companies' argument that remand would pose grave problems of management in the litigation.[33] They argued that removal of the case was in the nature of a bill of peace[34] designed to simply join all claims in one forum based upon the same cause of action. The court dismissed that argument by finding that state and federal courts would not be adjudicating identical claims because the plaintiffs, as indirect purchasers, had no federal claims whatsoever. Therefore, it was proper for California to bring the action in state court where it might receive proper recognition.

D. CRITIQUE

While the Ninth Circuit seemed to place considerable emphasis on the *Illinois Brick* decision, it is important to note that case had not been decided until after the appeal in *C & H Sugar* was filed.[35] It would appear that other factors weighed heavily in the court's decision to remand the case to state court. One of the factors was the dicta established in a prior Ninth Circuit case, *In re Western Liquid Asphalt,*[36] which held that there should be no bar to recovery to those who could demonstrate that they "bore the burden of the violation."[37] In *Western,* the court held that

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31. 588 F.2d at 1274.

32. *Id.*

33. Defendants cited Lee's Prescription Shops, Inc. v. Chas. Pfizer Co., Inc., (1970) TRADE REG. REP. (CCH) ¶ 73,180 (S.D.N.Y. 1970), IN WHICH THE COURT REFUSED TO REMAND STATING THAT TO DO SO WOULD BE BURDENSOME AND WASTEFUL.

34. The object of a bill of peace is to suppress useless litigation, to prevent multiplicity of suits, to restrain oppressive litigation, and to prevent irreparable mischief. 2 J. STORY, EQUITY JURISPRUDENCE § 853 (1866).

35. *Illinois Brick* was decided on June 9, 1977. 431 U.S. 720 (1977). However, the appeal for *C & H Sugar* was filed shortly after the July 23, 1976 denial of remand. 588 F.2d at 1271 n.3.

36. 487 F.2d 191 (9th Cir. 1973).

37. The court stated:

> The antitrust laws are to be construed so as to achieve the

indirect consumers have standing to sue based on the theory that unlawful prices charged to their contractors were actually passed on to the consumer.[38] The court's desire to be consistent with *Western* presented a problem for the court. By circumventing the problem posed by *Illinois Brick,* the court extended the questionable *Lambert Run* doctrine to include the field of multidistrict litigation.[39]

Thus, the Ninth Circuit greatly expanded and brought into the modern era a sixty year old rule which held that a federal case must be dismissed when removed from a state court that originally did not have proper jurisdiction. This problem was first evidenced in *Baseball,* where the *Lambert Run* rule was recognized to effect antitrust actions. Now in *C & H Sugar,* the Ninth Circuit again used the derivative jurisdiction doctrine to defeat unified federal control over an antitrust action to give the state courts a means to protect its citizens by application of state rather than federal law.

In view of the intent of multidistrict litigation to bring similar cases involving the same parties together in one forum, the *C & H Sugar* decision may have created additional problems. By permitting the remand of the state case, the court has justified the fragmenting of vast numbers of cases that would normally have been joined in a multidistrict suit.

Michael J. Walker

V. OTHER DEVELOPMENTS IN FEDERAL PRACTICE & PROCEDURE

In *Church of Scientology v. Adams*, 584 F.2d 893 (9th Cir. Oct., 1978), the court upheld a dismissal for lack of personal ju-

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> broad goals which Congress intended to effectuate. *One such policy goal is that there be no hiatus in the enforcement of these laws. Each individual who is injured may sue.* Thus, while we should not impose multiple liability upon defendants, nor give recovery to uninjured plaintiffs, neither should we bar recovery to those who can demonstrate that they bore the burden of the violation.

Id. at 200. (emphasis added). *But cf.*, Sherman, *Antitrust Standing: From* Loeb *to* Malamud, 51 N.Y.U. L. REV. 375 (1976) (sampling of cases where different results have been obtained).

38. 487 F.2d at 200.

39. This problem was articulated by District Judge Boldt in his order denying remand. 1976-2 TRADE REG. REP. (CCH) ¶ 61,004, at 66,996.

risdiction in a libel suit. The California church sued a Missouri publisher claiming jurisdiction in California on the basis of the publisher's revenues from California advertisers. The court held that because the advertising revenue was unrelated to the present action, that that revenue was not the basis for sufficient contact with California. The panel also held that because the Missouri publisher could not have foreseen that any substantial risk of defamation would arise from its circulation of approximately 150 articles in California, that California distribution was held to be insufficient contact with California.

In *Shell Oil Co. v. Train,* 585 F.2d 408 (9th Cir. Nov., 1978), the Shell Oil Company brought an action against the Environmental Protection Agency (EPA) and its administrator as part of an attack on the decision of the California Regional Water Quality Control Board to grant a class E permit for one of Shell's refineries. Shell was dissatisfied with the classification and consequently applied for a variance which was reviewed and denied by the Regional EPA office. Shell alleged in its complaint that the granting of the Class E permit and the denial of its application for the variance from that classification were decisions made by the Administrator of the EPA and not by the Regional Board which was the ostensible decision-making body. Shell's complaint, which was filed in district court, was dismissed for lack of subject-matter jurisdiction. The court of appeals held that alleged EPA coercion did not transform actions of the state agency into federal agency action reviewable by a federal court. Judge Wallace filed a dissenting opinion and would have found jurisdiction in federal court to review an informal and indirect EPA action.

In *International Society for Krishna Consciousness v. Kleppe,* 592 F.2d 529 (9th Cir. Jan., 1979), a religious society and one of its members brought suit alleging violation of their constitutional rights under 28 U.S.C. §§ 1331 and 1343(3),(4). Their petition for preliminary and final injunction relief was denied by the district court. The court of appeals held that even if the constitutional case or controversy requirement was satisfied, the cause of the religious society and its members, who sought freedom to districute literature and solicit contributions in a national park was not ripe for adjudication. It was not ripe because they had not applied for nor had been denied a permit under the challenged regulations and have never been prosecuted

for violation of such regulations. Additionally, new adopted regulations which were specifically designed to deal with their type of activities, cast doubt about the currency and significance of their challenge.

In *Jerlian Watch Co. v. Department of Commerce,* 597 F.2d 687 (9th Cir. May, 1979), the Jerlian Watch manufacturer sued the Secretaries of Interior and Commerce to challenge the validity of the 1979 allocation rules with respect to importation of duty-free watches. The court held that allocation rules were substantially related to traditional customs purposes and, thus, jurisdiction of a challenge to the rules was exclusively vested in the customs courts. Furthermore, plaintiffs had the adequate remedy in the customs court of importing more than a duty-free quota allocation, paying duties assessed, and then suing for refund. The plaintiffs had this remedy despite their contention that it was financially impossible for them to do so.

In *H. Ray Baker, Inc. v. Associated Banking Corp.,* 592 F.2d 550 (9th Cir. Mar., 1979), the court held that although a Philippine corporation had banking relationships in California it was unfair to require it to defend suit on an irrevocable letter of credit in California. The court examined the contacts that the Philippine corporation had and determined that the contacts were not sufficient for jurisdiction. The Philippine corporation had selected a New York bank and as a consequence the corporation could not have reasonably expected the issuance or negotiation of a letter of credit to have had effect in California.

In *Sierra Club v. Hathaway,* 574 F.2d 1169 (9th Cir. Aug., 1978), the Sierra Club, a non-profit environmental organization requested a preliminary injunction to prevent the Secretary of the Interior from executing lease agreements that would give private parties the right to explore for and commercially produce geothermal steam and associated resources in a known geothermal resource area. In denying the injunction, the court held that the casual use step of the exploration phase would not involve activities that would substantially affect the environment. Because the district court considered the testimony of nine experts in relevant fields, the district court's finding that the casual use permitted by the initial step of the exploration phase of the geothermal leasing program would not significantly affect the environment was not clearly erroneous.

In *Anrig v. Ringsby United,* 585 F.2d 1382 (9th Cir. Nov., 1978), plaintiffs brought an action against corporate and individual defendants to recover for breach of lease agreements and violations of the Clayton Act and the Securities Act. Subject matter jurisdiction was based on a federal question and diversity. The court held that the word "defendants", as used in 28 U.S.C. § 1391 (b) and (c) refers to indispensable defendants. Therefore, if a nonresident, nonindispensable party is listed as a defendant, that status will not automatically require dismissal of the entire suit for lack of venue. Rather, all nonindispensable parties should be dismissed to preserve proper venue for the indispensable parties.

In *Church of Scientology v. United States,* 591 F.2d 535 (9th Cir. Feb., 1979), the Church of Scientology petitioned for return of property seized and for the suppression of that evidence. The Ninth Circuit dismissed an appeal from the order denying those motions on the ground that such pre-indictment motions are mere steps in a criminal case. Because the judgment was interlocutory, it was not appealable.

In *Monti v. Department of Industrial Relations,* 582 F.2d 1226 (9th Cir. Sept., 1978), the plaintiff brought a civil rights class action suit charging the California Department of Industrial Relations with systematically engaging in a pattern of employment discrimination against female employees. The plaintiffs' motion for an order to be certified as a class action was denied by the district court. The plaintiffs appealed and further requested that the Ninth Circuit issue a writ of mandamus to compel the district court to certify the class. The court held that a denial of a motion for class certification is not immediately appealable under 28 U.S.C. section 1292(a)(1) and a writ of mandamus would be singularly inappropriate for appeal in this case because it would emasculate attempts to preserve the integrity of the congressional policy against piecemeal appeals.

In *Citizens Utilities Co. v. American Telephone & Telegraph Co.,* 595 F.2d 1171 (9th Cir. Apr., 1979), the court held that with respect to an antitrust action which had been pending for sixteen years and had not yet been tried, the district court's finding of prejudice due to plaintiff's lack of diligence was supported by the record. Therefore, the court found no abuse of discretion in dismissal for want of prosecution.

In *Lee v. Blumenthal,* 588 F.2d 1281 (9th Cir. Jan., 1979), plaintiff sought a writ of mandamus to compel the Secretary of the Treasury to redeem certain flower bonds. Since the court of claims has exclusive jurisdiction over contract actions against the United States where the amount in controversy exceeds $10,000.00 and has authority to render a money judgment founded upon any regulation of an executive department, the Ninth Circuit held that whether the action was characterized as one in contract or one to interpret regulations, the court of claims would be the proper forum.

In *Her Majesty Queen in Right v. Gilbertson,* 597 F.2d 1161, (9th Cir. Mar., 1979), the Canadian Province of British Columbia sued to recover on a judgment for taxes which had been awarded against defendants by a British Columbia Court. The Ninth Circuit examined the British Columbia claim in light of the revenue rule and reciprocity requirement and held that the courts of the United States could not enforce a judgment rendered for taxes by the courts of a foreign government.

In *Smith v. Lujan,* 588 F.2d 1304 (9th Cir. Jan., 1979), a lessee brought an action against the lessor's heirs for reexecution of a lost lease. The court held that the trial court did not err in holding that a suit in equity for a reexecution of a lost lease was not a "claim, or demand against the estate" for purposes of conforming to Guam's "dead man" statute which was identical to California's statute. Additionally, the court held that the doctrine of res judicata did not preclude the lessee's action since a prior order had determined only that the court had been without jurisdiction to order the administrator to execute the lease and, consequently, it did not dispose of issues presented in a subsequent action as to whether or not the lease was executed on a certain date, and if so, its terms and whether the executed copies were lost.

In *Burke v. Ernest W. Hahn, Inc.,* 592 F.2d 542 (9th Cir. Feb., 1979), labor union trustees brought suit for contributions incident to employment. The issue raised by the appeal was whether the district court had jurisdiction over a dispute concerning payments owed by the defendant to union trusts as a result of work completed by defendant's employee. The court held that because defendant's third-party complaint sought recovery of payments made for the same work that formed the ba-

sis for the engineers trustees' complaint in the event the engineers' trustees were successful, the federal district court had ancillary jurisdiction of the employer's claim over and against the trustees of the carpenter's fund. Additionally, with regard to the denial of the carpenters' trust's motion for summary judgment, the court held that the denial of summary judgment may not be reviewable on the theory that dismissal for lack of jurisdiction constitutes a final judgment in which denial of summary judgment merges, allowing review on appeal.

In *People of the Territory of Guam v. Landgraf,* 594 F.2d 201 (9th Cir. Mar., 1979), the defendant appealed from an order of the district court of Guam denying petition to remove his criminal prosecution pending in the superior court of Guam to a district court pursuant to 28 U.S.C. section 1443(1). The court of appeals held that it could not read the statute's reference to an action in "state" court as including an action in the courts of the Territory of Guam because when Congress has intended to extend section 1443(1) to an entity other than one of the fifty states, it has done so expressly.