COMMENTS

The Longshoreman and the Harborworker's Act—An Exclusive Remedy "Full of Sound and Fury, Signifying Nothing"—Herein of Unseaworthiness and Recovery-Over.—The injured longshoreman[1] has been the subject of legislation and judicial decisions in past years which have resulted in the growth of over-lapping and concurrent remedies available to him. It is the purpose of this Comment to highlight the above and to delineate their effect on the longshoreman-stevedore relationship with respect to existing federal legislation.

Rights of Recovery Before 1927

The satisfaction of a cause of action arising out of a maritime tort was traditionally vested with the admiralty side of the federal courts.[2]

1 The term "longshoreman" is used in this Comment to indicate shore workers who load and discharge vessels or who perform labor specifically connected with such loading and discharge. The term "stevedore" or "stevedoring company" refers to the employer of longshoremen. Stevedores are either "contract" stevedores, i.e., independent contractors, or "house" stevedores, i.e., where the shipowner performs its own stevedoring. The distinction is of great economic importance. See note 72, infra. The Comment refers to "injured" longshoremen, although many of the considerations expressed pertain to deaths also. However, the law is more complex in death actions. Survival and wrongful death actions are conferred by statute and there is no federal wrongful death statute covering longshoremen. Cf. N.J. Sandy Hook Pilots Ass'n v. Halecki, 358 U.S. 613, 79 S. Ct. 517, 3 L. Ed. 2d 541 (1959). Death does not give those surviving an action under federal maritime law. Harrisburg, 119 U.S. 199, 7 S. Ct. 140, 30 L. Ed. 358 (1886), Levinson v. Deupree, 345 U.S. 648, 73 S. Ct. 914, 97 L. Ed. 1319 (1953) (dictum), Cortes v. Baltimore Insular Line, Inc., 287 U.S. 367, 53 S. Ct. 173, 77 L. Ed. 368 (1932) (dictum), but see Kernan v. American Dredging Co., 355 U.S. 426, 78 S. Ct. 394, 2 L. Ed. 2d 382 (1958). Longshoremen are not seamen for the purposes of Merchant Marine Act suit, 41 Stat. 1007 (1920), 46 U.S.C. § 688 (1952) (hereinafter cited as Jones Act), Swanson v. Marra Bros., 328 U.S. 1, 66 S. Ct. 869, 90 L. Ed. 1045 (1946), nor are they covered by its wrongful death and survival provisions, incorporating by reference, Federal Employer's Liability Act, 35 Stat. 65 (1908), as amended, 45 U.S.C. §§ 51, 59 (1952) (hereinafter cited as FELA), nor covered by The Death on the High Seas Act, 41 Stat. 537 et seq. (1920), 46 U.S.C. § 561 et seq., hence must refer to state statutes and may do so. Western Fuel Co. v. Garcia, 257 U.S. 233, 42 S. Ct. 89, 66 L. Ed. 206 (1921), cf. N.J. Sandy Hook Pilots Ass'n v. Halecki, supra (wrongful death statute), Holland v. Steag, Inc., 143 F. Supp. 203 (D. Mass. 1956) (survival statute). Various problems arise upon an action on the death of a maritime worker, pursuing a state remedy. Is the unseaworthiness doctrine, see text at note 39 infra et seq., covered by state statutes using phrases as "wrongful act," "omission," "default?" Yes! N.J. Sandy Hook Pilots Ass'n v. Halecki, supra. What standard of contributory negligence should be used in applying the state remedy? Maritime! See 58 Colum. L. Rev. 736 (1958), 70 Harv. L. Rev. 1095 (1957); also, Gilmore & Black, Admiralty, 43 (1957) (hereinafter cited as Gilmore & Black).

2 Rights, duties and liabilities arising out of or incident to the employment of longshoremen on vessels lying in navigable waters are ordinarily governed by the rules of the maritime law. Minnie v. Port Huron Terminal Co., 295 U.S. 647, 55 S. Ct. 884, 79 L. Ed. 1631 (1935), Northern Coal and Dock Co. v. Strand, 278 U.S. 142, 49 S. Ct. 88, 73 L. Ed. 232 (1928). "The Judicial Power of the United States shall be vested in one supreme court and in such inferior Courts as the Congress may from time to time ordain and establish." U.S. Const. art. III, § 1. "The Judicial Power

The existence of a tort as "maritime" was dependent on two tests: one, it had to have occurred on navigable waters within federal jurisdiction and two, the maritime nature of the tort.[3] There is some authority for the view that the locality test was the only requirement,[4] but as concerns longshoremen, the actual solution is probably that the maritime nature test was presumed, in view of the occupation involved, leaving the locality test the

shall extend . . . to all Cases of admiralty and maritime Jurisdiction. . . ." Id. § 2. The Judiciary Act gave the federal district courts original and exclusive jurisdiction "of all civil causes of admiralty and maritime jurisdiction. . . .", but saved common-law actions, based on maritime torts, in state courts when "saving to suitors in all cases the right of a common law remedy where the common law is competent to give it. . . ." Act of September 24, 1789, c. 20, § 9, 1 Stat. 76, 77; re-enacted as Judicial Code, Act of March 3, 1911, c. 231, §§ 24, 256, 36 Stat. 1091, 1160. Saving to suitors insures a suitor of his common-law remedies. 1 C.J.S., Admiralty, 1253, n. 67. This refers to remedies to enforce the federal maritime law and not the creation of local and substantive rights. Knickerbocker Ice Co. v. Stewart, 253 U.S. 149, 40 S. Ct. 438, 64 L. Ed. 834 (1920), reversing 226 N.Y. 302, 123 N.E. 382 (1919). The maritime law and not the common law is to measure the liability of defendant. See Encarnacion v. Jamison, 281 U.S. 635, 50 S. Ct. 440, 74 L. Ed. 1082 (1930), affirming 251 N.Y. 218, 167 N.E. 422 (1929). The saving to suitors clause was interpreted as giving the plaintiff a choice of forums, applying their own substantive doctrines, save in an in rem action, which was of federal concern as it was not a common law remedy. See, e.g., Rounds v. Cloverport Foundry and Machine Co., 237 U.S. 303, 35 S. Ct. 596, 59 L. Ed. 966 (1915) (and distinctions therein). The theory was later amended wherein state courts could grant common law procedural rights while applying maritime substantive law. So. Pacific v. Jensen, 244 U.S. 205, 37 S. Ct. 524, 61 L. Ed. 1086 (1917). The emphasis was on "uniformity" of maritime law. The section now reads: "[A]ny civil case of admiralty or maritime jurisdiction, saving to suitors in all cases all other remedies to which they are otherwise entitled." 28 U.S.C. 1333(1) (1952). See Comment: The Tangled Seine: A Survey of Maritime Personal Injury Remedies, 57 Yale L.J. 220 (1947). As to liability of shipowners and vessels for personal injuries generally, see 48 Am. Jur., Shipping, § 541 et seq. For personal injury as a maritime tort, cognizable in admiralty, see I Am. Jur., Admiralty, § 49, also, Atlantic Transport v. Imbrovek, 234 U.S. 52, 34 S. Ct. 733, 58 L. Ed. 1208 (1913). Gilmore & Black, Chap. VI.

[3] The term "navigable waters" extends to all waters navigable in interstate or foreign commerce. Jackson v. Steamboat Magnolia, 61 U.S. 296, 15 L. Ed. 909 (1858); Gilmore & Black § 1-11. The jurisdiction of the courts of admiralty over torts generally depends upon two tests: the locality of place of injury and the maritime nature of the tort. 51 A.L.R. 117. Causes of action arising from maritime torts (including actions comparable to the common law action on the case) committed on navigable waters within the jurisdiction of federal courts are governed exclusively by maritime law. Robbins Dry Dock & Repair Co. v. Dahl, 266 U.S. 449, 45 S. Ct. 157, 69 L. Ed. 372 (1925). They are triable in admiralty courts. Spencer Kellogg & Sons v. Hicks, 285 U.S. 502, 52 S. Ct. 540, 76 L. Ed. 903 (1932). Also state courts applying maritime law. Kemp v. City of Los Angeles, 172 F. Supp. 66 (1959). See 33 U.S.C. 1331. Land injuries are not triable in admiralty courts. Cf. The Admiral Peoples, 295 U.S. 649, 55 S. Ct. 885, 79 L. Ed. 1633 (1935). Absent diversity of citizenship, a federal district court lacks jurisdiction to entertain an action on its civil jury side based on a maritime tort. Romero v. International Terminal Operating Co., 358 U.S. 354, 79 S. Ct. 468, 3 L. Ed. 2d 368 (1959), Paduano v. Yamashita Kisen Kabushiki Kaisha, 221 F.2d 615 (2d Cir. 1955), cf. Jordine v. Walling, 185 F.2d 662 (3d Cir. 1950). See 31 N.Y.U.L. Rev. 601 (1956).

[4] See 15 L.R.A. (n.s.) 1157.

one to be applied.[5] Thus, the cause of action must have fully accrued on navigable waters; that is to say, the place of injury determined its character.[6] The injured longshoreman was able to recover damages from the ship or shipowner, where he had received his injury on a vessel being loaded or discharged by the stevedore.[7] The liability was based on negligence; a want of care owed to an invitee in connection with structural or other conditions imputing the negligence of owner or crew.[8] The defense of assumption of risk and the fellow-servant rule were available as a bar to the action;[9] but longshoremen, suing on a maritime tort, enjoyed an advantage over workmen in land industry with respect to contributory negligence.[10]

In 1914, the Supreme Court held that a longshoreman, suing on a maritime tort, could sue both the shipowner and his employer for damages, and that the suit was properly triable in admiralty.[11] The body of the decision contained words which have come to haunt the stevedoring industry.[12] At this time, workmen's compensation statutes were in the process

[5] See 51 L.R.A. (n.s.) 1158.

[6] Atlantic Transport Co. v. Imbrovek, 234 U.S. 52, 34 S. Ct. 733, 58 L. Ed. 1208 (1914). Locality refers to the location of the person or thing injured. Rundell v. La Compagnie General Transatlantique, 100 Fed. 655 (7th Cir. 1900). But see note 37, infra.

[7] See 44 A.L.R. 1025, and collected cases.

[8] On a negligence theory, see, e.g., The Earl of Dunmore, 120 Fed. 858 (E.D.N.Y. 1903) (defective hatch cover), Cliffe v. Pacific Mail S.S. Co., 81 Fed. 809 (N.D. Cal. 1897), The Italia, 178 Fed. 996 (E.D.N.Y. 1910) (defective covering of other deck openings), The Helios, 12 Fed. 732 (S.D.N.Y. 1882) (unguarded deck openings), Frazier v. Luckenbach, 248 Fed. 1011 (S.D. Fla. 1918) (unguarded doors), The Max Morris, 24 Fed. 860 (S.D.N.Y. 1885) (unguarded gaps in railings), Keliher v. The Nebo, 40 Fed. 31 (S.D.N.Y. 1887) (defective platforms), The Aurora, 178 Fed. 587 (D. Ore. 1910), aff'd 191 Fed. 960 (9th Cir. 1911) (defective gangways), The Conde Wilfredo, 77 Fed. 324 (5th Cir. 1896) (stanchions insecurely fastened), The Truro, 31 Fed. 158 (E.D.N.Y. 1887) (defective ladders), The Alabama, 242 Fed. 431 (5th Cir. 1917) (want of ladders), Anderson v. The Ashebrooke, 44 Fed. 124 (E.D. Tex. 1890) (ladders improperly located), The Chicago, 156 Fed. 374 (W.D.N.Y. 1907) (skids suspended from defective hinges), The Joseph B. Thomas, 86 Fed. 658 (9th Cir. 1889) (materials insecurely piled or placed), The Anglo-Patagonian, 228 Fed. 1014 (E.D. Va. 1915), aff'd 235 Fed. 92 (4th Cir. 1916), cert. denied, 242 U.S. 636, 37 S. Ct. 19, 61 L. Ed. 539 (1916) (anchor insecurely fastened), The Santiago, 131 Fed. 383 (W.D.N.Y. 1904) (insufficient light). See 80 C.J.S., Shipping, § 80 (n. 88).

[9] See 44 A.L.R. 1116; also Annot., 118 A.L.R. 458.

[10] Annot., 44 A.L.R. 1132.

[11] Atlantic Transport Co. v. Imbrovek, supra note 6.

[12] "The libelant was injured on a ship, lying in navigable waters, and while he was engaged in the performance of a maritime service. We entertain no doubt that the service in loading and stowing a ship's cargo is of this character. Upon its proper performance depend in large measure the safe carrying of the cargo and the safety of the ship itself; and it is a service absolutely necessary to enable the ship to discharge its maritime duty. *Formerly the work was done by the ship's crew;* but, owing to the exigencies of increasing commerce and the demand for rapidity and special skill, it has become a specialized service devolving upon a class 'as clearly identified with maritime affairs as are the mariners.'" 234 U.S. at 61, 62, 34 S. Ct. at 735, 58 L. Ed. at 1212-3. (Emphasis supplied.) The contention that the "work was done by the ship's crew" is strongly contested in Tetreault, Seamen, Seaworthiness, and the Rights of Harborworkers, 39 Cornell L.Q. 318, 412 (1954).

of enactment throughout the country,[13] and the constitutionality of such statutes had been upheld.[14] Thus, the question arose whether the longshoreman, injured in a maritime tort, was properly covered by the state acts.[15] In 1917, the Supreme Court in *Jensen v. Southern Pacific Company* held that the longshoreman's occupation was maritime in character and that injuries resulting therefrom were items of exclusive federal jurisdiction.[16]

[13] All states have enacted workmen's compensation statutes. For description of the provisions and benefits see 2 Larson, Workmen's Compensation §§ 57.00-64.00 (1952) (hereinafter cited as 2 Larson). E.g. Laws 1922, Chapter 615, amending Laws 1913, Chapter 816 and Laws 1914, Chapter 41 (New York); McKinney's Consolidated Laws of New York Annotated, Workmen's Compensation Law.

[14] E.g. New York Central R.R. Co. v. White, 243 U.S. 188, 37 S. Ct. 247, 61 L. Ed. 667 (1917) (New York Statute).

[15] See, e.g. Southern Pac. Co. v. Jensen, 215 N.Y. 514, 109 N.E. 600 (1915).

[16] 244 U.S. 205, 37 S. Ct. 524, 61 L. Ed. 1086 (1917). The Court restricted state workmen's compensation statutes which would result in "prejudice to the characteristic features of the general maritime law or interfering with the proper harmony and uniformity of that law in its international and interstate relations." Id. at 216, 37 S. Ct. at 529, 61 L. Ed. at 1098. Justice Holmes' dissent argued for the inclusion of the state statutes in the common-law remedies saved to suitors. See note 2, supra. "No doubt there sometimes has been an air of benevolent gratuity in the admiralty's attitude about enforcing state laws. But of course there is no gratuity about it. Courts cannot give or withhold at pleasure. If the claim is enforced or recognized it is because the claim is a right, and if a claim depending upon a state statute is enforced it is because the State had constitutional power to pass the law. Taking it as established that a State has constitutional powers to pass laws giving rights and imposing liabilities for acts done upon the high seas when there were no such rights or liabilities before, what is there to hinder its doing so in the case of a maritime tort? Not the existence of an inconsistent law emanating from a superior source, that is, from the United States. *There is no such law. The maritime law is not a corpus juris—it is a very limited body of customs and ordinances of the sea.*" Id. at 220, 37 S. Ct. at 530-1, 61 L. Ed. at 1100. (Emphasis supplied.) "If admiralty adopts common-law rules without an act of Congress it cannot extend the maritime law as understood by the Constitution. It must take the rights of the parties from a different authority, just as it does when it enforces a lien created by the State. *The only authority available is the common law or statutes of a State.*" Id. at 221, 37 S. Ct. at 531, 61 L. Ed. at 1101. (Emphasis supplied.) But is workmen's compensation a common-law remedy? "[T]he common law is not a brooding omnipresence in the sky, but the articulate voice of some sovereign . . . that can be identified. . . ." Id. at 222, 37 S. Ct. at 531, 61 L. Ed. 1101. See 28 U.S.C. § 1333 (1952) for legislative effectuation of Justice Holmes' reasoning, where "common-law remedies" was amended to read "all other remedies to which they are otherwise entitled." See note 2, supra. The dissent of Justice Pitney was succinct: "There is no doubt that, throughout the entire life of the nation under the Constitution, state courts not only have exercised concurrent jurisdiction with the courts of admiralty in actions ex contractu arising out of maritime transactions, and in actions ex delicto arising upon navigable waters, but that in exercising such jurisdiction they have, without challenge until now, adopted as rules of decision their local laws and statutes, recognizing no obligation of a federal nature to apply the law maritime. . . ." Id. at 254, 37 S. Ct. 544, 61 L. Ed. at 1115. This decision was pivotal and, regarding the prestige of the dissenters, of less than forceful weight. See Gilmore & Black, 333 et seq. State compensation acts were held applicable in T. Smith & Son v. Taylor, 276 U.S. 179, 48 S. Ct. 228, 72 L. Ed. 520 (1928) (injuries sustained in performance of a maritime contract, not on navigable waters), P. J. Carlin Constr. Co. v. Heaney, 299 U.S. 41, 57 S. Ct. 75, 81 L. Ed. 27 (1936) (injury incurred on navigable waters, not performing a maritime contract).

The court reasoned that the national character of the industry necessitated a uniformity of jurisdiction, which would be shattered if the various state concepts were permitted to control the question. Congress twice attempted to extend jurisdiction over maritime torts to the states and to thereby enable the injured harborworker, including the longshoreman, to claim the provisions of the applicable workmen's compensation statute,[17] but both attempts were invalidated.[18] In doing so, the Supreme Court indicated that Congress should legislate a uniform law.[19] After this, Committee meetings were held to consider a federal compensation act to cover shoreside personnel.[20] Before the federal statute was enacted, the Supreme Court decided the case of *International Stevedoring Company v. Haverty*,[21] affirming an award against the employer of the injured longshoreman. However, the court based its decision on the rationale that longshoremen were "seamen," hence within the purview of the *Jones Act*.[22] Both *Jensen* and *Haverty*

[17] The Act of October 6, 1917, c. 97, 40 Stat. 395 added to section 24 of the Judicial Code the following italicized language: "Third, of all civil causes of admiralty and maritime jurisdiction, saving to suitors in all cases the right of a common-law remedy where the common law is competent to give it, *and to claimants the rights and remedies under the workmen's compensation law of any State; of all seizures on land or waters not within admiralty and maritime jurisdiction. . . .*" The Act of June 10, 1922, c. 260, 42 Stat. 634 amended the language to read: "Third, of all civil causes of admiralty and maritime jurisdiction, saving to suitors in all cases the right of a common-law remedy where the common law is competent to give it, *and to claimants for compensation for injuries to or death of persons other than the master or members of the crew of a vessel their rights and remedies under the workmen's compensation law of any State, District, Territory, or possession of the United States, which rights and remedies when conferred by such law shall be exclusive; . . . Provided, That the jurisdiction of the district courts shall not extend to causes arising out of injuries to or death of persons other than the master or members of the crew, for which compensation is provided by the workmen's compensation law of any State, District, Territory, or possession of the United States.*" (Emphasis supplied.)

[18] Knickerbocker Ice Co. v. Stewart, 253 U.S. 149, 40 S. Ct. 438, 64 L. Ed. 834 (1920) (invalidating the 1917 amendment), Washington v. Dawson & Co., 264 U.S. 219, 44 S. Ct. 302, 68 L. Ed. 646 (1924) (invalidating the 1922 amendment). Justice Holmes dissented in both cases, following the line he indicated in *Jensen*, supra note 16.

[19] "Without doubt Congress has the power to alter, amend or revise the maritime law by statutes of general application embodying its will and judgment. This power, we think, would permit enactment of a general employer's liability law or general provisions for compensating injured employees: . . ." Washington v. Dawson & Co., supra, at 227-228, 44 S. Ct. at 305, 68 L. Ed. at 652.

[20] See Ambler, Seamen or "Wards of the Admiralty" But Longshoremen Are Now More Privileged, 29 Wash. L. Rev. 243, 253 et seq. and notes (1954). Comment: Overlapping Remedies for Injured Harborworkers: Interaction on the Waterfront, 67 Yale L.J. 1205, 1206 (n. 7), 1240 (n. 159) (1958).

[21] 272 U.S. 50, 47 S. Ct. 19, 71 L. Ed. 157 (1926), affirming Haverty v. International Stevedoring Company, 134 Wash. 235, 235 Pac. 360, 238 Pac. 581 (1925). Justice Holmes, in delivering the opinion, used the Imbrovek rationale, supra note 12, in holding that a longshoreman qualified under the provisions of the Jones Act, supra note 1, note 22, infra.

[22] Merchant Marine Act, 1920 (Jones Act), 41 Stat. 1007, 46 U.S.C. § 688 (1952), providing: "Any seaman who shall suffer personal injury in the course of his employment may, at his election, maintain an action for damages at law, with the right of trial by jury, and in such action all statutes of the United States modifying or extend-

have caused a great deal of confusion by their bases on a view of seamen not traceable to valid authority or precept.[23]

FROM 1927 TO 1946

The Longshoremen's and Harborworker's Compensation Act was passed by Congress in 1927.[24] It was designed to afford relief to those ineligible under state statutes by reason of the *Jensen* case and to implement the replacement of the tort suit remedy by a compensation scheme,[25] which implementation had hitherto been invalidated by the Supreme Court.[26] The Act was to cover "[W]here disability or death results from an injury occurring upon the navigable waters of the United States (including any dry dock) . . . ."[27] Save for the fact that no compensation was provided for injuries caused by the intoxication or intention of the employee, the Act covers accidental injury or demise issuing from and during the course of employment, certain diseases, and death or injury occasioned by the willful act of another.[28] The liability of the employer is absolute and without fault, and the remedy to the employee *"exclusive and in place of all other liability of such employer to the employee, . . .",*[29] save that the noncompliance of the employer subjects him to tort suit.[30] The employee cannot waive the benefits conferred by the Act.[31] The Act sets forth a detailed schedule of benefits to be accorded by the employer for certain injuries as well as for death, and also a detailed procedural system to effectuate its purpose.[32]

Although initially enacted as the exclusive remedy of the employee against the employer and applicable "only . . . if recovery for the disability may not validly be provided by State law.",[33] conflict naturally developed, where the harborworker was concerned, as to the proper jurisdiction where

ing the common-law right or remedy in cases of personal injury to railway employees shall apply. . . ." Supra note 1. Gilmore & Black 279-82.

23 See Tetreault, op. cit. supra note 12, 412.

24 Longshoremen's and Harborworkers' Compensation Act, 44 Stat. 1424 (1927), as amended, 33 U.S.C. §§ 901-50 (1952) (hereinafter cited as the Act). Held constitutional, Crowell v. Benson, 285 U.S. 22, 52 S. Ct. 285, 76 L. Ed. 598 (1932). It excludes masters and crew members, who are covered by the Jones Act, supra note 22, and officers and employees of the United States, covered by the Federal Employees Compensation Act, 39 Stat. 742 (1916), as amended, 5 U.S.C. §§ 751-93 (1952). Id. at § 903(a)(1), (2).

25 Hearings, Committee on Judiciary, 69th Cong., 1st Sess. 40 (April 1926). See Ambler, op. cit. supra note 20, 253 n. 29.

26 Supra note 18.

27 33 U.S.C. § 903(a).

28 33 U.S.C. §§ 920, 902(a).

29 33 U.S.C. §§ 904(b), 905. (Emphasis supplied.)

30 33 U.S.C. § 905. Note that in such suit, the employer may not plead the defenses.

31 33 U.S.C. § 915(b).

32 33 U.S.C. §§ 908, 909 (benefits), 906 (commencement of compensation), 910 (determination of pay), 913 (filing), 919, 923 (procedure), 921 (review), 939 (administration).

33 33 U.S.C. § 903(a). See Gilmore & Black 339.

border-line factual situations were involved,[34] complicated further by the "maritime-but-local" doctrine,[35] which was alleviated to some degree by the Supreme Court in *Davis v. Department of Labor,* indicating that in those cases falling in a "twilight zone" of uncertainty, the first forum selected by the claimant should be presumed to have proper jurisdiction.[36]

[34] The state board had to find that the relief could be "validly provided" without impinging on the "uniformity" doctrine of Jensen, for the legislative intent of the Act was held to be along the Jensen rationale. See Davis v. Dep't of Labor, 317 U.S. 249, 256, 63 S. Ct. 285, 87 L. Ed. 246 (1942). How does this balance with the earlier Congressional attempts to provide state compensation for maritime injuries? See note 17, supra, Gilmore & Black 347-55. The claimant had to choose the correct forum. See note 35, infra. The choice of one did not toll the Statute of Limitations of the other. The time limit for filing a claim under the Act is a year from date of injury or death. § 913(a). See 2 Larson §§ 78.20-.43, appendix, table 19, for state limitation information. Under the Act, compensation payments extend the limit to one year after date of payment. §§ 913(a). "Where recovery is denied any person, in a suit brought at law or in admiralty to recover damages in respect to injury or death . . . the limitation of time . . . shall begin to run only from the date of termination of such suit." § 913(d). Does this apply to a state compensation proceeding? No! It is not a "suit brought at law." Dawson v. Jahncke Drydock, Inc., 33 F. Supp. 668 (E.D. La. 1946).

[35] The Jensen decision had stated that state law could change the maritime law in some measure. Southern Pac. Co. v. Jensen, supra note 16, 216, 37 S. Ct. 524, 529, 61 L. Ed. 1086. In a subsequent case, the Court stated: "The subject is *maritime-but-local* in character and the specified modification of or supplement to the rule applied in admiralty courts, when following the common law, will not work material prejudice to the characteristic features of the general maritime law, nor interference with the proper harmony and uniformity of that law in its international and interstate relations." Western Fuel Co. v. Garcia, 257 U.S. at 242, 42 S. Ct. at 90, 66 L. Ed. at 214 (1921). (Emphasis supplied.) The line had to be defined and "[F]or the next decade and a half 'maritime-but-local' was one of the most flourishing branches of federal jurisprudence." Gilmore and Black at 347. Services "local in character" are those not "so directly connected with navigation and commerce that to permit the rights of the parties to be controlled by the local law would intererfere with the essential uniformity of the general maritime law." Alaska Packers' Ass'n v. Industrial Accident Commission, 276 U.S. at 469, 48 S. Ct. at 346, 72 L. Ed. at 657 (1928). The following were held to be maritime-but-local services. Millers' Indemnity Underwriters v. Braud, 270 U.S. 59, 46 S. Ct. 194, 70 L. Ed. 470 (1926) (diving), Fuentes v. Gulf Coast Dredging Co., 54 F.2d 69 (5th Cir. 1931) (dredging), State v. Duffy, 113 Ohio St. 96, 148 N.E. 572 (1925) (building), Balestrere v. Industrial Accident Commission, 91 Cal. App. 98, 266 Pac. 968 (1928) (fishing in local waters), Eclipse Mill Co. v. Dep't of Labor and Industries of Washington, 141 Wash. 172, 251 Pac. 130 (S.C. 1926); aff'd 277 U.S. 135, 48 S. Ct. 505, 72 L. Ed. 820 (1928) (logging). The following were held to be maritime and not local. London Guarantee & Accident Co. v. Industrial Accident Commission, 279 U.S. 109, 49 S. Ct. 296, 73 L. Ed. 632 (1929) (worker on pleasure fishing vessel), John Baizley Iron Works v. Span, 281 U.S. 222, 50 S. Ct. 306, 74 L. Ed. 819 (1930) (repairing vessel), Maritime torts local in nature: Carlin Constr. Co. v. Heaney, 299 U.S. 41, 57 S. Ct. 75, 81 L. Ed. 27 (1936) (construction worker injured on vessel traveling to island on which he was to work), Alaska Packer's Ass'n v. Industrial Accident Commission, supra (cannery worker injured pushing a boat into water). Maritime torts, not local in nature, Parker v. Motor Boat Sales, Inc., 314 U.S. 244, 62 S. Ct. 221, 86 L. Ed. 184 (1941) (decedent, nominally a janitor, drowned while helping to place outboard motors on boats), London Guarantee & Accident Co. v. Industrial Accident Commission, supra (fatal injury incurred on pleasure craft about a mile from shore). See Gilmore & Black 347-8 on the Parker case, 2 C.J.S., Admiralty, § 62, 80 C.J.S., Shipping, § 85 et seq.

[36] 317 U.S. 249, 63 S. Ct. 225, 87 L. Ed. 246 (1942). "There is, in the light of the

Longshoremen, as a genus, were never subject to the "twilight zone" nor to the "maritime-but-local" doctrine, as their occupation was deemed to be of national, hence exclusive federal concern.[37] Thus the effect of the Act was to provide an exclusive compensation type remedy for maritime torts causing injury or death to longshoremen, with the right accruing to them of third-party actions on a negligence theory.[38] In this period, the legislative intent can be said to have been fully implemented, but, in recent years, the provisions and intent of the Act have been effectively by-passed through the evolution of certain theories, expounded in the decisions of the courts, and applied to longshoremen and their employers, the stevedoring companies. These are the concepts of unseaworthiness of the vessel and recovery-over.

cases referred to, clearly a *twilight zone* in which the employees must have their rights determined case by case and in which particular facts and circumstances are vital elements. . . . Under all the circumstances of this case, *we will rely on the presumption of constitutionality in favor of the state enactment;* for any contrary decision results in our holding the Washington act unconstitutional as applied to this petitioner. A conclusion of unconstitutionality of a state statute can not be rested on so hazardous a factual foundation. . . ." Id. at 256-8, 63 S. Ct. 229-30, 87 L. Ed. at 250-1. (Emphasis supplied.) See Gilmore & Black, 350 et seq. The intent was to lessen the hardships caused by the operation of statutes of limitations where the injured harborworker was faced with an election. See note 34, supra, Gilmore & Black, 347 et seq.; Note, Jurisdiction of State and Federal Compensation Agencies Over Injuries Occurring on Navigable Waters, 53 Yale L.J. 348 (1944); Comment: 67 Yale L.J. 1205, supra note 20, 1212 (n. 26). The decision grants true election for claimants. 317 U.S. 249, 260-64, 63 S. Ct. 255, 87 L. Ed. 246 (dissent). The rationale was aimed at nebulous jurisdictional problems, but later was extended to include clear-cut factual situations. See, e.g. Baskin v. Industrial Accident Commission, 338 U.S. 854, 70 S. Ct. 99, 94 L. Ed. 523 (1949), Bethlehem Steel Co. v. Moores, 335 U.S. 874, 69 S. Ct. 233, 93 L. Ed. 417 (1948). For extension treatment of "recovery-over," note 56, infra, therein defined as an award obtained by a harborworker "under the Longshoreman's Act subsequent to a formal state award or receipt of voluntary payments under state law.", see 67 Yale L.J. 1205, 1215 et seq.

[37] Loading and unloading a vessel is maritime but not local in nature. E.g., Employers' Liability Assur. Corp. v. Cook, 281 U.S. 233, 50 S. Ct. 308, 74 L. Ed. 823 (1930). Before the Act, Jensen had been limited to injuries incurred on the vessel. State Industrial Commission v. Nordenholt Corp., 259 U.S. 263, 42 S. Ct. 473, 66 L. Ed. 933 (1922). Later, federal courts were permitted to extend the maritime remedy to injuries ashore. See O'Donnell v. Great Lakes Dredge & Dock Co., 318 U.S. 36, 63 S. Ct. 488, 87 L. Ed. 596 (1943). See the Act for the Extension of Admiralty Jurisdiction, 62 Stat. 496 (1948), 46 U.S.C. § 740 (1952), granting jurisdiction to the district courts for maritime torts even though "consummated" on land. This was not designed to preempt state jurisdiction, but to provide further remedy for one not covered by state law. See Revel v. American Export Lines, 162 F. Supp. 279 (E.D. Va. 1958).

[38] "If on account of a disability or death for which compensation is payable under this chapter the person entitled to such compensation determines that some person other than the employer is liable for damages, he may elect . . . to receive such compensation or to recover damages against such third person." The Act, § 933(a). Note that the employee's remedy against the employer is exclusive. Id. § 905. Once the employee has accepted compensation under an award, his rights against third parties are subrogated to the employer. Id. § 933(b). If compensation after an award is paid by an insurance company, the employee's right is subrogated to it. Id. § 933 (i). But see text at note 85, infra et seq.

1946 AND AFTER

A. *Unseaworthiness of the Vessel*

Although not applied to longshoremen until 1946,[39] unseaworthiness has had a long history and evolution in connection with seamen. The concern of the courts with the rights of seamen was expressed by Justice Story in *Harden v. Gordon,* one hundred and thirty-seven years ago:[40]

"Every court should watch with jealousy an encroachment upon the rights of seamen, because they are unprotected and need counsel; because they are thoughtless and require indulgence; because they are credulous and complying; and are easily overreached. But courts of maritime law have been in the constant habit of extending towards them a peculiar, protecting favor and guardianship. They are emphatically the *wards of the admiralty;* and though not technically incapable of entering into a valid contract, they are treated in the same manner, as courts of equity as accustomed to treat young heirs, dealing with their expectancies, wards with their guardians, and cestui que trust with their trustees."

With respect to seamen, the concept appeared that the shipowner had a duty to provide a seaworthy vessel, although the theory, in early years, only affirmed the right of a crew member to abandon an unseaworthy ship.[41] Through the nineteenth century, the remedy of seamen for damages was restricted to maintenance and cure,[42] where the injury was caused by the negligence of master or crew, as tort remedy was precluded by the fellow-servant rule.[43] The recognition that the seaman had a remedy for injuries caused by the unseaworthiness of the ship came in 1903, where the liability was indemnity "for injuries received by seamen in consequence of the unseaworthiness of the ship or a failure to supply and keep in order the proper appliances appurtenant to the ship."[44] Litigation evolved on this point, even though the inclusion of operating negligence as a cause of un-

39 Seas Shipping Co. v. Sieracki, 328 U.S. 85, 66 S. Ct. 872, 90 L. Ed. 1099 (1946).

40 11 Fed. Cas. at 485, no. 6047 (C.C.D. Me. 1823). (Emphasis supplied.)

41 Gilmore & Black 316.

42 "The shipowner's liability (for maintenance and cure) is not restricted to injury or illness arising out of or causally related to the seaman's shipboard duties; except for injury and illness caused by the seaman's gross and willful misconduct or existing at the time the seaman signed on and knowingly concealed by him, the shipowner is liable for any injury which occurs or any illness which manifests itself while the seaman is under articles." Gilmore & Black at 254. Maintenance is living expenses during the inactivity of the seaman and is granted without proof of fault. Cure is medical expenses until recovery. Id. 267-9.

43 See the authorities in The Osceola, 189 U.S. 158, 23 S. Ct. 483, 47 L. Ed. 760 (1903). The fellow-servant doctrine was amended to exclude vice-principals by the LaFollette Act: "That in any suit to recover damages for any injury sustained on board vessel or in its service seamen having command shall not be held to be fellow-servants with those under their authority." Act of March 4, 1915, c. 153, 38 Stat. 1185. This was amended by the Jones Act, supra note 22. The Longshoremen's Act eliminates the defenses of the fellow-servant doctrine, assumption of risk and contributory negligence, § 905.

44 The Osceola, supra.

seaworthiness did not come about for many years.[45] Actions on this theory diminished greatly after the passage of the *Jones Act* in 1920, seemingly a more propitious remedy, because it provided for recovery of damages from the employer of a seaman injured in the course of employment by the negligence of master, fellow-servant or crew, or the owner of the vessel.[46] Then, too, there was a belief that an injured seaman had to choose between the *Jones Act* remedy and that of unseaworthiness,[47] and that the former was more advantageous. The case of *Mahnich v. Southern* revolutionized the doctrine by holding that negligence in the operation of the vessel causes an unseaworthy condition, remediable by an action for indemnity on that principle;[48] thus removing the dividing line set up by the *Osceola* case.

The longshoreman, during this period, was restricted to the remedies of maritime law and, then, to those of the Act. This state of affairs was disrupted by the Supreme Court in the case of *Seas Shipping v. Sieracki*.[49] The claimant was an employee of a stevedoring company under contract to load a vessel for petitioner. He was injured when a shackle broke, causing a boom to fall. The District Court found that the defect in the shackle would have been unascertainable by inspection,[50] so that the liability of the shipowner, if any, must necessarily be based on unseaworthiness; thus the issue presented was the applicability of the doctrine to the longshoreman. The Supreme Court held that the longshoreman was a "seaman" for the purposes of applying the unseaworthiness doctrine. The rationale was that the claimant was performing a task on the vessel traditionally performed by the crew, hence could recover against the shipowner.[51] A subsequent case

45 Mahnich v. Southern S.S. Co., 321 U.S. 96, 64 S. Ct. 455, 88 L. Ed. 561 (1944). The litigation was extensive and varied, e.g., Carlisle Packing Co. v. Sandanger, 259 U.S. 255, 42 S. Ct. 475, 66 L. Ed. 927 (1922) (seaman's injuries caused by gasoline in a can marked "coal oil"); see Ambler, op. cit. supra note 20, 246-7 (n. 15), Gilmore & Black 308-15.

46 Gilmore & Black 250-1. Jones Act held constitutional. Panama R.R. Co. v. Johnson, 264 U.S. 375, 44 S. Ct. 391, 68 L. Ed. 748 (1924).

47 Gilmore & Black 288-90. A seaman may sue for unseaworthiness and for Jones Act negligence in one action and, indeed, does not exercise his full remedy unless he does so. E.g., McAllister v. Magnolia Petroleum Co., 357 U.S. 221, 78 S. Ct. 1201, 2 L. Ed. 2d 1272 (1958).

48 Supra note 45. Contributory negligence has never been an absolute defense in suits brought by seamen to recover damages for unseaworthiness, but has been applied in mitigation of damages under a theory of comparative negligence. See, e.g. Socony-Vacuum Oil Co. v. Smith, 305 U.S. 424, 59 S. Ct. 262, 83 L. Ed. 265 (1939).

49 Supra note 39. This decision changed the duty of the shipowner from that of due diligence to maintain a seaworthy ship to an absolute, non-delegable duty to do so. See note 51, infra. Prior to this case, injured longshoremen pursued a negligence theory against the third-party shipowner. E.g. Gerrity v. The Kate Cann, 2 Fed. 241 (E.D.N.Y. 1880), aff'd, 8 Fed. 719 (C.C.N.Y. 1881). See Ambler, op. cit. supra note 20, 248-9 (n. 18). After Sieracki, the action on negligence by the injured longshoreman against the shipowner diminished, for the negligence is actually a lesser included element of the unseaworthiness. Gilmore & Black 364.

50 Sieracki v. Seas Shipping Co., 57 F. Supp. 724 (E.D. Pa. 1944).

51 Supra notes 12, 16. The duty of the shipowner is "absolute." "It is essentially a species of liability without fault, analogous to other well known instances in our law. Derived from and shaped to meet the hazards which performing the service im-

recognized the right of longshoremen to sue on the unseaworthiness theory, in addition to their right to collect workmen's compensation and to bring an action against the third-party shipowner on ground of negligence.[52] The scope of the unseaworthiness theory was increased in *Alaska S.S. Co., Inc. v. Petterson,* which affirmed a judgment stating that the liability for unseaworthiness was an absolute, non-delegable, liability of the shipowner, even though caused by the employer of the injured man while said employer had temporary control of the vessel.[53] The doctrine imposed a liability of absolute and non-delegable nature for deficiency in personnel or equipment. This remedy is one which became greatly expanded and has been made available to harborworkers exposed to the hazards of the vessel.[54] The result

poses, the liability is neither limited by conceptions of negligence nor contractual in character. . . . It is a form of absolute duty owing to all within the range of its humanitarian policy." Seas Shipping Co. v. Sieracki, supra note 39, at 94-5, 66 S. Ct. at 877, 90 L. Ed. at 1106. "[D]ue diligence of the owner does not relieve him from this obligation." Id. at 104, 66 S. Ct. at 881, 90 L. Ed. at 1111 (in dissent arguing that the doctrine should not be extended to longshoremen).

52 Pope & Talbot, Inc. v. Hawn, 346 U.S. 406, 78 S. Ct. 1206, 2 L. Ed. 2d 1278 (1953).

53 Alaska S.S. Co., Inc. v. Petterson, 347 U.S. 396, 74 S. Ct. 601, 98 L. Ed. 798 (per curiam); rehearing denied, 347 U.S. 994, 74 S. Ct. 639, 98 L. Ed. 1092 (1954). Thus, control is no longer a factor, although after Sieracki it had been thought that lack of control of the vessel released the shipowner. See 69 Harv. L. Rev. 1128 (1956). A stevedore in control of the vessel can render it unseaworthy and impose liability on the shipowner for injuries incurred by longshoremen as a result of the unseaworthiness. See, e.g., Grillea v. United States, 232 F.2d 919 (2d Cir. 1956). Is absolute seaworthiness required? No, "Reasonable" seaworthiness. Cf. Grillea v. United States, supra.

54 The remedy exists only for shipboard injury or death. See note 78, infra. In Sieracki, supra note 39, the Court had said that the duty of maintaining a seaworthy vessel was one "owing to all within the range of its humanitarian policy." Id. at 95, 66 S. Ct. at 877, 90 L. Ed. at 1106. Who are these? The Second Circuit limited the rule to longshoremen (and, of course, to seamen). Guerinni v. United States, 167 F.2d 352 (2d Cir. 1948), cert. denied, 335 U.S. 843, 69 S. Ct. 65, 93 L. Ed. 393 (1948). In Pope & Talbot, Inc. v. Hawn, 346 U.S. 406, 74 S. Ct. 202, 98 L. Ed. 143 (1953), the Supreme Court broadened the scope considerably. Hawn was a carpenter employed to work on a grain vessel. The Court said: "The ship on which Hawn was hurt was being loaded when the grain loading equipment developed a slight defect. Hawn was put to work on it so that the loading could go on at once. There he was hurt. His need for protection from unseaworthiness was neither more nor less than that of the stevedores [longshoremen] then working with him on the ship or of seamen who had been or were about to go on a voyage. All were subjected to the same danger. All were entitled to like treatment under law." Id. at 413, 74 S. Ct. at 207, 98 L. Ed. at 153. Gilmore & Black § 6-55. The criterion seems to be that of work traditionally performed by seamen. Who are not within the doctrine? N.J. Sandy Hook Pilots Ass'n v. Halecki, supra note 1 (sub-contractor repairman), McDaniel v. Lisholt, 358 U.S. 925, 79 S. Ct. 222, 3 L. Ed. 2d 299 (1959) (fireman-job not traditionally performed by crew), Lyon v. United States, 265 F.2d 219 (2d Cir. 1959) (repairman), Flowers v. Travelers Ins. Co., 258 F.2d 220 (5th Cir. 1958) (longshoreman performing duties as a welder), Filipek v. Moore-McCormack Lines, 258 F.2d 734 (2d Cir. 1958) (boom tester), Berge v. Nat. Bulk Carriers, 251 F.2d 717 (2d Cir. 1958) (shipyard rigger), Latus v. United States, 170 F. Supp. 837 (E.D.N.Y. 1959) (painter on moth-ball vessel). As for items of unseaworthiness see Crumady v. Joachim Hendrik Fisser, 358 U.S. 423, 79 S. Ct. 445, 3 L. Ed. 2d 413 (1959) (winch), Duplanty v. Matson Nav. Co., 1959 A.M.C. 678 (Sup. Ct. Wash.) (gangway maintained by owner for crew), DeVan v.

of *Sieracki* was that where an employer's negligence had caused the employee-longshoreman's injury on the vessel, the owner of the vessel bcame liable in damages on the unseaworthiness theory and was thus placed in a position of having to repay the employer that which he had paid in compensation despite the employer's negligence.[55] The shipowner was in need of a remedy.

B. *Recovery-Over*

The second theory which, with that of unseaworthiness, has resulted in circumvention of the exclusive remedy provision of the Act, is that of recovery-over.[56] This concerns the right of the shipowner to recover the damages paid to the injured longshoreman from the party whose negligence caused the unseaworthy condition. Prior to *Sieracki,* the unseaworthiness doctrine was available only to seamen,[57] and longshoremen, permitted to sue third parties by the Act, could recover from the shipowner only on a negligence theory.[58] After *Sieracki,* however, the question of the shipowner's remedy became very important. At first, the Supreme Court took the position that if the unseaworthy condition was attributable to the shipowner in any degree, there could be no recovery-over, as one joint tort-feasor had no right to contribution from another.[59] This rationale left the employer-

Penna. R.R., 167 F. Supp. 336 (E.D. Pa. 1958) (adjacent vessel), Pierce v. Erie R.R., 264 F.2d 136 (2d Cir. 1959) (oil spot), Casbon v. Stockard S.S. Co., 173 F. Supp. 845 (E.D. La. 1959) (scaffold), Fappiano v. United States, 1959 A.M.C. 197 (S.D.N.Y.) (hatch cover), Oleszcuk's Case, 266 F.2d 79 (4th Cir. 1959) (running rigging), Considine v. Black Diamond S.S. Co., 163 F. Supp. 109 (D. Mass. 1958) (lower hold), Blankenship v. Ellerman's Wilson Line, 159 F. Supp. 479 (D. Md. 1958) (insufficient lighting).

55 See 66 Yale L.J. 584 (1957).

56 Recovery-over is used in this Comment to indicate the shipowner's recovery from the employer of the injured longshoreman where the employer has caused the unseaworthy condition; the competent producing cause of the injury. But see note 36, supra. The shipowner's protection from liability for the stevedore's negligence causing injury to his employee arises under the theories of contribution or indemnity. Crawford v. Pope & Talbot, Inc., 206 F.2d 784 (3d Cir. 1953). See Weinstock, The Employer's Duty to Indemnify Shipowners for Damages Recovered by Harbor Workers, 103 U. Pa. L. Rev. 321 (1954).

57 Tetreault, op. cit. supra note 12, 383. Generally, Gilmore & Black 315-33.

58 E.g. The Pacific Pine, 31 F.2d 152 (W.D. Wash. 1929), also Williams Steamship Co. v. Parsons, 96 F.2d 219 (4th Cir. 1938), U.S. Fidelity v. United States, 152 F.2d 46 (2d Cir. 1945).

59 Halcyon Lines v. Haenn Ship Ceiling Corp., 342 U.S. 282, 72 S. Ct. 277, 96 L. Ed. 318 (1952). "In the absence of legislation, courts . . . have generally held that they cannot on their own initiative create an enforceable right of contribution as between joint tort-feasors. . . . We have concluded that it would be unwise to attempt to fashion new judicial rules of contribution and that the solution of this problem should await congressional action. . . ." Id. at 285-6, 72 S. Ct. at 279-80, 96 L. Ed. at 320. Thus, the Court said that, barring legislation and recovery-over on an indemnity theory, the shipowner must bear the full liability, for damages will not be apportioned by way of contribution, save in collision cases. See 25 Geo. Wash. L. Rev. 708 (1957). "[W]e believe sound judicial administration requires us to point out that in the area of contractual indemnity an application of the theories of 'active' or 'passive' as well as 'primary' or 'secondary' negligence is inappropriate." Weyer-

stevedore almost invulnerable.[60] The Supreme Court had discussed recovery-over on an express contract of indemnity prior to *Halcyon*,[61] and lower courts attempted to evade the inequity presented by *Halcyon;* one, on an implied contract between shipowner and stevedore;[62] another, on the principle that the passive tort-feasor is entitled to indemnification by the active tort-feasor.[63] The Supreme Court finally settled the question on a "warranty of workmanlike service" theory in *Ryan Stevedoring Co., Inc. v. Pan-Atlantic S.S. Corp.*,[64] evading the exclusive remedy intent of the Act by saying that the claim against and the liability of the employer-stevedore was based on contract, not tort, hence not "on account of" the injury. The *Ryan* rationale is law today.[65]

C. *Result*

As has been stated above, the Act reserves to the longshoreman, and to a harborworker covered by its provisions, the right to sue third parties,

haeuser S.S. Co. v. Nacirema Operating Co., 355 U.S. at 569, 78 S. Ct. 442, 2 L. Ed. 2d 495 (1958).

60 Unless the shipowner was absolutely free from negligence, he could not, according to Halcyon, recover-over against the stevedore, hence had to bear the total cost arising out of an injury to the cause of which he contributed little.

61 American Stevedores v. Porello, 330 U.S. 446, 67 S. Ct. 847, 91 L. Ed. 1011 (1947), remanding the case to the District Court for determination of the word "responsible" in an indemnity clause contained in the contract between shipowner and stevedore, indicating that it could mean indemnity on the sole fault of the stevedore, indemnity on the concurrent fault of both stevedore and shipowner or proportional indemnity. Also, Brown v. American-Hawaiian S.S. Co., 211 F.2d 16 (3d Cir. 1954).

62 Allen v. States Marine Corp., 132 F. Supp. 146 (S.D.N.Y. 1955). See Crawford v. Pope & Talbot, Inc., supra note 56. "It is difficult to conceive of a situation where there is no contract, either express or implied, between an employer whose men are aboard or about a vessel and the owner or charterer of such vessel." Brown v. Hawaiian S.S. Co., supra, 18 (n. 4).

63 Berti v. Compagnie di Navigation Cyprien Fabre, 213 F.2d 397 (2d Cir. 1954). Cf. McFall v. Compagnie Maritime Belge, 304 N.Y. 314, 107 N.E.2d 463 (1952).

64 Palazzolo v. Pan-Atlantic S.S. Corp., 211 F.2d 277 (2d Cir. 1954), affirmed without opinion, Ryan Stevedoring Co., Inc. v. Pan-Atlantic S.S. Corp., 349 U.S. 901, 75 S. Ct. 575, 99 L. Ed. 1239 (1955), vacated 349 U.S. 926, 75 S. Ct. 769, 99 L. Ed. 1257, affirmed 350 U.S. 124, 76 S. Ct. 232, 100 L. Ed. 133 (1956). The employer's negligence was a breach of a "warranty of workmanlike service." Id. at 133, 76 S. Ct. at 237, 100 L. Ed. at 142. Thus the exclusive remedy protection of the employer is evaded for the ground of recovery is contract and not the injury. 350 U.S. 124, 132, 133, 76 S. Ct. 232, 237, 100 L. Ed. 133, 141, 142. Is this duty of the stevedore owed only to the party who has contracted his services? No. The stevedore who enters into a contract with the charterer of a vessel, owes this duty to the shipowner, even though the latter is not a party to the contract. Cf. Crumady v. Joachim Hendrik Fisser, supra note 54. Is the stevedore's liability dependent on his causing the unseaworthy condition? No, it exists if the stevedore brings it into play. Ibid. Need the contract between stevedore and shipowner be express? The Supreme Court has granted certiorari to review a case involving this question. Docket No. 697—October Term—1959—Waterman Steamship Corporation v. Dugan & McNamara, Inc. It would seem the main issue in unseaworthiness is one of extension. See Crumady v. Joachim Hendrik Fisser, supra note 54.

65 Gilmore & Black 373-4. Note that Czaplicki, see infra, has been "read broadly" and that the employer cannot "force a statutory assignment of the cause of action. . . ."

whose negligence has caused their injury.[66] It also provides that this right is subrogated to the employer where the injured harborworker has accepted a final award of compensation.[67] Judicial decisions have vitiated the intent of the Act with respect to the above.

1. *Third-Party Actions*

It has been seen that the unseaworthiness doctrine was made available to longshoremen; that the unseawothiness of a vessel could be caused by the negligence of the stevedore and that the shipowner, liable to the injured longshoreman, could recover-over against the stevedore for breach of warranty, where the stevedore's negligence produced the unseaworthy condition on the vessel.[68] Thus, for all practical purposes, a longshoreman, injured through the negligence of his employer, has had fashioned for him a method by which he may sue his employer, even though the Act purportedly exists as an exclusive remedy.[69] The result has been criticized on theory and fact.[70] As a matter of semantics, the employer is sued for breach of warranty and not for personal injury.[71] The line, if any, is exceedingly fine and it is submitted here that the Act has been effectively nullified, in this connection, and that this nullification has resulted in an economic inequity for the contract stevedoring industry.[72]

2. *After a Formal Award*

After acceptance of a formal award of compensation, the right of the injured harborworker against third parties is subrogated or assigned to his employer.[73] The employer may pursue the claim by suit or compromise.[74]

66 Supra note 38.

67 Ibid.

68 See text and note material note 38, supra.

69 Supra note 29.

70 See Tetreault, op. cit. supra note 12, 391-403; Comment, 67 Yale L.J., op. cit. supra note 20, 1244; Ambler, op. cit. supra note 20, 262; 66 Yale L.J. 581 (1957); The Tangled Seine: A Survey of Maritime Personal Injury Remedies, 57 Yale L.J. 243 (1947).

71 See note 64, supra.

72 The stevedoring industry comprises "house" and "contract" stevedores. See note 1, supra. A shipowner performing his own stevedoring services is a "house" stevedore. Naturally, an injured longshoreman cannot pursue the unseaworthiness theory against a vessel when working for a "house" employer because the shipowner is not a third party in this case but is his employer. Consequently, the Act is operative in this instance. The "contract" stevedore is an independent contractor; a service organization tied to the shipowner contractually. It is this employer and his employees to whom this Comment has been referring. Necessarily, the latter must prepare for higher tort recoveries, i.e., injury and death allocations over and above those necessitated by the Act; whereas the former need only anticipate compensation costs. The difference must reflect in the rates of a competitive concern, thus producing an inequity of competition. The Supreme Court, in the case of Herd v. Krawill, 359 U.S. 297, 79 S. Ct. 766, 3 L. Ed. 2d 820 (1959), permitted another competitive disparity in a question concerning the extension of a limitation-of-liability provision between shipper and carrier to the stevedore. See Note, 5 N.Y.L. Forum 409 (1959).

73 Supra note 38.

74 44 Stat. 1440 (1927), 33 U.S.C. § 933(d) (1952); See Note, 66 Yale L.J. 581, 586-7 (1957).

In any recovery, the employer takes expenses of litigation, medical care and compensation payments and the employee takes the remainder.[75] The Act is not conditional, for it must have been presumed, upon enactment, that the assignee-employer would wish to recoup his payments to the employee by action against the third party.[76] Thus, a longshoreman, injured by the negligent operation of X Corporation's truck, while working for Y Stevedoring Corporation, elects to accept a compensation award. The Y Corporation, as assignee, will take action against X Corporation to recover. No conflict of interests exists here and none seems to have been contemplated by the Act.[77] But, conversely, a longshoreman-employee of Y Stevedoring Corporation is injured on the ship of X Corporation, for whom Y Corporation was performing stevedoring services. The negligence of Y Stevedoring Corporation caused the unseaworthiness which injured the employee.[78] The injured worker accepts a formal award. Now a conflict of interests exists and a dilemma too. If Y proceeds to sue the X Shipping Corporation, on the right subrogated to it, Y sues its own customer, which it may be reluctant to do, and may also have to indemnify the X Shipping Corporation.[79] By pursuing the right assigned to it, the stevedoring concern is potentially exposing itself to greater liability than that represented by the amounts paid to the injured employee. Consequently, the situation pictured in the dissent by Mr. Justice Black in *Ryan* became possible, wherein the employer attempted to force a formal award and abandon the cause.[80] In doing this, the employer would not, as a practical matter, lose the amount paid as compensation, for insurance premiums,[81] to cover this liability, are reflected in rates; so too, when the stevedore is self-insured.[82] The consequence of this was that the longshoreman, having accepted the formal award, was effectively shut out from further compensation for his injuries where the interest of his employer was adverse to his own. As Mr. Justice Black stated in *Ryan:*[83]

75 33 U.S.C. § 933(e)(1)(2).

76 "Acceptance of such compensation under an award in a compensation order filed by the deputy commissioner *shall* operate as an assignment to the employer of *all* right of the person entitled to compensation to recover damages against such third person." § 933(b). (Emphasis supplied.)

77 Ibid.

78 This is the most frequent situation and the only one of real concern with respect to the vitiating of the Act. The unseaworthiness remedy is only available for a shipboard injury or death. Frederick v. American Export Lines, Inc., 227 F.2d 450 (2d Cir. 1955), cert. denied, 350 U.S. 989, 76 S. Ct. 475, 100 L. Ed. 855 (1956). Cf. Jacobson v. Columbia Hudson Lumber Co., 1959 A.M.C. 468.

79 Thus, it presents an absurd picture of a plaintiff suing himself, clearly not a situation envisaged by the Act. The maximum amount payable under the Act for an injury is $17,280.00. 33 U.S.C. § 914(m). In Ryan, for example, the recovery against the stevedore was $75,000.00.

80 Ryan Stevedoring Co., Inc. v. Pan-Atlantic S.S. Corp., supra note 64, 135 et seq., 76 S. Ct. 232, 238 et seq., 100 L. Ed. 133, 142 et seq. See text at note 83, infra.

81 44 Stat. 1439 (1927), 33 U.S.C. § 932(1). See also §§ 935, 936, 938.

82 Id. at § 932(2).

83 350 U.S. at 139, 144, 145, 76 S. Ct. at 240, 242, 243, 100 L. Ed. at 145, 147.

"I have set out the evidence in some detail because I think it shows almost beyond doubt that this stevedoring company is being required to pay a $75,000 verdict "on account of" injuries to an employee. . . . (T)he Court's action here not only deprives the employer of his limited liability, it makes the right of employees to recover damages from third parties a barren purpose. Palazzolo was able to make an election and bring his own suit, because his employer was financially interested in the outcome of his case and therefore advanced money to Palazzolo to sustain him during his injury until his case against the third party could be tried. . . . Hereafter stevedoring companies . . . will know that it is decidedly to their advantage that no third-party actions be brought. [Against a shipowner.] Human nature and habits being what they are, employers will not be eager to finance suits against themselves. . . ."

Of course, this feature of the Act was not of overwhelming importance, for the well advised longshoreman refrained from accepting a formal award.[84] Since 1956, however, there have been decisions which have nearly eliminated whatever advantage existed for the employer.

In the case of *Czaplicki v. The Hoegh Silvercloud*,[85] the Supreme Court interpreted the Act to presuppose the situation where the interest of the employer is not in conflict with that of the employee who has accepted a formal award. In this case, a longshoreman had obtained and accepted a formal award. The insurer of the employer, also the insurer of the shipowner, did not bring the action, subrogated to it, against the shipowner. The court seized the elements of *conflict of interest* and *inaction* to fashion a construction of the statute so as to allow Czaplicki to bring suit in his own name as "the only person with sufficient adverse interest to bring suit."[86] This decision is narrow in its holding and was regarded as an ineffectual protection of the employee, for the employer was fully empowered to settle with the shipowner to cover compensation and expenses, or some portion thereof, thus removing the essential allegation of inaction from the factual situation.[87] Subsequent decisions, however, have indicated judicial concern over the problem to the extent of negating the element of inaction and indicating that where a conflict of interests exists, the injured employee is the only party entitled to bring the action,[88] or that the burden of proof is on the employer to rebut a presumption of adverse interest.[89] Thus the case of *Johnson v. Sword Line, Inc.*,[90] involving assignment, via acceptance of a formal award, to the stevedore and its carrier, who were clearly liable to indemnify the shipping company; that is, likely to pay the judgment on the right of action assigned to them, held that the employer must establish a "valid basis" for inaction or be subject to a presumption that a conflict of interests exists. And in the case of *D'Amante v. Isthmian*

84 See Comment, 67 Yale L.J., op. cit. supra note 20, 1241-2 (n. 157).
85 351 U.S. 525, 76 S. Ct. 946, 100 L. Ed. 1387 (1956).
86 Id. at 531, 76 S. Ct. at 950, 100 L. Ed. at 1394.
87 E.g. Note, 66 Yale L.J. 581 (1957).
88 D'Amante v. Isthmian Lines, Inc., 159 F. Supp. 468 (E.D.N.Y. 1958).
89 Johnson v. Sword Line Inc., 1958 A.M.C. 1942 (3d Cir.).
90 Ibid.

Lines, Inc.,[91] the third-party risk insurer of a stevedoring corporation, to whom plaintiff's right had been subrogated, attempted to evade the *Czaplicki* rationale by hiring a law firm to represent the plaintiff's interests against the stevedore-insured. In effect, the party liable was bringing the action, hence acting so as to avoid the "inaction" allegation of *Czaplicki*.[92] The sham was disallowed. The trend indicates that the Supreme Court may eventually hold that the existence of the longshoreman-stevedoring company-shipping company relation, where a maritime tort is involved, raises an irrebutable presumption of adverse interest, thereby removing them, with respect to subrogation upon acceptance of a formal award, from the operation of the Act. This line of decisions resolves an inequity and the writer has no quarrel with them save that they are necessitated, as was *Ryan*, by bad fruit, stemming from the lack of judicial restraint which caused the first inroads into the Act.[93] Certainly no adverse interest was contemplated by the legislators, for none was possible where the exclusive remedy provision of the Act had practical effect.

CONCLUSION

The result of the decisions to date has been the grafting of a tort remedy to that of compensation; a result not contemplated by the words of the Act.[94] Upon the inroads, the remedies were initially co-existent, yet alternate, but the *Czaplicki* case and the subsequent decisions thereto tend to place the tort remedy in the character of an additive to the automatic

[91] Supra note 88.

[92] "In giving the assignee exclusive control over the right of action, however, we think that the statute presupposes that the assignee's interests will not be in conflict with those of the employee, and that through action of the assignee the employee will obtain his share of the proceeds of the right of action, if there is a recovery. Here, where there is such a conflict of interests, the inaction of the assignee operates to defeat the employee's interest in any possible recovery. Since an action by Traveler's would, in effect, be an action against itself, Czaplicki is the only person with sufficient adverse interest to bring suit." Czaplicki v. The Hoegh Silvercloud, supra note 85 at 531, 76 S. Ct. at 950, 100 L. Ed. at 1394. See Annot., 98 L. Ed. 160.

[93] See Ambler, op. cit. supra note 20, 262. This seems to be an arguable conclusion. In Pope & Talbot, Inc. v. Hawn, 346 U.S. 406, 74 S. Ct. 202, 98 L. Ed. 143 (1953), Justice Jackson, in dissent, stated: "[T]his is enough to demonstrate that Congress knew and respected the difference between the seaman to whom it preserved admiralty remedies plus the remedies of the Jones Act, and harbor workers, such as claimant, who are given the remedies of the compensation act, like most other shore workers. I cannot bring myself to believe that it is either the congressional will or the tradition of maritime law or common sense to mingle the two wholly separate types of labor in their remedies as is being done in this case." Id. at 426, 74 S. Ct. at 213-4, 98 L. Ed. at 159-60. See note 70, supra. The oral argument of the Sieracki case was heard by seven members of the Court. Mr. Justice Jackson was in Europe conducting the Nuremberg trials and Mr. Justice Reed was absent, although he cast his vote with the majority. Both dissented in Pope & Talbot Inc. v. Hawn, supra. The Sieracki result might never have come about had the full court heard the argument of counsel. See Paper, Let's Have Another Look at Sieracki v. Seas Shipping Co., 328 U.S. 85, by Vincent A. Catoggio, a member of the New York Bar.

[94] Supra note 29.

compensation machinery,[95] thus superimposing upon the class coverage of the compensation scheme the higher tort award possibility, with its attendant evils.[96] The writer submits that *Ryan* and *Czaplicki* are good law, but their need stems from the extension of the seaman's remedy for unseaworthiness to longshoremen. The theoretical validity of this extension has been critisized,[97] even though its source must be respected. However, the practical situation which has evolved certainly indicates a need for revision. The shipping companies, with some exceptions, have been lax in their investigating procedures, immediately after an accident, to isolate and fix the exact circumstances surrounding it, which, when coupled with plaintiff's strategy of delaying commencement of suit until the end of the statute of limitations,[98] combine to make a case susceptible to puffing, collusion or even fraud.[99] Thus, the field has been flooded with unseaworthiness litigation.[100] It should be noted that the ultimate expense of litigation and judgments to the stevedore is borne by the shipping companies in the form of an increased rate.

Judicially, the Act may be brought to proper focus by overruling *Sieracki,* but, as such judicial action seems unlikely, the correction must be legislative. There has been a Bill introduced in Congress "To amend the Longshoremen's and Harborworkers' Compensation Act to insure that employers will be immune from suit for injuries for which compensation has been paid."[101] The Bill proposes to add to Section 5 of the Act[102] the following italicized clause: "The liability of an employer prescribed in section 4 shall be exclusive and in place of all other liability of such employer . . . on account of such injury, *or by reason of an employer's breach of any duty or obligation, except on express contractual assumption of liabilities owed by such employer to another against whom such employee has a cause of action subject to the provisions of Section 33 of this Act, . . .*" With reference to the problem at hand, this means that the employer-stevedore would not be ultimately liable to the shipping company on plaintiff-longshoreman's judgment unless the stevedore had expressly held the shipping company "harmless." It must be pointed out that, should the Bill be enacted, its

95 Stevedoring companies, with respect to third-party suits against the shipowner for unseaworthiness, seem to be automatically adverse parties in interest under the Czaplicki rationale, and that of the subsequent cases.

96 E.g. Pierce v. Erie R.R., supra note 54. (Concerning an oil spot which may never have existed.)

97 See notes 70, 93, supra.

98 See note 34, supra.

99 Letter to the writer from Mr. Walter J. Byrne, Executive Vice-President, John W. McGrath Corporation, New York City. Mr. Byrne is a professional engineer and is an expert in the field of safety and preventative maintenance in shipping and stevedoring operations. He indicates that the clearly defined case of unseaworthiness, as falling booms, is a rarity; that more often, the condition is a border-line one.

100 The 1959 A.M.C. Index-Digest devotes 41 pages to the sub-section "Personal Injury."

101 H.R. 11267, introduced by Rep. Durham (D) of North Carolina on March 18th, 1960.

102 Supra note 29.

effect, at best, is partial. The unseaworthiness remedy would still be available against the shipping companies and, as a practical matter, there would be very few stevedoring contracts signed which did not contain a "hold harmless" agreement; so that, as a result, the same situation would obtain. This Bill places the contractual recovery-over within the exclusive remedy provision of the section, seemingly rectifying that which has been outlined in this Comment, but it must be pointed out that the effect may be nil in that the *Sieracki* rationale would remain and in that it is possible that the courts will side-step the intent of this Bill just as they did the Section it attempts to amend.

Express definition of Congressional intent that the Act be the sole remedy of harborworkers vis-a-vis their employers by reiteration and the rendering of unseaworthiness remedy inapplicable to shore workers[103] would leave only problems of identity and jurisdiction; thus preserving to the longshoreman his negligence action against third parties, yet implementing the class coverage of the Act. Another possible revision could be the elimination of the unseaworthiness doctrine as applied to longshoremen, where the condition was solely caused by the stevedore. Naturally, the injured worker would retain a tort remedy based on negligence, but recovery-over would be greatly modified, and the Act would be revitalized. Perhaps the best solution would be to include the shipowner in the compensation scheme. The owners would, thus, have a fixed, calculable liability and the inequities which have developed would disappear. True, the idea of a compensation remedy is the master-servant relationship,[104] but there exist state statutes imposing compensation liability on general contractors where the employee of a sub-contractor is injured.[105] The contention that such a step would subject the shipowner to hardship is erroneous in view of the existence of the high value remedy now available against them.[106] Whatever the solution, the need exists to accord to the Act the effect intended.

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103 See H.R. 6740 for effectuation of this intent.

"Sec. 197. In any action upon a claim arising under admiralty and maritime law against any ship or vessel of any type, or its owner, agent, or charterer for damages for personal injury to or death of any person, other than a member of the crew of the ship or vessel on which injury occurs, as a result of acts or omissions of the owner, agent, or charterer or any of his officers, agents, servants, employees, contractors, or any crew member of the ship or vessel, or the condition of the ship or vessel, liability of the ship or vessel or its owner, agent, or charterer shall be determined without respect to and shall not in any such case be based upon any warranty of seaworthiness or breach thereof."

104 Crowell v. Benson, supra note 24.

105 Enumerated in 66 Yale L.J. 581, 589 (n. 47) (1957).

106 Id. at 589. The raising of compensation levels might seem to entail more expense for the employer, but present compensation payments are disproportionate to possible tort recoveries, see note 78, supra, hence elimination of the latter from the longshoreman-stevedore-shipowner triangle would reduce allocations for tort suit coverage or protection, producing a surplus which could be used to implement higher compensation benefits. The Act provides for computation of pay. § 910. Compensa-

TAXATION—ADMINISTRATIVE LAW—CONSTRUCTION AND APPLICATION OF INTERNAL REVENUE STATUTE RELATING TO RETROACTIVE EFFECT OF RULINGS AND REGULATIONS.—The recent case of *Wolinsky v. United States*[1] focused attention on the controversial internal revenue statute[2] dealing with the retroactive effect of administrative rulings and regulations as relating to internal revenue laws.

The statute in question,[3] delegates authority to the Commissioner of Internal Revenue to nullify or change a prior ruling or regulation based upon a mistake of law, by issuing a new ruling or regulation having a retroactive application. Taxpayer in the *Wolinsky*[4] case was a manufacturer of automobile seat covers, selling both to private owners and automobile dealers, who was not aware of Internal Revenue Commissioner's private rulings that retail seat cover sales "custom made" to private owners of automobiles were outside the scope of the statute[5] imposing an excise tax on automobile accessories. Thus, the taxpayer paid taxes on all his sales from the commencement of his operations in 1948 until September of 1950 when advised of the private rulings exempting from tax, seat cover sales made to private owners. Wolinsky then filed a claim for refund, and thereafter received a ruling reaffirming the Commissioner's position that only sales to automobile dealers were taxable under the statute.[6] However, a year and a half later, the Treasury Department rejected taxpayer's claim for refund, stating that it had changed its position as embodied in a ruling,[7] wherein the Commissioner decided that all sales of seat covers, whether made to retail customers or to dealers, came within the excise tax statute,[8] and that

tion for disability cannot exceed $54.00 a week. § 906(b); nor, for death benefits, is the average weekly wage of the deceased to be considered more than $81.00. § 909(e). See H.R. 9552—H.R. 9317—Proposed amendment to the Longshoremen's and Harbor Workers' Compensation Act to Increase Benefits and to Provide Penalties for Discrimination, introduced by Rep. Roosevelt (D) of California proposing raising the calculable maximum wage to $121.00. Passage of a higher compensation amendment should be accompanied by an amendment covering inadequacies. E.g. § 910(c): "If either of the foregoing methods of arriving at the average annual earnings of the injured employee cannot reasonably and fairly be applied, such average annual earnings shall be such sum as, having regard to the . . . earnings . . . of other employees of the same or most similar class. . . ." Many longshoremen work at other jobs. If injured, they have not worked a sufficient amount of time to establish an average weekly wage. Hence their compensation will be based on the average wage of another, most likely a steady employee. Payments are designed to compensate for lost time, but the above result shows that the stevedore may be bearing the cost of the lost time of some other occupation, or worse, may be compensating a fraud. Such a method is not realistically consonant with the day-to-day nature of longshore labor.

1 271 F.2d 865 (2d Cir. 1959).
2 68A Stat. 917 (1954), 26 U.S.C. § 7805(b) (1954).
3 Ibid.
4 See note 1, supra.
5 53 Stat. 410 (1939), 26 U.S.C. § 3403(c) (1952). Since 1954 this statute was re-enacted and now is 68A Stat. 481 (1954), 26 U.S.C. § 4061(b) (1958).
6 Ibid.
7 S.T. 944, 1952-2 Cum. Bull. 255.
8 See note 5, supra.

this new ruling was not to be applied retroactively, except to deny refund claims, and then only if the claimant could not show reliance on prior rulings.

The District Court[9] upheld manufacturer's action to recover for the allegedly erroneous excise taxes paid, stating that at the time they were paid, a part of the business was not subject to taxation. The Court of Appeals[10] reversed this decision finding no error in the construction placed upon the manufacturer's excise tax statute[11] by the Treasury Department in its 1952 ruling,[12] holding that all seat cover sales are taxable.[13] But the basis for the court's denial of relief to the taxpayer was founded on the internal revenue statute[14] which permits the Commissioner to issue a new ruling having a retroactive effect, and thus voiding an old ruling which was based on a mistake of law.[15] Relying on this statute the court recognized the right of the Commissioner to modify a ruling retroactively, and found no abuse of discretion on his part,[16] nor any exercise of an arbitrary distinction in limiting the ruling's retroactive effect to refund actions.[17] The court concluded that the claimant could not demonstrate reliance on prior rulings, and in fact found it difficult to understand this provision contained in S.T. 944;[18] for how could one show reliance on rulings that he need not pay taxes, when he is seeking a refund for taxes paid? The *Wolinsky* decision also referred to questions of jurisdiction in tax refund actions, but the important element in the case deals with the court's construction of the retroactive aspect of the statute, which presents interesting questions as to the propriety of retroactive taxation.

9 See note 1, supra at 865, 867.

10 See note 1; supra.

11 See note 5, supra.

12 See note 7, supra.

13 See Masao Hirasuna v. McKenney, 245 F.2d 98, 103 (9th Cir. 1957), holding that all sales of seat covers to automobile dealers are within purview of the excise tax section. See two recent cases upholding the construction placed upon § 3403(c) by the Treasury Department in S.T. 944, United States v. Keeton, 238 F.2d 878 (4th Cir. 1956), cert. denied, 353 U.S. 973, 77 S. Ct. 1056, 1 L. Ed. 2d 1135 (1957); Campbell v. Brown, 245 F.2d 662 (5th Cir. 1957).

14 See note 2, supra.

15 See Automobile Club of Michigan v. Commissioner, 353 U.S. 180, 77 S. Ct. 707, 1 L. Ed. 2d 746 (1957), rehearing denied, 353 U.S. 989, 77 S. Ct. 1279, 1 L. Ed. 2d 1147 (1957). See H.S.D. Co. v. Kavanagh, 191 F.2d 831 (6th Cir. 1951), holding that rulings of the Commissioner approving employee trusts were binding upon a succeeding Commissioner, and could not be revoked by him; Time Oil Co. v. Commissioner, 258 F.2d 237 (9th Cir. 1958), holding that Commissioners of Internal Revenue are bound by acts of prior Commissioners in approving pension plans and allowing tax advantages to employees. The last two cases seem to say that the Commissioner has attempted an improper correction of a mistaken inference of fact as opposed to a proper correction of a mistake of law.

16 See Lesavoy Foundation v. Commissioner, 238 F.2d 589 (3rd Cir. 1956).

17 See Aran v. United States, 259 F.2d 757 (9th Cir. 1958), cert. denied, 358 U.S. 866, 79 S. Ct. 100, 3 L. Ed. 2d 100 (1958), where taxpayer, a manufacturer of a bottle warmer for use in automobiles, who had paid taxes for five years under § 3403(c), received a ruling that sale of these articles was not within that Section, only to have this ruling repudiated ten months later, had his claim for refund disallowed.

18 See note 7, supra.

I. Retroactive Taxation in General

As in the *Wolinsky* case, the usual type of retroactive taxation is in the form of an administrative ruling or regulation which relates back to an internal revenue law. However, a tax statute might also have a retroactive effect, where the language used in the act clearly indicates such a construction,[19] or where the congressional intent is apparent that the tax statute operate retrospectively.[20] Generally, laws are presumed to have a prospective effect in the absence of an express provision to the contrary.[21] Unless such a declaration of intent of retroactivity is embodied in the statute, laws are not to be applied to cases which arose before their enactment.[22]

The fact that a tax statute has a retroactive application is insufficient to render it unconstitutional and invalid as a denial of due process.[23] But the retroactive imposition of a tax may be so arbitrary and capricious as to result in a confiscation, a denial of due process of law and a violation of the Fifth Amendment.[24]

[19] Kentucky Jockey Club v. Lucas, 14 F.2d 539 (W.D. Ky. 1926); Stockdale v. Atlantic Insurance Co., 20 Wall (U.S.) 323, 22 L. Ed. 348 (1874); Brushaber v. Union P.R. Co., 240 U.S. 1, 36 S. Ct. 236, 60 L. Ed. 493 (1916); Tyee Realty Co. v. Anderson, 240 U.S. 115, 36 S. Ct. 281, 60 L. Ed. 554 (1916).

[20] Claridge Apartments Co. v. Commissioner, 323 U.S. 141, 65 S. Ct. 172, 89 L. Ed. 139 (1944), holding that retroactivity even where permissible, is not favored except upon the clearest mandate; Brewster v. Gage, 280 U.S. 327, 50 S. Ct. 115, 74 L. Ed. 457 (1930), stating that ordinarily statutes establish rules for the future, and they will not be applied retrospectively unless that purpose plainly appears; United States v. Magnolia Petroleum Co., 276 U.S. 160, 48 S. Ct. 236, 72 L. Ed. 509 (1928); Lewellyn v. Frick, 268 U.S. 238, 45 S. Ct. 487, 69 L. Ed. 934 (1925).

[21] Hassett v. Welch, 303 U.S. 303, 58 S. Ct. 559, 82 L. Ed. 858 (1938); United States v. Heth, 3 Cranch (U.S.) 399, 2 L. Ed. 479 (1806); Reynolds v. M'Arthur, 2 Pet (U.S.) 417, 7 L. Ed. 470 (1829); Schwab v. Doyle, 258 U.S. 529, 42 S. Ct. 391, 66 L. Ed. 747 (1922); United States v. Magnolia Petroleum Co., 276 U.S. 160, 48 S. Ct. 236, 72 L. Ed. 509 (1928).

[22] Schwab v. Doyle, supra, commenting that the initial admonition is that laws are not to be considered as applying to cases which arose before their passage unless that intention be clearly declared; Erdman v. Martinez, 184 U.S. 578, 22 S. Ct. 515, 46 L. Ed. 697 (1902); White v. United States, 191 U.S. 545, 24 S. Ct. 171, 48 L. Ed. 295 (1903); Gould v. Gould, 245 U.S. 151, 38 S. Ct. 53, 62 L. Ed. 211 (1917).

[23] Fernandez v. Wiener, 326 U.S. 340, 66 S. Ct. 178, 90 L. Ed. 116 (1945), rehearing denied, 327 U.S. 814, 66 S. Ct. 525, 90 L. Ed. 1038 (1946), holding that a retroactive estate tax does not violate the due process clause of the fifth amendment; Milliken v. United States, 283 U.S. 15, 51 S. Ct. 324, 75 L. Ed. 809 (1931), stating that a tax is not necessarily and certainly arbitrary and therefore invalid because retroactively applied, and taxing acts having retroactive features have been upheld in view of the special circumstances disclosed and considered by the court; Brushaber v. Union P.R. Co., 240 U.S. 1, 36 S. Ct. 236, 60 L. Ed. 493 (1916), holding that Income Tax provisions of Tariff Act of 1913 were not unconstitutional by reason of retroactive operation, the period covered not extending prior to the time when the sixteenth amendment was operative, nor do they deny due process of law.

[24] Nichols v. Coolidge, 274 U.S. 531, 47 S. Ct. 710, 71 L. Ed. 1184 (1927), holding that the estate tax statute insofar as it requires that there shall be included in the gross estate of a decedent for purposes of estate taxation, the value of property transferred by decedent prior to its passage, merely because the conveyance was intended to take effect in possession or enjoyment at or after his death, is arbitrary, capricious,

Thus, the essential area of retroactive taxation is found in the field of administrative rulings and regulations as applied to internal revenue statutes. The courts will normally allow the retroactive operation of administrative regulations in the fields of taxation[25] and police regulation,[26] but are reluctant to do so when dealing with contractual rights[27] and rights between private individuals.[28] The question of retroactivity of administrative rulings and regulations in the tax field has been covered in the federal internal revenue statutes since 1921,[29] and is determinative of the scope and extent to which rulings and regulations of the Treasury Department are given retroactive effect. The present statute under the 1954 Internal Revenue Code is section 7805(b),[30] which provides that the Secretary of the Treasury or the Commissioner of Internal Revenue, with approval of the Secretary, "may prescribe the extent if any to which any ruling or regulation, relating to internal revenue laws shall be applied without retroactive effect." It is the proper construction and application of this statute which will govern the propriety of retroactive regulations.

In construing this statute a great deal of weight must be given to the nature of the administrative ruling or regulation.[31] Since regulations are not effective until after a statute has been enacted, the type of regulation dealt with will be determined by the scope given to the statute. If the statute does not express the entire law, but requires the issuance of rulings and regulations in order to implement and carry out the law, the regulation would be deemed a legislative regulation to operate only from the time of its promulgation. If, however, the original statute is declarative of the complete law but is general or ambiguous in its terms, then an administrative ruling or regulation which is designed to interpret the doubtful meaning of

and amounts to confiscation; Blodgett v. Holden, 275 U.S. 142, 48 S. Ct. 105, 72 L. Ed. 206 (1927), deciding that the statute insofar as it undertakes to impose a tax on gifts fully consummated before its provisions taxing gifts came before Congress, is invalid under the due process clause of the fifth amendment.

25 See dissenting opinion of Justice Douglas in Helvering v. Griffiths, 318 U.S. 371, 63 S. Ct. 636, 87 L. Ed. 843 (1943), where in support of the position that retroactive effect should be given to a Treasury Regulation which amended an earlier one, it was pointed out that "every revenue act which Congress has passed has a retroactive effect" this being "something on which taxpayers of necessity take their chances."

26 Speert v. Morgenthau, 73 App. D.C. 70, 116 F.2d 301 (1940).

27 United States v. Macdaniel, 7 Pet (U.S.) 1, 8 L. Ed. 587 (1833).

28 Arizona Grocery Co. v. Atchison, T&S.F.R. Co., 284 U.S. 370, 52 S. Ct. 183, 76 L. Ed. 348 (1932).

29 Act of November 23, 1921, § 1314, 42 Stat. 314 (1921); 44 Stat. 114 (1926), 26 U.S.C. § 1108(a) (1926); 48 Stat. 757 (1934), 26 U.S.C. § 506 (1934); 53 Stat. 467 (1939), 26 U.S.C. § 3791(b) (1952); 68A Stat. 917 (1954), 26 U.S.C. § 7805(b) (1958).

30 See note 2, supra.

31 See Griswold, A Summary of the Regulations Problem, 54 Harvard Law Review 398 (1941); Brown, Regulations, Re-enactment, and the Revenue Acts, 54 Harvard Law Review 377 (1941); Alvord, Treasury Regulations and the Wiltshire Oil Case, 40 Columbia Law Review 252 (1940); Surrey, The Scope and Effect of Treasury Regulations Under the Income, Estate, and Gift Taxes, 88 U. of Pa. Law Review 556 (1940); Paul, Use and Abuse of Tax Regulations in Statutory Construction, 49 Yale Law Journal 660 (1940); Lee, Legislative and Interpretive Regulations, 29 Georgetown Law Journal 1 (1940).

the statute is considered an interpretive regulation, for it prescribes a rule of conduct in itself, and thus necessarily relates back to the statute and is in this sense retroactive.[32]

II. Statute As Affecting "Automatic Retroactivity" of Rulings and Regulations

Where interpretive regulations are involved there is strong support for the principle of automatic retroactivity in that the regulation refers directly back to the statute and is applicable as of the time of its enactment. This view is found in the leading case of *Manhattan General Equipment v. Commissioner*[33] where it was held that departmental regulations and interpretations as to computations of taxable income, on shares of stock received by taxpayer pursuant to a corporate reorganization, might properly correct prior erroneous regulations and interpretations and be applied to transactions before their promulgation, and that the regulation is no more retroactive in its operation than is a judicial determination construing and applying a statute to a case at hand. The court reasoned that the original regulations were inconsistent with the statute and thus could not lawfully be applied, while the amendatory regulations were in accord with the intention of the statute, and did not give rise to an undue retroactive operation because of their effectuation of the proper legislative intent.

On the subject of automatic retroactivity, the court in the *Manhattan* case said:[34]

"The contention that the new regulation is retroactive is without merit. Since the original regulation could not be applied, the amended regulation in effect became the primary and controlling rule in respect of the situation presented. It pointed the way for the first time, for correctly applying the

[32] Helvering v. Reynolds, 313 U.S. 428, 61 S. Ct. 971, 85 L. Ed. 1438 (1941), stating that a transaction consummated between the time statute was created and the time the regulation was issued was subject to the regulation.

[33] 76 F.2d 892 (2d Cir. 1935), affirmed 297 U.S. 129, 56 S. Ct. 397, 80 L. Ed. 528 (1936), rehearing denied, 297 U.S. 728, 56 S. Ct. 587, 80 L. Ed. 1010 (1936).

[34] Id. at 135, 56 S. Ct. at 400, 80 L. Ed. at 531. See dissenting opinion of Circuit Judge Manton at 76 F.2d 900, in which it was said that an internal revenue regulation which is interpretive of the law, rather than declaratory thereof, has in reality no retroactive effect of itself upon the statute in connection with which it was promulgated. A contrary finding was set forth in Larkin v. United States, 78 F.2d 951 (8th Cir. 1935), where without referring to the retroactivity statute under consideration here, the court ruled that a Treasury decision was prospective and not retroactive in its operation, stating that such is the rule in regard to statutes, in the absence of language or surrounding circumstances indicating the contrary. Another case in point, where transactions occurred prior to the earliest retroactivity statute is Shearer v. Anderson, 16 F.2d 995 (2d Cir. 1927), holding that Internal Revenue Regulations construing Internal Revenue provisions are not retroactively applicable to a similar earlier ruling; Accord, Knapp-Monarch Co. v. Commissioner, 139 F.2d 863 (8th Cir. 1944). Upholding the principle of automatic retroactivity is the case of Roger's Inc. v. United States, 163 F. Supp. 225 (W.D. Pa. 1958), reversed on other grounds, 265 F.2d 615 (3rd Cir. 1959), where it was held that a treasury regulation which merely clarifies what the language of the statute always was intended to convey is no more retroactive in its operation than is a judicial determination construing and applying a statute to a case in hand.

antecedent statute to a situation which arose under the statute . . . . The statute defines the rights of the taxpayer and fixes a standard by which such rights are to be measured. The regulation constitutes only a step in the administrative process. It does not, and could not, alter the statute. It is no more retroactive in its operation than is a judicial determination construing and applying a statute to a case at hand."

It would, therefore, seem that Section 7805 of the revenue code, speaking in terms of administrative power to limit retroactivity, does not affect automatic retroactivity. Authority to the contrary is found in the case of *Automobile Club of Michigan v. Commissioner*[35] where the court after referring to Section 3791(b) of the 1939 Code[36] decided that Commissioner had not abused his discretion in making his rulings retroactively applicable to the years 1943 and 1944 in a 1945 revocation of 1934 and 1938 rulings exempting an auto club from federal income taxes based on determination that such clubs are not entitled to an exemption. The court mentioned that it was necessary to determine whether the Commissioner's action concerning the retroactive ruling resulted in an abuse of discretion.

Thus the principle of automatic retroactivity cannot be construed to be as *automatic* as its name implies. True, an interpretive regulation will normally take effect from the time of the enactment of the statute, but this will be governed by the amount of discretion exercised by the Commissioner so as to avoid any inequitable result. An example of abuse of discretion is found in *Lesavoy Foundation v. Commissioner*,[37] where after stating that the statute gives the Commissioner discretionary power to determine the extent of retroactivity in a specific case, with the result that exercise of power making rulings retroactive is not to be interfered with unless it exceeded the bounds of discretion, the court held the Commissioner's discretionary power to make rulings retroactive had been exceeded where a certificate of exemption from taxation granted a taxpayer in 1945 was revoked in 1951 and revocation was made retroactive to 1946, thereby imposing a deficiency on taxpayer. The court ruled that the Commissioner was guilty of abuse of discretion in changing his mind as to the exemption granted to the taxpayer, on the basis that a charitable foundation had departed from its exempt purpose, where individuals representing taxpayer committed no fraud and made no misstatements, and thus resulting in taxpayer being liable for a tax bill so large as to wipe him out of existence.

35 See supra note 15, Automobile Club of Michigan v. Commissioner.

36 See note 29, supra.

37 See note 16, supra. Accord on abuse of discretion is Miller v. Nut Margarine Co., 284 U.S. 498, 52 S. Ct. 260, 76 L. Ed. 422 (1932), where plaintiff made and sold a product not taxable under Oleomargarine Act, in reliance upon determinations by the courts and the commissioner as inapplicable in like cases on assurance from Revenue Bureau that its product wouldn't be taxed. Later the Commissioner changed his ruling and ordered that the tax be enforced against plaintiff's entire product from the beginning. The court held that this would have destroyed the business, ruined the plaintiff, and inflicted great loss, and that the Commissioner's action was not only based on an erroneous interpretation of the statute, but was arbitrary and capricious, and that a suit could be maintained to enjoin the collection.

Thus, Section 7805 has a marked effect on the principle of automatic retroactivity, confirming the Commissioner's authority to correct any rulings or regulations retroactively but limiting any retroactive application to the extent necessary to avoid inequitable results.[38] However, this limitation on retroactivity has been held not to extend to cases where, in the absence of abuse of discretion, taxpayer has relied to his prejudice on the Commissioner's original regulation,[39] although the court may fortify its decision, refusing to permit retroactive operation of amendatory regulations, by pointing out the detriment to the taxpayer resulting from reliance on the original regulation.[40] It has also been recently held that the doctrine of equitable estoppel is no bar to the correction by the Commissioner of a mistake of law by retroactively revoking such a ruling.[41]

III. Effect of Statute Upon Retroactivity of Changes in Rulings or Regulations After Re-enactment of Statute to Which Rulings or Regulations Have Reference

The power vested in the Commissioner under Section 7805 to make rulings and regulations retroactive is severely limited in cases where prior to the administrative revisions congress has re-enacted the statute to which the ruling or regulation has reference thus giving sanction to the existing regulation. The case of *Helvering v. R. J. Reynolds Tobacco Co.*[42] is the leading exponent of this rule denying retroactive operation to amended treasury regulations where the original regulations survived re-enactment of the statute to which they referred.

In the *R. J. Reynolds* case a treasury regulation was issued as a proper interpretation of a revenue act deciding that gain accruing to a corporation as a result of purchase and resale of its own stock did not constitute gross income for income tax purposes, and that the regulation was given the force of law by re-enactment of the revenue statute without change, so that

38 Recognition by court that § 7805 authorizes the Commissioner to limit the retroactivity of internal revenue regulations appears in Commissioner v. Fisher, 150 F.2d 198 (6th Cir. 1945), reversed on other grounds, 327 U.S. 512, 66 S. Ct. 686, 90 L. Ed. 818 (1946); Ayer v. Blair, 58 App. D.C. 110, 25 F.2d 534 (1928). See dissenting opinion of Circuit Judge Manton in Manhattan General Equipment v. Commissioner at 76 F.2d 899, where it was said that the retroactivity statute vested internal revenue authorities not with discretion to apply a regulation with retroactive effect, but with discretion to apply it without such effect. See Helvering v. Griffiths, note 25, supra, noting that the retroactivity statute does not increase the power of the Treasury to make retroactive rulings.

39 Goldfield Consol. Mines Co. v. Scott, 247 U.S. 126, 38 S. Ct. 465, 62 L. Ed. 1022 (1918), where a Regulation of the Treasury Department dealing with the cost value of property at the beginning of the tax period, which was clearly erroneous under previous decisions of U.S. Supreme Court, was held not to preclude taxation under correct principles of law, as laid down in previous court decisions.

40 See Helvering v. Griffiths, note 25, supra.

41 See supra note 15, Automobile Club of Michigan v. Commissioner, disapproving Stockstrom v. Commissioner, 88 App. D.C. 286, 190 F.2d 283 (1951).

42 306 U.S. 110, 59 S. Ct. 423, 83 L. Ed. 536 (1939).

a subsequent treasury regulation taking the opposite position was inapplicable to past transactions. The court in amplifying this reasoning said:[43]

"Since the legislative approval of existing regulations by re-enactment of the statutory provision to which they appertain gives such regulations the force of law, we think that Congress didn't intend to repeal the rule of law that existed during the period for which the tax is imposed."

Thus, the basis for this re-enactment rule denying retroactive operation to administrative construction in this area is that these long standing regulations which remain in force after the statute to which they refer is re-enacted, are given the force of law. Such was the rule laid down in *Helvering v. Winmill*[44] where the court commented:[45]

"Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially re-enacted statutes are deemed to have received congressional approval and have the effect of law."

The scope of this re-enactment rule does not extend to the limitation on the rule making authority as regards future action. This was the holding in *American Chicle Co. v. U.S.*[46] where an antecedent administrative interpretation of the federal revenue act did not render it impossible, after statutory provision in question had been re-enacted without change, for the Commissioner to promulgate a regulation changing for the future, the earlier practice, where the new regulation complied with the meaning of the statute. Thus, the court in *Helvering v. Wiltshire Oil Co.*[47] stated:[48]

"The oft-repeated statement that administrative construction receives legislative approval by re-enactment of a statutory provision, without material change covers the situation where the validity of administrative action standing by itself may be dubious or where ambiguities in a statute or rules are resolved by reference to administrative practice prior to re-enactment of a statute; and where it does not appear that the rule or practice has been changed by the administrative agency through exercise of its continuing rule-making power. It does not mean that a regulation interpreting a provision of one act becomes frozen into another act merely by re-enactment of that provision, so that administrative interpretation cannot be changed prospectively through exercise of appropriate rule making powers."

Added impetus for the re-enactment rule denying retroactive operation is found in *Helvering v. Reynolds*,[49] which upheld the retroactive operation

43 Id. at 116, 59 S. Ct. at 426, 83 L. Ed. at 542.
44 305 U.S. 79, 59 S. Ct. 45, 83 L. Ed. 52 (1938).
45 Id. at 83, 59 S. Ct. at 46, 83 L. Ed. at 55.
46 316 U.S. 450, 62 S. Ct. 1144, 86 L. Ed. 1591 (1942).
47 308 U.S. 90, 60 S. Ct. 18, 84 L. Ed. 101 (1939), rehearing denied, 308 U.S. 638, 60 S. Ct. 292, 84 L. Ed. 530 (1939).
48 Id. at 100, 60 S. Ct. at 24, 84 L. Ed. at 107. Cf. Morrissey v. Commissioner, 296 U.S. 344, 56 S. Ct. 289, 80 L. Ed. 263 (1935); United States v. Dakota-Montana Oil Co., 288 U.S. 459, 53 S. Ct. 435, 77 L. Ed. 893 (1933).
49 See note 32, supra.

of an interpretive regulation. In the *Reynolds* case a Treasury regulation was promulgated in 1935 pursuant to the 1934 Revenue Act which included contingent remainders in the rule that the date of acquisition of property by bequest, devise, or inheritance, is the date of decedent's death for purposes of ascertaining gain or loss on sale of property acquired in such manner, and the court held that the regulation did not infringe any vested right where it was applied in the case of a sale made in 1934 applicable to the 1934 Revenue Act even though the treasury regulation was not yet promulgated. The fact that the regulation was not issued until after the transaction in question had been consummated was considered immaterial by the court in light of the retroactive applicability of the interpretive regulation to the 1934 statute at hand. To this point, it is clear that a regulation cannot be applied to transactions which occurred before the effective date of the statute which the regulation is designed to implement, where the statute itself is not retroactive.[50] Thus, in the *Reynolds* case, the court recognized the validity of the interpretive regulation as applied retroactively, but even more important as related to the denial of retroactive operation in the re-enactment area, the court in the *Reynolds* case qualified the *R. J. Reynolds Tobacco* case and distinguished it from their case on the ground that:[51]

> "The transactions there in question took place at a time when a regulation was in force which expressly negatived any tax liability. The regulation remained outstanding for a long time and was followed by several re-enactments of the statute. About five years after the transactions in question took place the prior regulation was amended so as to impose a tax liability. There are no such circumstances here."

Thus, the court in the *Reynolds* decision was aware of the rule of law set down in the *R. J. Reynolds Tobacco* case which limited retroactive operation of regulations in the area of re-enactment, but pointed out that the circumstances were different, for the regulations in question had not survived statutory re-enactment, and therefore held that the retroactive effect given to the regulation was proper and equitable.

There has been much authority in case law to the effect that retroactive operation of regulations is prohibited in the re-enactment field,[52] and this

[50] Commissioner of Internal Revenue v. Commodore, 135 F.2d 89 (6th Cir. 1943).

[51] See note 32, supra at 432, 61 S. Ct. at 974, 85 L. Ed. at 1441.

[52] See Aluminum Co. v. United States, 123 F.2d 615 (3rd Cir. 1941), declaring that whatever validity and effect the change in administrative enforcement of the statute permitting a domestic corporation which receives dividends from a foreign subsidiary to claim credit for taxes paid by subsidiary, may have had and has prospectively, it cannot operate retroactively where an earlier well established administrative practice recurrently received implied congressional approval by re-enactment of the statute without substantial change; Rasquin v. Humphreys, 308 U.S. 54, 60 S. Ct. 60, 84 L. Ed. 77 (1939), holding that an amended treasury regulation providing that a gift becomes complete and subject to federal gift tax when donor has so parted with dominion and control as to leave in him no power to cause the beneficial title to be revested in himself is whatever validity it may have when applied prospectively so plainly in conflict with terms of the statute imposing the tax as to preclude its application retroactively to trust created before its promulgation; Commissioner v. Monarch, 114 F.2d 314 (1st Cir. 1940),

position is most cogently expressed in the case of *Helvering v. Griffiths.*[53] In the *Griffiths* case the Treasury Department amended its regulation governing taxation of stock dividends and struck out the clause which expressly exempted these transactions from income tax. The original regulation was enacted in recognition of *Eisner v. Macomber,*[54] which held that a dividend in common stock, paid on common stock, constitutes no income, as the term was used in the Sixteenth Amendment of the Federal Constitution. The court ruled that the Treasury Department was without power to give the amended regulation retroactive effect to the prejudice of a stockholder previously receiving a stock dividend, where the statute under which the regulation was adopted was re-enacted while the original regulation was in force, and Congress was in complete accord with the Treasury regulation as originally promulgated. Holding that, as ruled in the original regulation, the transaction was not subject to income tax, the court said:[55]

"We are asked to make a retroactive holding that for some seven years past a multitude of transactions have been taxable although there was no source of law from which the most cautious taxpayer could have learned of the liability. If he consulted the decisions of this court, he learned that no such tax could be imposed; if he read the Delphic language of the Act in connection with existing decisions, it, too, assured him there was no intent to tax; if he followed the Congressional proceedings and debates, his understanding of nontaxability would be confirmed; if he asked the tax collector himself, he was bound by the Regulations of the Treasury to advise that no such liability existed. It would be a pity if taxpayer could not rely on this concurrent assurance from all three branches of government."

As expressed in the opinion, the main basis for the court's decision was that the earlier rather than the amended regulation was thought by the court to be in agreement with the legislative intent as expressed in the pertinent Revenue Act.

commenting that where administrative practice supporting taxpayer's interpretation of statute was for thirteen years, the Commissioner wouldn't be permitted to apply retroactively against the taxpayer any new regulation made after the tax year in question particularly after congressional re-enactment under regulations establishing such administrative practice; Guggenheim v. Rasquin, 28 F. Supp. 322 (E.D.N.Y. 1939), deciding that where the Treasury Department has acted for years under an express interpretation of gift tax and Congress has implicitly accepted such interpretation by re-enacting the same statute, a new interpretation by Treasury Department shouldn't have retroactive effect, without a showing of congressional authority; McCaughn v. Hershey Chocolate Co., 283 U.S. 488, 51 S. Ct. 510, 75 L. Ed. 1183 (1931), where it was said that "The re-enactment of the statute by Congress, as well as the failure to amend it in the face of the consistent administrative construction, is at least persuasive of a legislative recognition and approval of the statute as construed"; Jones v. Magruder, 42 F. Supp. 193 (D. Md. 1941), the court citing § 3791(b) stated that it was doubtful whether revised internal revenue regulations could properly be given retroactive effect, in view of the fact that prior to the revision Congress had repeatedly re-enacted the statute to which the regulation had reference; Lang v. Commissioner, 304 U.S. 264, 58 S. Ct. 880, 82 L. Ed. 1331 (1938); Cammarano v. United States, 358 U.S. 498, 79 S. Ct. 524, 3 L. Ed. 2d 462 (1959).

[53] See note 25, supra.

[54] 252 U.S. 189, 40 S. Ct. 189, 64 L. Ed. 521 (1920).

[55] See note 25, supra at 402, 63 S. Ct. at 652, 87 L. Ed. at 863.

The bulk of the cases limiting retroactive operation in the re-enactment area deal with regulations which are given the force of law. This is normally the case, because any rulings issued, which are consistent with the intention of the statute to which they relate, will later be incorporated into a regulation, and then when the statute is repeatedly re-enacted, any amended regulations will be precluded from having a retroactive effect. But when dealing solely with rulings, a recent case has held that the so-called re-enactment doctrine is more properly applied to regulations which have the force of law rather than to rulings of the Internal Revenue Commissioner.[56] Another case has held that interpretive rulings on the regulations do not have the force and effect of Treasury decisions.[57] Authority for the proposition that the re-enactment doctrine does not apply to rulings is found in the case of *Automobile Club of Michigan v. Commissioner*,[58] which was cited earlier as the basis for the Revenue Commissioner's necessary exercise of permissible discretion in making rulings and regulations retroactive, so as to avoid any inequitable results. The *Automobile Club* case upheld a ruling which was given a retroactive application, on the theory that whatever force be given to a regulation by re-enactment of the statute to which the regulation refers is immaterial to the question of whether a change in a ruling might be retoactively applied. On this line of thinking, there is the general feeling that rulings have no more binding or legal force than an opinion of another lawyer.[59]

IV. Conclusion

Section 7805 of the 1954 Internal Revenue Code which prescribes the extent to which any ruling or regulation, relating back to an internal revenue law, shall be applied without retroactive effect, has been broadly construed and applied by the courts in permitting the Commissioner to enact rulings and regulations with a retroactive effect. The Commissioner, when dealing with legislative regulations, which by their nature are designed to supplement, by filling in details of a statute which by its terms refers to administrative action as necessary to complete the rules of conduct sought to be prescribed, will make changes only prospectively so that the legislative ruling or regulation will operate only from the time of its promulgation. The general application of Section 7805 is in the area of interpretive rulings or regulations which prescribe a rule of conduct in themselves, and relate back to an internal revenue statute, and in that sense are automatically retroactive. The Commissioner's retroactive revocation of prior rulings or regulations in this area cannot be disturbed unless he abused the discretion given him by Section 7805, so as to result in an inequity.

The other major limitation on the retroactive effect of regulations under Section 7805 is in the area of amendments to valid Treasury regula-

56 Kaiser v. United States, 262 F.2d 367 (7th Cir. 1958), cert. granted, 359 U.S. 1010, 79 S. Ct. 1150, 3 L. Ed. 2d 1035 (1959).

57 Bartels v. Birmingham, 332 U.S. 126, 132, 67 S. Ct. 1547, 91 L. Ed. 1947 (1947).

58 See supra note 15, Automobile Club of Michigan v. Commissioner.

59 United States v. Bennett, 186 F.2d 407, 410 (5th Cir. 1951).

tions which have survived re-enactment of the statute to which they refer. These amendments subsequent to re-enactment of the statute are allowed only prospective operation, but this re-enactment doctrine does not extend to rulings which do not have the force of law, and such rulings, therefore, can have a retroactive operation despite repeated statutory re-enactment.

Thus, Section 7805 of the Internal Revenue Code will continue to permit retroactive operation of rulings and regulations when the above requirements are met, and limitations are absent. It appears, however, that the overriding rationale for allowing retroactive operation of rulings and regulations is governed by whether or not the amended regulation reflects the correct point of law as embodied in the statute to which it refers and, thus, is indicative of the proper congressional and legislative intent. A.H.M.

TAXATION—EVASION AND AVOIDANCE—CRIMINAL AND CIVIL LIABILITY.— To one not familiar with our laws of income taxation the terms "tax avoidance" and "tax evasion" have no apparent difference in meaning. However, the distinction holds a great deal of significance for students of taxation. It has been facetiously suggested among the latter that the difference between avoidance and evasion can mean five years in federal penitentiary. In a crude manner, this illustrates a fundamental distinction between avoidance and evasion. Avoidance is legal and evasion is criminal in nature. Tax avoidance is recognized as a valid positive approach to our system of taxation. Large corporations and respected citizens have competent professional assistance on a retainer basis, for the sole purpose of reducing tax liability by methods which do not illegally overcome our tax laws, but rather use such laws to the taxpayer's advantage.

In *Gregory v. Helvering*[1] the Supreme Court spoke in classic terms of tax avoidance as "the legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them by means which the law permits. . . ."[2] It has also been suggested that "conduct in escaping taxation by methods permitted by law is not illegal and is not properly speaking evasion".[3] However, although a taxpayer has the right to minimize or avoid taxes by any legal means, transactions actuated by such a motive will be scrutinized carefully and, in determining their validity, form will be disregarded in favor of substance,[4] when the legal form in which it is cast is a device to evade the just share of tax burden.[5]

1 Gregory v. Helvering, 293 U.S. 465, 55 S. Ct. 266, 79 L. Ed. 596 (1935).

2 Superior Oil Co. v. Mississippi, 280 U.S. 390, 395-396, 50 S. Ct. 169, 174, 74 L. Ed. 504, 508 (1930); United States v. Isham, 17 Wall 496 (1871); Jones v. Helvering, 71 F.2d 214, 217 (4th Cir. 1934).

3 15 Words and Phrases 781 (Permanent Edition).

4 Higgins v. Smith, 308 U.S. 473, 60 S. Ct. 355, 84 L. Ed. 406 (1940); Titus v. United States, 150 F.2d 508 (10th Cir. 1945).

5 Anderson v. Commissioner, 164 F.2nd 870 (7th Cir. 1947); Fred Smith Entertainment Co. v. Commissioner, 167 F.2nd 356 (6th Cir. 1948); Wall v. United States, 164 F.2d 462 (5th Cir. 1954); Hansan v. Birmingham, 190 F.2d 206 (8th Cir. 1951); Cold Metal Co. v. Commissioner, 247 F.2d 864 (6th Cir. 1957); Roscoe v. Commissioner, 215 F.2d 478 (5th Cir. 1954).

Where an individual taxpayer attempted to manipulate two corporate entities for the sole purpose of reducing personal tax liability, the Supreme Court agreed with the Commissioner and held that, although the plan conformed to the statute's provisions, there was obviously no compliance with its intent.[6] However, in *Commissioner v. Eldridge*,[7] taxpayer purchased shares of stock in a rising market; when the market broke in 1929, taxpayer sold the shares to a corporation owned by himself, organized solely for the purpose of distributing automobiles, and thereby gained the benefit of a loss deduction,[8] while constructively maintaining the same market position. The Commissioner's plea to have the corporate entity done away with was denied since taxpayer's intention was to effectuate a valid sale. In another case[9] the Court allowed the partnership tax treatment on a transfer of property from the corporation when the defendant proved a valid purpose for such partnership. The Court held that mere purpose to avoid tax by transfer of property does not in itself vitiate the transaction for tax purposes, the test being whether the transaction under scrutiny is in fact what it appears to be in form. In still another case,[10] a trust amendment created three trusts instead of one. The Court allowed the amendment, regarding as immaterial the government's contention that the plain purpose of the amendment was to lower the tax bracket.

Evasion on the other hand is illegal. Congress has enacted severe measures and allows the Internal Revenue Service wide latitude in stamping out evasion. Evasion has been defined as "an act of eluding or avoiding or avoidance by artifice".[11] As can readily be seen the word "artifice" used in the above definition of evasion is of great significance since this word alone distinguishes evasion from avoidance. Artifice implies a contrivance or device of some kind and may even correspond with trickery or fraud.[12] It also imputes craftiness and deceit and imports some element of moral obliquity.[13]

The government may, as the nature and extent of the evasive act indicates, impose civil penalties, or refer the case to the Department of Justice for criminal prosecution. However, in *Helvering v. Mitchell*,[14] the Court said that invocation of one sanction does not exclude resort to the other. The revenue statutes contain very drastic penalties as enforcement provisions. Such penalties are divisible into two principal categories:

6 See note 1, supra.

7 Commissioner v. Eldridge, 79 F.2d 629 (9th Cir. 1935); Accord, Jones v. Helvering, 71 F.2d 214 (5th Cir. 1934).

8 This type loss deduction is no longer permitted under Int. Rev. Code of 1954, Section 267(b)(2).

9 Chisholm v. Commissioner, 78 F.2d 14 (2d Cir. 1935).

10 Commissioner v. McIlvaine, 78 F.2d 787 (7th Cir. 1935).

11 Black, Law Dictionary (4th Ed. 1951).

12 United States v. Corlin, 44 F. Supp. 940, 943 (S.D. Cal. 1942).

13 Finch v. Gibson, 140 Tenn. 134, 203 S.W. 759 (1918).

14 Helvering v. Mitchell, 303 U.S. 391, 58 S. Ct. 630, 80 L. Ed. 917 (1938); Hanby v. Commissioner, 67 F.2d 125 (4th Cir. 1933). In fact proof of conviction may be sufficient evidence to sustain the imposition of the 50% fraud penalty.

a. Specific Penalties, consisting of fines with maximum limits and imprisonment, and
b. *Ad Valorem* Penalties, measured by a percentage of the tax liability.

An *ad valorem* penalty, which is civil in nature, may be determined and assessed by the Treasury; but specific penalties, which are criminal in nature, cannot be so assessed and are enforceable only by a suit and prosecution in the federal courts.[15]

The largest single deterrent in the government's arsonal of civil penalties is the *ad valorem* 50% fraud penalty. The statute governing this reads in pertinent part:

"If any part of any deficiency is due to fraud with an intent to evade tax, then 50 per centum of the total amount of the deficiency (in addition to such deficiency) shall be so assessed, collected and paid. . . ."[16]

This penalty is imposed in the following manner. Assume taxpayer filed a return showing tax liability of $10,000, and subsequently the Internal Revenue Service examined this return and established that $20,000 in additional taxes was owing the government. Taxpayer's total liability for that year aside from the tax paid would be $30,000, which includes the $20,000 deficiency and the 50% fraud penalty of $10,000.

The possible sources of fraud in income tax cases are obviously limitless; ingenuity of the taxpayer plus complexity of the statutes add up to a very comprehensive field for evasion. To warrant the addition of a civil fraud penalty, taxpayer must have engaged in an act of intentional wrongdoing with the specific purpose of evading a tax believed to be owing.[17] All the facts and circumstances surrounding the conduct of the taxpayer's business must be considered, including all the facts incident to the preparation of the alleged fraudulent return.[18] A conclusion must be reached not on isolated testimony but upon the whole record.[19]

Although it is impossible to state a general definition of the term "fraud", it is feasible to consider some factors which are taken into consideration in determining whether fraud has been committed. Negligence whether slight or great is not the equivalent of fraud with intent to evade tax.[20] But the consistent failure to report substantial amounts of income over a number of years, standing alone, is effective evidence of fraudulent

[15] Treas. Reg. III, Section 29.145-1; Treas. Reg. 103 Section 19.145-1; Treas. Reg. 101.94 Art. 145-1; Ledbetter v. Bailey, 274 Fed. 375 (1921).

[16] Int. Rev. Code of 1939, Section 293(b).

[17] Mitchell v. Commissioner, 118 F.2d 308, 310 (5th Cir. 1941); Wiseley v. Commissioner, 185 F.2d 263, 266 (6th Cir. 1950); Powell v. Granquist, 252 F.2d 56.60 (9th Cir. 1958); Ries v. United States, 172 F. Supp. 929 (E.D. Pa. 1959).

[18] A. Brigham Rose, Tax Ct. Mem. Op., Dkt. 5138 (1949) Aff'd per curiam 188 F.2d 355 (9th Cir. 1951); Geo. Discos, Tax Ct. Mem. Op., Dkt. 25323 (1951).

[19] Stewart S. Freedman, Tax Ct. Mem. Op., Dkt. 30470 (1952); David E. Ringler, Tax Ct. Mem. Op., Dkt. 32284 (1952).

[20] Goldberg v. Commissioner, 239 F.2d 316, 321 (5th Cir. 1956); Fairchild v. United States, 240 F.2d 944, 947 (5th Cir. 1957); Eagle v. Commissioner, 242 F.2d 635, 638 (5th Cir. 1957); Jones v. Commissioner, 259 F.2d 300 (5th Cir. 1958); Carter v. Campbell, 264 F.2d 930 (5th Cir. 1959).

intent.[21] Hence, defendant was convicted of understating income to the extent of $200,000 over a five-year period.[22] Ignorance, error of law, or inefficiency coupled with ignorance have not been held to constitute fraud.[23] However, failure to disclose income because it might embarrass the taxpayer and others by reason of admitting a fraudulent transaction is not considered a valid excuse for failure to report such income.[24] Lax record keeping does not necessarily indicate fraud.[25] However, large understatements of income will be considered fraudulent, unless something more than mere carelessness is offered in defense.[26] The taxpayer's intelligence should be considered by the Court;[27] but, in addition, the defendant's lack of accounting and bookkeeping procedures should also be evaluated by the Court.[28] Such matters as disappearance of records and torn pages give rise to suspicions of fraud, although such doubts may be explained away.[29] Also, manipulations of inventories by a corporate officer, designed to conceal taxable income constitute fraud.[30] Unexplained bank balances are also a strong indication of fraud.[31]

The Commissioner regards the income tax return as one entity when the fraud penalty is invoked, and there are no provisions for dividing a deficiency into segments and atributing part thereof to the taxpayer's negligence and part to fraud. The entire deficiency will be considered fraudulent and the 50% penalty applied thereto when fraud is proven.[32]

Unlike a taxpayer's suit for refund of deficiency, where the findings of the Commissioner have *prima facie* validity,[33] and where the burden of overcoming the presumption is shifted to the taxpayer,[34] when the Commissioner brings an action to impose the fraud penalty, the government never gets the benefit of a presumption of fraud,[35] but must establish the fraud by clear and convincing evidence.[36]

Where the case involves a deficiency and a civil fraud penalty, each party has its own burden of proof. The result, as was pointed out in *Snell*

21 Schwarzkopk v. Commissioner, 246 F.2d 731, 734 (3d Cir. 1957).

22 Ibid.

23 Mitchell v. Commissioner, 118 F.2d (5th Cir. 1941); Kenneth Blanchard, Tax Ct. Mem. Op., Dkt. 24010 (1953).

24 Abe Wolkowitz, Tax Ct. Mem. Op., Dkt. 15249 (1949); Alvin S. Loeb, Tax Ct. Mem. Op., Dkt. 21935 (1951).

25 D. H. Willey Lumber Co., Tax Ct. Mem. Op., Dkt. 10864 (1948); Aff'd 177 F.2d 200 (6th Cir. 1949).

26 E. J. Adams, Tax Ct. Mem. Op., Dkt. 15264 (1948).

27 Louis Halle, 7 T.C. No. 245 (1949); Aff'd 175 F.2d 500 (2d Cir. 1949).

28 See note 25, supra.

29 Lillian Kilpatrick, 22 T.C. No. 446 (1954).

30 Jacksonville Paper Co., Tax Ct. Mem. Op., Dkt. 116 (1954).

31 Martin T. Manton, Tax Ct. Op., Dkt. 18455 (1950).

32 Richardson v. Commissioner, 264 F.2d 400 (4th Cir. 1959).

33 Holland v. United States, 348 U.S. 121, 75 S. Ct. 127, 99 L. Ed. 150 (1954).

34 Goldberg v. Commissioner, 239 F.2d 316 (5th Cir. 1936); Kashat v. Commissioner, 229 F.2d 282 (6th Cir. 1956); Halle v. Commissioner, 175 F.2d 500 (2d Cir. 1949).

35 Int. Rev. Code of 1954, section 7454, ". . . the burden of proof in respect of such issue shall be upon the Commissioner. . . ."

36 Valetti v. Commissioner, 260 F.2d 185, 188 (3d Cir. 1958); Commissioner v. Rubinstein, 264 F.2d 478 (3d Cir. 1959).

Isle Inc. v. Commissioner,[37] may end in a stand off from failure of either party to establish its burden of proof.[38] The fact that there is a deficiency, does not alone create a presumption of fraud.[39]

Another civil penalty which the Commissioner may use in enforcing the tax laws is the 25%[40] *ad valorem* penalty for failure to file a timely return. However when such failure to file is due to reasonable cause and not willful neglect the penalty is not imposed. The Internal Revenue Code also imposes a 5% *ad valorem* penalty[41] when any part of a deficiency is due to negligence, or intentional disregard of rules and regulations, but without intent to defraud.

While the *ad valorem* penalties are most frequently resorted to in the administration of income tax laws, Congress has seen fit to prescribe several specific or personal penalties of a criminal character, consisting of fines and imprisonment.[42] These sections provide in pertinent part that:

a. Any person who *willfully* fails to pay such estimated tax, make such return or declaration, keep such records or supply such information required by law or regulations, shall be guilty of a misdemeanor and upon conviction thereof be fined not more than $10,000 or imprisoned for not more than one year, or both, together with the costs of prosecution.[43]

b. Any person who *willfully* attempts in any manner to evade or defeat any tax, shall in addition to other penalties, be guilty of a felony and upon conviction thereof, be fined not more than $10,000 or imprisoned for not more than five years, or both, together with the costs of prosecution.[44]

A willful violation is requisite under both paragraphs (a) and (b).[45] In *Hargrove v. United States*,[46] the Court said, "Where a statute simply denounces doing of an act as criminal, especially in offenses *mala prohibita*, the law imputes intent; but where the statute denounces as criminal, only its 'willful' doing, specific wrongful intent, that is, actual knowledge of the existence of an obligation and a wrongful intent to evade it, is of the essence".[47] Willfullness is more than mere knowledge and intentional failure to pay the tax; some element of evil motive and want of justification in view of all the financial circumstances of the taxpayer is required to sustain

37 Snell Isle Inc. v. Commissioner, 90 F.2d 481 (5th Cir. 1937).
38 Drieborg v. Commissioner, 225 F.2d 216, 218 (6th Cir. 1955).
39 Olinger v. Commissioner, 234 F.2d 823 (5th Cir. 1956).
40 Int. Rev. Code of 1939, Section 291(a).
41 Int. Rev. Code of 1939, Section 293(a).
42 Int. Rev. Code of 1939, Section 145(a); Int. Rev. Code of 1939, Section 145(b).
43 Int. Rev. Code of 1939, Section 145(a).
44 Int. Rev. Code of 1939, Section 145(b).
45 See note 42, supra.
46 Hargrove v. United States, 67 F.2d (7th Cir. 1935).
47 Potter v. United States, 155 U.S. 438, 15 S. Ct. 144, 39 L. Ed. 214 (1894); Felton v. United States, 96 U.S. 699, 24 L. Ed. 875 (1878); Spurr v. United States, 174 U.S. 728, 19 S. Ct. 812, 43 L. Ed. 1150 (1899); Foster v. United States, 256 Fed. 207 (5th Cir. 1919); Bentall v. United States, 256 Fed. 744 (8th Cir. 1919);

a conviction.[48] Such willfullness may be inferred from conduct such as keeping a double set of books, making false entries or alterations, or false invoices or documents, destruction of books or records, concealment of assets or covering up sources of income, handling of one's affairs so as to avoid making the records usual in transactions of the same kind, and any conduct the likely effect of which would be to mislead or conceal.[49] In *United States v. Rosenblum*,[50] the defendants made huge profits from the sale of whiskey above ceiling prices. Defendants subsequently admitted knowing that such profits should have been included in income. The Court held that a deliberate falsification was of itself sufficient to sustain a charge under 145 (b).[51] In another case,[52] the president of a corporation, who owned all of its stock, deposited checks made payable to the corporation, for sales, into his personal account, and when preparing both individual and corporate returns, no mention was made of such checks on either of the returns. The Court refused defendant's appeal and stated that the only reasonable interpretation of defendant's activities could be that of willful evasion. However, in *Bahjes v. United States*,[53] the defendant who deposited the proceeds of large gravel sales belonging to the corporation, into his own private brokerage account was not convicted. The Court reasoned that when one has a bona fide misconception of the law, regardless of the presumption that ignorance of the law will not excuse, the act will not result in criminal liability. The statute[54] is applicable only where there is the element of willfulness. The government's exercise of Section 145(a)[55] is well illustrated by the *Palermo* case.[56] The defendant earned a large income and filed a true return. However, he had an obstinate attitude toward paying taxes. The District Court convicted him, reasoning that this was a willfull refusal to pay, since Palermo did file a timely return, had ample cash to pay his tax liability, and enjoyed many luxuries which he could have chosen second to his tax bills.

As in other cases, the guilt of a defendant in criminal tax proceedings must be established beyond a reasonable doubt, though not a mathematical certainty.[57] In the recent case of *United States v. Bridell*,[58] the president and principal stockholder was acquitted on charges of willfully evading

O'Brien v. United States, 51 F.2d 193 (7th Cir. 1931); United States v. Praeger, 149 Fed. 474 (W.D. Tex. 1907).

48 Spies v. United States, 317 U.S. 492, 63 S. Ct. 364, 87 L. Ed. 418 (1942); United States v. Glascott, 216 F.2d 487 (7th Cir. 1954); United States v. Palermo, 157 F. Supp. 578 (E.D. Pa. 1957).

49 Spies v. United States, 317 U.S. 492, 63 S. Ct. 304, 87 L. Ed. 418 (1942).

50 United States v. Rosenblum, 176 F.2d 321 (7th Cir. 1949).

51 See note 44, supra.

52 Currier v. United States, 166 F.2d 346 (1st Cir. 1948).

53 Bahjes v. United States, 172 F.2d 1 (6th Cir. 1949).

54 See note 44, supra.

55 See note 43, supra.

56 United States v. Palermo, 157 F. Supp. 578 (E.D. Pa. 1957).

57 Holland v. United States, 348 U.S. 121, 75 S. Ct. 127, 99 L. Ed. 150 (1954); Linquata v. United States, 173 F.2d 201 (1st Cir. 1949).

58 United States v. Bridell, 60-1 U.S.T.C. (C.C.H.) (1960).

income taxes under Section 145 (b).[59] The defendant paid the salaries of his caretaker and maintenance man, outside laborers, and cook-housekeeper, all employed at his home and charged these payments on the books of the corporation as business expenses. Similar treatment was given payments by the corporation for a yacht, and Miami Beach, Florida, properties used by the president and his family for entertainment of their personal friends. The defendant prevailed since the government could not prove beyond a reasonable doubt that taxpayer did not truly believe that these expenditures were not valid expenses of the corporation.

The government may gather evidence and present its case based on either one or both[60] of the following methods:

1. Specific items of unreported income. The government acquires such information via the Bureau's normal auditing procedure, and also by using informants to whom the Commissioner is authorized to pay up to 10% of any tax, penalty, and interest collected from such delinquent taxpayers.[61]

2. The Net Worth Method. The net worth method can best be termed a formula for deriving taxable income when inadequate or no records at all are kept by the taxpayer. In a typical net worth prosecution the government, having concluded that the taxpayer's records are inadequate as a basis for determining income tax liability, attempts to establish an "opening net worth" or total net value of the taxpayer's assets at the beginning of a given year. It then attempts to prove increases in the taxpayer's net worth for each succeeding year during the period under review and calculates the difference between the adjusted net values of the taxpayer's assets at the beginning and end of each of the years involved. The non-deductible expenditures, including living expenses, are added to these increases, and if the resulting figure for any year is substantially greater than the taxable income reported by the taxpayer for such year, the government claims the excess represents unreported taxable income. In addition, the government asks the jury to infer willfulness from this understatement, when taken in connection with direct evidence of "conduct the likely effect of which would be to mislead or conceal".[62] The net worth method operates in the following manner. Assume that the government establishes taxpayer's net worth to be $15,000 as of the given year in question. The government then uncovers assets amounting to $40,000 in hidden bank accounts and safe deposit boxes, thus increasing the starting net worth to $55,000. Furthermore, the government adds to this figure the value of furs, automobiles and homes purchased during this period, of let's assume $20,000, plus reasonable living expenses of $5,000. The resultant net worth at the end of the period would be $80,000, from which a reasonable closing net worth of $20,000 is deducted leaving taxable income of $60,000 which had not been reported, and is subject to deficiency judgment, penalties and interest.

[59] See note 44, supra.

[60] Keenan v. United States, 267 F.2d 118 (7th Cir. 1959), stands for principle that both methods used together are not prejudicial.

[61] This procedure is authorized by T.D. 5183 (1942).

[62] See note 49, supra.

Although the government deems the net worth method useful in the enforcement of criminal sanctions, careful study indicates that the method is so fraught with danger for the innocent that close scrutiny must be given its use.

One basic assumption in establishing guilt by this procedure is that most assets derive from a taxable source, and that when this is not so, the taxpayer can easily explain away the discrepancy. The application of such an assumption raises serious legal problems in the administration of criminal law. Unlike civil actions, the prosecution must always prove guilt beyond a reasonable doubt. This has led many of our courts to be disturbed by the use of the net worth method, particularly in the scope and the latitude which it allows prosecutors.[63] But the net worth method has not grown up overnight. It was first utilized in such cases as *Capone v. United States*,[64] and *Guzik v. United States*,[65] to corroborate direct proof of specific unreported income. In *United States v. Johnson*,[66] the Court approved its use to support the inference that taxpayer, owner of a vast and elaborately concealed network of gambling houses upon which he declared no income, had indeed received unreported income in a "substantial amount". It was a potent weapon in establishing taxable income from undisclosed sources when all other efforts failed. Since the *Johnson* case, however, this method's horizons have been widened until now it is used in most evasion cases, regardless of the amount of tax deficiency involved. The net worth method in ordinary income-bracket cases as evolved from the deficiencies in *Johnson, Capone,* or *Guzik,* greatly increase the chances for error.

There are many other assumptions which can be dangerous, among which is the equation of unexplained increases in net worth with unreported taxable income. Obviously such an assumption has many weaknesses. It may be that gifts, inheritances, loans and the like account for the newly acquired wealth. There is also great danger that the jury may assume that once the government has established the figures in its net worth computations, the crime of tax evasion automatically follows. Although it may appear just to expect the taxpayer to explain the "bulge" in his net worth, he may be entirely honest and yet remain unable to recount his financial history.

"While these pitfalls inherent in the net worth method do not foreclose its use, they do require the exercise of great care and restraint. Trial courts should approach these cases in the full realization that the taxpayer may be ensnarled in a system, which though difficult for the prosecution to utilize, is equally hard for the defendant to refute. Appellate courts should review the cases, bearing constantly in mind the difficulties that arise when circumstantial evidence as to guilt is the chief weapon of a method that is itself only on approximation".[67]

63 Demetree v. United States, 207 F.2d 892, 894 (5th Cir. 1953); United States v. Caserta, 199 F.2d 905, 907 (3d Cir. 1952); United States v. Fenwick, 177 F.2d 488 (7th Cir. 1949).

64 Capone v. United States, 51 F.2d 609 (7th Cir. 1931).

65 Guzik v. United States, 54 F.2d 618 (7th Cir. 1931).

66 United States v. Johnson, 319 U.S. 503, 63 S. Ct. 1233, 87 L. Ed. 1546 (1943).

67 See note 33, supra.

Civil and criminal penalties, however, are not the entire solution to the problem of tax evasion. In some circles of our society, tax evasion is considered a fashionable crime and those who defraud the government of the greatest amounts of money are considered most worthy of social acclaim. The only logical solution is to provide more effective tax education for our taxpayers. Only when such education is accomplished, will tax evasion be classed as evil and regarded as a crime by our society. B.A.R.