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Recent Decisions

RECENT DECISIONS

Community Property — Divorce — The Community Nature of a Military Retirement Fund

Gilberto Mora sued for divorce from Flora Mae Mora after fourteen years of marriage. At the time of trial Gilberto, a member of the armed forces for twenty-five years, was eligible for retirement. On the basis of his service he was to receive upon retirement a monthly income for life; the retirement plan provided that Gilberto would forfeit his rights to such income if he died while in the service or was dishonorably discharged. The trial court concluded that this retirement fund was not the community property of the spouses. *Held, reversed*: A husband's interest in a military retirement plan is a presently vested property right, regardless of the forfeiture clause, and that portion of the retirement fund accumulated during the marriage constitutes community property of the spouses. *Mora v. Mora*, 429 S.W.2d 660 (Tex. Civ. App. 1968), *error dismissed w.o.j.*

Earlier Texas cases recognized the conflict between jurisdictions which considered retirement or pension funds a gift from the employer to the employee upon retirement and jurisdictions which considered such funds a type of compensation earned during the period of employment.[1] The Texas courts came to the conclusion that the fund represented property earned by the employee during the period of employment.[2] Under article 4619[3] such funds were then classified as community property of the spouses.

In recent years in Texas a conflict focused on whether a forfeiture clause in the retirement fund agreement denied the employee a vested property right in the fund. If the forfeiture clause were a condition precedent, no property rights would vest in the employee prior to his retirement,[4] and thus no community property rights would arise prior to retirement. But if the clause were a condition subsequent, a vested property right would arise in the money accumulated in the retirement fund;[5] the employee would have a vested interest subject to divestment, and this interest would constitute community property acquired at the time an amount of money was placed in the fund and credited to the employee.

In *Mora* the San Antonio court of civil appeals took the position that a forfeiture clause was a condition subsequent, for "[o]nly rights in existence can be forfeited."[6] The court stated that no federal statute or regulation divested it of power to make necessary orders "affecting the retire-

[1] Lee v. Lee, 112 Tex. 392, 247 S.W. 828 (1923); Kirkham v. Kirkham, 335 S.W.2d 393 (Tex. Civ. App. 1960); McCamey v. Hollister Oil Co., 241 S.W. 689 (Tex. Civ. App. 1922), *aff'd*, 115 Tex. 49, 274 S.W. 652 (1925).

[2] *See* Herring v. Blakely, 385 S.W.2d 843 (Tex. 1965), *noted in* 19 Sw L.J. 370 (1965); Kirkham v. Kirkham, 335 S.W.2d 393 (Tex. Civ. App. 1960).

[3] Tex. Rev. Civ. Stat. Ann. art. 4619 (1960) provides that all property acquired during marriage except by gift, devise or descent shall be community property.

[4] *See* A. Corbin, Contracts § 628 (1952).

[5] *Id.*

[6] 429 S.W.2d at 662.

ment benefit as part of the property settlement in a divorce action."[7] The situation in *Mora* was contrasted with the situation in *Allen v. Allen*,[8] where the court was deprived of this power by federal statute.

From the express language in such retirement plans, the agreement contemplates that the employee has a property right in the fund and that his right may be lost, forfeited, or divested if the employee performs some specified act in the future. From the standpoints of equity and the wording of the majority of forfeiture clauses in retirement plan agreements, an employee's interest in such funds should be regarded as a vested right subject to divestment and, therefore, as the community property of the spouses prior to retirement. The problem the courts must now resolve is how to divide this interest upon divorce when the employee will not receive any income from the fund until some future date.[9]

T.W.W.

Constitutional Law — Juvenile Proceedings — Due Process for the Delinquent

The Juvenile Court of Harris County, Texas, found the defendant, Debra Fay Leach, aged twelve, to be a delinquent child.[1] The charge of delinquency was based on the fact that she had run away from her home on several occasions. Debra Fay had been placed in the detention ward of the juvenile authorities at the request of her parents and had remained there until trial. During her incarceration, and before counsel was appointed for her, Debra Fay was interrogated by a probation officer. The child was not told of her right to have an attorney with her during these questioning periods, nor was she told of her right to remain silent. At trial the interrogating officer testified, on the basis of Debra Fay's statements, that the child was "endangering her morals by the runaways and what took place during the runaways."[2] *Held, reversed*: Proceedings in juvenile cases which may lead to commitment must meet the requirements of due process, including written notice of the specific charge, notification to the child and his parents of the child's right to be represented by counsel retained by them (or appointed), and application of the constitutional priv-

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[7] *Id.*

[8] 363 S.W.2d 314 (Tex. Civ. App. 1962).

[9] In Kirkham v. Kirkham, 335 S.W.2d 393 (Tex. Civ. App. 1960), the court affirmed the trial court's allowance of a money judgment against the husband for the wife's share of the retirement fund, although the husband had no present right to income from the fund. In the instant case the court noted that the trial court could enter a decree requiring the husband to pay the wife a share of the monthly payments "if, as, and when he receives them." 429 S.W.2d at 663. Because such retirement funds often constitute substantially all the assets of a married couple, this latter approach appears to be the more equitable.

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[1] TEX. REV. CIV. STAT. ANN. art. 2338-1, § 3(f) (Supp. 1967), providing that a child may be delinquent when he "habitually deports himself so as to injure or endanger the morals or health of himself or others."

[2] Leach v. State, 428 S.W.2d 817, 820 (Tex. 1968).

ilege against self-incrimination. *Leach v. State*, 428 S.W.2d 817 (Tex. Civ. App. 1968).

In determining specifically that the interrogation and testimony of the probation officer denied Debra Fay the constitutional essentials of due process, the court applied the standards established in *In re Gault*.[3] There, the United States Supreme Court decided that the same principles applicable to adults in criminal proceedings must be enforced in cases involving juveniles, even if the proceedings are before a juvenile court and only determine the status of "delinquency." The Court stated that such proceedings, "which may lead to commitment to a state institution, must be regarded as 'criminal' for purposes of the privilege against self incrimination. To hold otherwise would be to disregard substance because of the feeble enticement of the 'civil' label-of-convenience which has been attached to juvenile proceedings."[4]

The statute under which Debra Fay Leach was committed was part of the Civil Statutes of Texas.[5] Courts have traditionally used a different standard of due process in "civil" proceedings under the theory of *parens patriae*,[6] or the philosophy that juvenile proceedings are not "in the nature of a criminal trial, but constitute merely a civil inquiry . . . looking to the treatment, reformation, and rehabilitation of the minor child."[7] One inroad toward recognizing the need for constitutional protection in a juvenile proceeding was the Supreme Court's decision in *Kent v. United States*,[8] which held that "assistance of counsel was essential to the validity of a transfer of jurisdiction by a juvenile court to a district court."[9] The Texas court in *Leach* acknowledged that all the safeguards essential to due process in a criminal trial are required in a juvenile proceeding, and found them lacking in this case. The testimony of the probation officer should have been excluded from the proceedings on the basis that "[i]nculpatory admissions made prior to a waiver of the privilege against self-incrimination, or opinions based thereon, are not admissible."[10] In addition, because no counsel was timely appointed to safeguard appellant's rights and because the child was not warned of her constitutional privileges, the court felt that the proceedings constituted "clear violations of federal due process."[11] So holding, the court implicitly recognized that the delinquency statute is penal in nature and, thus, must be treated as penal in its enforcement.

R.A.K.

[3] 387 U.S. 1 (1967), *noted in* 28 LA. L. REV. 492 (1968), *and* 47 NEB. L. REV. 558 (1968).

[4] 387 U.S. 1, 49-50 (1967).

[5] *See* note 1 *supra*. A concurring opinion preferred to base the decision on the "obvious unconstitutionality of that portion of the statute here in issue." 428 S.W.2d at 821.

[6] Sovereign power guardianship over persons under disability. For a general discussion, see Note, *Criminal Procedure—Due Process in Juvenile Delinquency Proceedings*, 28 LA. L. REV. 492 (1968).

[7] *In re* Holmes, 379 Pa. 599, 109 A.2d 523, 525 (1954). The court went on to say: "Their purpose is not penal but protective—aimed to check juvenile delinquency" and to protect a potential criminal during his adolescent life. *Id.*

[8] 383 U.S. 541 (1966).

[9] Note, *supra* note 6, at 495.

[10] 428 S.W.2d 817, 820 (Tex. 1968). The court cited Miranda v. Arizona, 384 U.S. 436 (1966).

[11] 428 S.W.2d at 821. The court noted, *id.* at 820, that according to *In re* Gault, 387 U.S. 1, 36 (1967), "[A] probation officer is also an arresting officer and cannot act as counsel for the child."

Corporate Law — Stockholder's Inspection Rights — Traditional State Right Enforced by Federal Court

After the corporation repeatedly refused to grant Stern his stockholder's right to inspect corporate books and records, Stern brought suit[1] in federal district court[2] in Pennsylvania, the state of incorporation, requesting an order to permit inspection. The inspection right was authorized by a Pennsylvania statute.[3] The district court dismissed the action on the ground that because the relief sought was mandamus, the court was precluded from exercising jurisdiction under the All Writs Act.[4] The Court of Appeals for the Third Circuit affirmed.[5] *Held, reversed*: A federal district court has jurisdiction to grant equity relief in a diversity action by a stockholder against a corporation, where the stockholder seeks to inspect the corporate books and records as authorized by state statute, even where such state statute is labeled "mandamus." *Stern v. South Chester Tube Co.*, 390 U.S. 606 (1968).

At common law a stockholder was entitled to inspect the books and records of a private corporation at a reasonable time and place, and for a proper purpose.[6] Enforcement of this inspection right was generally accomplished by mandamus.[7] In the instant case, both lower courts interpreted the relief sought by Stern as in the nature of mandamus. A line of cases holding that the All Writs Act denied jurisdictional power to federal courts to issue mandamus where it was the only relief sought led the two courts to conclude that they were denied such power in the present case.

The Supreme Court viewed Stern's complaint as basically one seeking equitable relief and not mandamus. In concluding that the lower courts erred in interpreting the nature of the relief sought, the Court distinguished most of the cases relied upon as suits against a public official, whereas the present case involved a private party. The Supreme Court found only one prior case, *Knapp v. Lake Shore R.R.*,[8] in which it had held a federal court without jurisdiction to issue a writ of mandamus against a private party. But the Court distinguished *Knapp* on the ground that it was a suit at law in which mandamus was expressly sought and which was brought at a time when law and equity were divided. Because mandamus was restricted to actions at law, the *Knapp* court was unable to grant such relief. The subsequent merger of law and equity eliminated this limitation

[1] Stern was a resident of New York and held $10,000 or more of stock; South Chester Tube Company was incorporated in Pennsylvania—thus federal court original jurisdiction was invoked under 28 U.S.C. § 1332(a) (1964), where diversity of citizenship and an amount in controversy in excess of $10,000 were both met.

[2] Stern v. South Chester Tube Co., 252 F. Supp. 329 (E.D. Pa. 1966).

[3] PA. STAT. ANN. tit. 15, § 2852-308B (1958).

[4] 28 U.S.C. § 1651 (1964). Federal courts are authorized to issue "all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law."

[5] 378 F.2d 205 (3d Cir. 1967).

[6] 18 C.J.S. *Corporations* § 502 (1939); W. FLETCHER, PRIVATE CORPORATIONS § 2214 (perm. rev. repl. 1967).

[7] 18 AM. JUR. 2D *Corporations* §§ 444-49 (1965); W. FLETCHER, *supra* note 6, § 2251. Mandamus is a writ issuing from a court of competent jurisdiction and directed to a person, officer, corporation, or inferior court, commanding performance of some particular duty resting on the person to whom it is sent. 55 C.J.S. *Mandamus* §§ 1, 2 (1939).

[8] 197 U.S. 536 (1905).

on the federal court's power to grant equitable relief. Pennsylvania statutes set out both the stockholders' right to request inspection of the books and records[9] and the right of state courts to issue a compulsory judicial order for enforcing such rights.[10] The Supreme Court felt that the Pennsylvania statutory relief, although labeled "mandamus," was actually equitable in nature. The Court reasoned that since Stern had no adequate remedy at law, a federal court could have jurisdiction to grant the relief sought under its equity power. The issue of whether such result would be obtained even if there were no similar state remedy in statutory form was expressly avoided.

By the *Stern* decision, the Supreme Court has recognized the jurisdictional power of federal courts to grant equitable relief to stockholders in a diversity action where rights of inspection are refused by the corporation, in the event that state statutory provisions authorize such relief. *Stern* makes available an old remedy in a new forum. It is not a surprising decision, because it complements an established structure of federal regulation of various corporate activities.[11]

T.E.S.

Jurisdiction — Foreign Corporation Doing Business as a Partner

Plaintiff was injured when the automobile in which he was a passenger collided with a truck driven by an employee of a partnership doing business in Odessa, Texas. After moving from Texas to Ohio, plaintiff sued Freedom Newspapers, Inc., a California corporation and controlling partner in the Odessa partnership, for damages resulting from the accident. The suit was brought in an Ohio federal district court, where jurisdiction was based upon diversity of citizenship. Freedom Newspapers moved for a change of venue to a Texas federal district court, alleging that the Texas court was the proper venue,[1] and that personal jurisdiction over Freedom Newspapers could be obtained pursuant to the Texas long-arm statute.[2] *Held, motion granted*: Owning a controlling interest in a Texas partnership constitutes sufficient contact with Texas to subject the non-resident partner to the jurisdiction of the Texas courts. *Myers v. Freedom Newspapers, Inc.*, 274 F. Supp. 93 (N.D. Ohio 1967).

Historically, jurisdiction over foreign corporations was determined by

[9] PA. STAT. ANN. tit. 15, § 2852-308B (1958).
[10] *Id.* tit. 12, § 1911 (1967).
[11] *See, e.g.*, A. BROMBERG, SECURITIES LAW (1967), for a discussion of federal regulation of fraud in the securities field.

[1] 28 U.S.C. § 1391(a) (Supp. II, 1965-66): "A civil action wherein jurisdiction is founded only on diversity of citizenship may, except as otherwise provided by law, be brought only in the judicial district where all plaintiffs or all defendants reside, or in which the claim arose." *See also id.* § 1391(c) for venue in a suit against a corporation.
[2] TEX. REV. CIV. STAT. ANN. art. 2031b (1964).

such tests as corporate presence[3] and corporate consent.[4] However, in the landmark case of *International Shoe Co. v. Washington*,[5] the Supreme Court discarded previous jurisdictional tests and established a less restrictive standard. To be amenable to service under this test, a foreign corporation need only have "certain minimum contacts" with the state so that the exercise of jurisdiction would not offend traditional notions of fair play and substantial justice.[6] In formulating the "minimum contacts" standard, the Court focused on the necessity of balancing the interests of the plaintiff, defendant corporation, and the forum state.[7] Once due process limits are defined, a state must still enact a "long-arm" statute authorizing "minimum contacts" jurisdiction.[8] The applicable Texas statute[9] provides that if a foreign corporation fails to appoint a resident agent, the Secretary of State may be served as the agent of the foreign corporation whenever the foreign corporation is "doing business" in Texas. This statute was designed to exploit maximum jurisdictional rights consistent with the Federal Constitution.[10]

"Minimum contacts" litigation involving a corporate partner operating a partnership in another state has been sparse. This is probably due to the fact that until recently many corporations were statutorily forbidden partnership status.[11] Furthermore, even when authorized by statute, the right of a corporation to be a partner was very restricted, often depending on the charter of the corporation.[12] Other related partnership situations have been litigated to a greater degree. In *Schenstrom v. Continental Machines, Inc.*,[13] a federal district court held that a corporation was not "doing business" in a foreign state merely because it owned an interest in a separately operated partnership located in the forum. It is significant to note that jurisdiction was refused even though the separately owned partnership was completely dominated by the foreign corporation.

Although for jurisdictional purposes individuals and corporations cannot always be treated alike,[14] the "minimum contacts" jurisdictional test is clearly applicable to both non-resident individuals and corporations.[15] Thus,

[3] *See, e.g.*, International Harvester Co. v. Kentucky, 234 U.S. 579 (1914); Pennoyer v. Neff, 95 U.S. 714 (1877).

[4] *See, e.g.*, Lafayette Ins. Co. v. French, 59 U.S. (18 How.) 404 (1855). *See also* Note, *The Application of the First Amendment to Long Arm Jurisdiction*, 21 Sw. L.J. 808 (1967).

[5] 326 U.S. 310 (1945).

[6] *Id.* at 316.

[7] F. JAMES, CIVIL PROCEDURE 640 (1965).

[8] Atwood Hatcheries v. Heisdorf & Nelson Farms, 357 F.2d 847 (5th Cir. 1966). *See generally* VanDercreek, *Texas Civil Procedure, Annual Survey of Texas Law*, 21 Sw. L.J. 155 (1967).

[9] TEX. REV. CIV. STAT. ANN. art. 2031b, § 4 (1964). The Secretary of State can be served as the agent of the foreign corporation whenever the foreign corporation is doing business in Texas, defined to include: (1) "entering into contract . . . with a resident of Texas to be performed in whole or in part by either party in this State," (2) "the committing of any tort in whole or in part" in Texas, or (3) any other act which "may constitute doing business."

[10] Atwood Hatcheries v. Heisdorf & Nelson Farms, 357 F.2d 847 (5th Cir. 1966).

[11] *See, e.g.*, Merchants' Nat'l Bank v. Wehrmann, 202 U.S. 295 (1906).

[12] *See, e.g.*, Mervyn Inv. Co. v. Biber, 184 Cal. 637, 194 P. 1037 (1921); Consolidated Furniture Mfrs. v. Goldstein, 140 Cal. App. 563, 35 P.2d 627 (1934); Humble Oil & Ref. Co. v. Strauss, 243 S.W. 528 (Tex. Civ. App. 1922).

[13] 7 F.R.D. 434 (S.D.N.Y. 1947).

[14] *E.g.*, a corporation is subject to suit in the state of its incorporation, even though it may not be engaged in business or carrying on any activities there.

[15] McGee v. International Life Ins. Co., 355 U.S. 220, 222-23 (1957).

cases dealing with jurisdiction over out-of-state individual partners have some bearing on whether an out-of-state corporate partner should be subject to the jurisdiction of a particular state. For example, in *Bedford v. Dillinger*[16] "minimum contacts" were satisfied solely because the non-resident individual defendants were partners in a Texas partnership, even though they were not physically present within the state.[17] In *Stoner v. Higginson*[18] service upon an individual non-resident defendant was upheld because the defendant's partnership was engaged in business in the jurisdiction at the time service was made.

The threshold question in *Myers* was whether the Texas court could obtain personal jurisdiction over the defendant foreign corporation based solely upon its partnership interest-activity. The defendant was not conducting its primary business in Texas; thus, jurisdiction had to be based on its partnership interest. The court determined that the defendant's partnership, which it controlled, was sufficient business activity within the state to satisfy the requirements of due process. Applying traditional partnership principles, the court reasoned that the corporation was doing business in Texas because each partner acts as the agent of the other and the activities of one are imputed to all.

Myers v. Freedom Newspapers, Inc., seems to exemplify the steadily expanding jurisdiction over foreign corporations, evidenced by broader constitutional decisions and implemented by far-reaching long-arm statutes. It is unclear, however, whether the decision in *Myers* can be extended to other situations involving out-of-state corporations. In reaching its decision, the court in dicta reiterated the rule of *Cannon Mfrs. v. Cudahy Packing Co.*,[19] which holds that the ownership of a foreign subsidiary is not, in itself, sufficient contact with that state to subject the parent corporation to jurisdiction therein.[20] From an academic viewpoint, it might be urged that this distinction should be discarded. If the *Myers* situation constitutes sufficient contact with a foreign state, the exercise of jurisdiction over a foreign parent corporation whose only contact with the forum state is the ownership of a subsidiary therein seems equally reasonable. However, it is unlikely that this will become the law in the near future, for historical precedent, which dictates that corporations and partnerships should be treated differently for jurisdictional purposes because shareholders, unlike partners, have limited personal liability, will be difficult to overcome.

A.W.Z.

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[16] 310 F.2d 583 (5th Cir. 1962).

[17] The partnership agreement provided for payment of certain commissions to a partner. The former partner, suing for commissions, was allowed to acquire jurisdiction over non-resident former partners by citation upon the Secretary of State of Texas, where the non-resident partners actually participated in the partnership business in the state.

[18] 316 Pa. 481, 175 A. 527 (1934).

[19] 267 U.S. 333 (1925). In *Cannon* the substantive issue did not arise out of the activities of the subsidiary.

[20] Cases subsequent to *Cannon* have maintained that when a separate corporate identity is not retained the parent is subject to the jurisdiction of the foreign state. *See, e.g.*, Skupski v. Western Navigation Corp., 123 F. Supp. 309 (S.D.N.Y. 1954); Spacarb, Inc. v. Automatic Canteen Co., 101 F. Supp. 485 (S.D.N.Y. 1951).

Labor Law — Life of Grievance Procedure After Contract Termination

The union notified Kingsport Publishing Corporation that it was unequivocally terminating the labor agreement at the contract termination date. Some eight months after the contract expired, and during negotiations with the union for a new agreement, the company discharged a union employee for refusal to carry out a foreman's instructions. The union sought to initiate grievance proceedings as set out in the expired contract. Kingsport refused to follow this grievance machinery, but exhibited a willingness to pursue the matter in negotiations. The union declined to negotiate and filed an unfair labor practice charge with the National Labor Relations Board under section 8(a)5[1] of the National Labor Relations Act. The Board determined that because grievance handling is a mandatory subject of bargaining,[2] the company was guilty of an unfair labor practice by reason of its unilateral action and petitioned the court for enforcement of its order so holding. *Held, enforcement refused*: Kingsport had a right to decline to follow the previous grievance procedure where the prior union agreement had expired, negotiations for a new contract had not been concluded, and the grievance procedure had not become a part of the established operational pattern. *Kingsport Publishing Co. v. NLRB*, 69 L.R.R.M. 2193 (6th Cir. 1968).

That grievance procedure is a mandatory subject of bargaining is well established,[3] and the facts in *Kingsport* reflected the company's willingness to negotiate on this matter. Therefore, the point of contention centered around the availability to either party of unilateral change or unilateral action concerning a grievance.

In *NLRB v. Katz*[4] the Supreme Court held that "an employer's unilateral change in conditions of employment under negotiation is . . . a violation of Section 8(a)5."[5] The Board has further pronounced that employment practices of the employer may become conditions of employment and, as such, may survive the termination of an agreement.[6] In *Kingsport* the union and the Board, following the dictates of *Katz*, maintained that a unilateral change in a mandatorily bargainable item was automatically a violation of section 8(a)5.

The company based its defense upon two theories. The first was that the union termination letter exceeded section 8(d)[7] requirements and constituted a waiver of their right to bargain about any change regarding a condition of employment. The court disposed of this argument as being unnec-

[1] 29 U.S.C. § 158(a)5 (1964): "It shall be an unfair labor practice for an employer—to refuse to bargain collectively with the representatives of his employees . . . ."

[2] *See* Fibreboard Paper Products Corp. v. NLRB, 379 U.S. 203 (1964); Marine Workers Union v. NLRB, 320 F.2d 615 (3d Cir. 1963), *cert. denied*, 375 U.S. 984 (1964).

[3] *Id.*

[4] NLRB v. Katz, 369 U.S. 736 (1962).

[5] *Id.* at 743.

[6] Shell Oil Co., 149 N.L.R.B. 283 (1964) (the practice of contracting out occasional maintenance work on a unilateral basis).

[7] 29 U.S.C. § 158(d) (1964).

essary to a decision. The second company defense centered upon the premise that grievance machinery is based upon contract. Since no contract existed, the company urged that no grievance machinery was in effect. This theory was based on *J. Wiley & Sons*,[8] which declared that arbitration was a contractual matter and that the company could not be compelled to arbitrate where it was not bound by an arbitration agreement. Because arbitration was the final step in the grievance process which the union insisted upon, the company argued that it could not be required to go through grievance procedure. The court, recognizing the contractual basis of arbitration, nevertheless did not base its decision on the second contention of the company.

The *Kingsport* court followed the reasoning of an Eighth Circuit decision, *NLRB v. Frontier Homes Corp.*,[9] where it was held: "Expired contract rights affecting mandatory bargaining issues, therefore, have no efficacy unless the rights have become a part of the established operational pattern and thus become a part of the *status quo* of the entire plant operation."[10] The Sixth Circuit in *Kingsport* reasoned that the expiration of eight months without a single grievance being processed through the previously existing machinery was sufficient for a finding that such machinery was not a part of the "established operational pattern."

By refusing enforcement of the Board's order the court has given additional instruction to the Board in its dealings with the effect of contract provisions in expired labor agreements. This instruction should strengthen the rights of parties to an expired labor agreement to disregard provisions set out in such agreement, even though mandatorily bargainable, where the provisions can be shown not to be a part of the status quo of the plant operation.

R.B.S.

Labor Law — Remedies — Order to Employer To Grant Checkoff

The National Labor Relations Board found that H. K. Porter Company had violated section 8(a)(5) of the National Labor Relations Act[1] by failing to bargain in good faith with the union on the issue of a checkoff provision. The Board ordered the company to bargain collectively[2] and the court of appeals enforced the order,[3] indicating that the company would not be permitted to refuse a checkoff provision "for some concocted rea-

[8] John Wiley & Sons v. Livingston, 376 U.S. 543 (1964).
[9] NLRB v. Frontier Homes Corp., 371 F.2d 974 (8th Cir. 1967).
[10] *Id.* at 981.

[1] 49 Stat. 451 (1935), *as amended*, 29 U.S.C. § 158(a)(5) (1964).
[2] 153 N.L.R.B. 1370 (1965).
[3] United Steelworkers of America v. NLRB, 363 F.2d 295 (D.C. Cir.), *cert. denied*, 385 U.S. 851 (1966).

son not heretofore advanced."[4] The union and the company disagreed as to the interpretation of the circuit court's decree of enforcement. While the union interpreted the decree as obligating the company to agree to a dues-checkoff provision, the company felt that it was required only to discuss the possibility of such a provision. In spite of these divergent interpretations the court denied a union motion to clarify the decree for the purpose of inviting the Board to test the competing ideas with further investigation.[5] The Board accepted the arguments of the company and declined to institute contempt proceedings. The union again asked the circuit court to clarify its enforcement decree. The subsequent clarification and remand of the case to the Board for further proceedings indicated that the Board would be warranted in ordering the company to grant the checkoff provision "in return for a reasonable concession by the union."[6] *Held, supplemental order issued*: An order obligating the employer to grant checkoff but not requiring the union to give a reasonable concession is warranted where the employer has repeatedly violated section 8(a)(5) and its opposition to granting checkoff is based solely on a desire to thwart the consummation of a collective bargaining agreement. *H.K. Porter Co.*, 172 N.L.R.B. No. 72 (1968).

The circuit court felt compelled to clarify its original decree because it disagreed with the Board that the company's interpretation of its obligation was correct. In the court's opinion, the company could not "purge itself of its bad faith and meet its Section (d) obligation [to bargain collectively] by agreeing simply to negotiate on alternatives to a checkoff."[7] For this reason and to establish guidelines for the Board, the clarification discussed the circumstances under which checkoff could be imposed as a remedy for bad faith bargaining. These circumstances included the two violations of section 8(a)(5) and the acknowledgment by the company that it had no business reason for refusing the checkoff. Thus it would have been proper for the Board to order the company to grant this provision in return for a reasonable union concession on wages or insurance, which were the two remaining issues in dispute. In addition, the court stated that "in an appropriate case the Board could simply order the company to grant a checkoff."[8]

In *Porter* two policies of the National Labor Relations Act were in conflict, *i.e.*, freedom of contract and the guarantee of the right of employees to bargain collectively. The court reasoned that in such a case the Board must seek the remedy which would best effectuate one of the policies with the least cost to the other policy. In certain instances, therefore, ordering an employer to grant checkoff may be the only way to guarantee the employees' right to bargain collectively, regardless of the intrusion into freedom of contract.

[4] United Steelworkers of America v. NLRB, 389 F.2d 295, 297 (D.C. Cir. 1967).
[5] *Id.*
[6] *Id.* at 299.
[7] *Id.* at 298.
[8] *Id.* at 300.

It is significant that the Board in its second order followed the guidance of the court; it is even more noteworthy that the Board went to the limit of the judicial directive by not requiring a reasonable concession from the union. The Board apparently rejected the court's distinction between appropriate cases for an absolute remedy and cases warranting an order of reciprocal concessions. The basis for this rejection was that "to permit [the company] to hold out for some 'reasonable concession' by the Union in return for the checkoff . . . would imply that the [company] is now being ordered to surrender a position that it had legitimately maintained."[9] The Board concluded that such an implication would be contrary to the finding that the company's opposition was solely designed to thwart the consummation of the collective bargaining agreement.

Utilization of an absolute order eliminates the confusion which would have been caused by attempts to distinguish the "appropriate case" mentioned by the court from less extreme cases. Indeed, it is difficult to construct a more extreme example of a section 8(a)(5) violation than *Porter*. Moreover, it is unlikely that a remedy requiring reciprocal concessions would have been more effective in breaking the cycles of impasse between the parties, unless the Board has dictated the substance of the union's concession, which would be beyond its statutory authority.

B.A.N.

Taxation — Partnerships — Partner May Be an Employee Under Section 119

Armstrong, manager of the Armstrong Ranch, was provided by the partnership which owned the ranch with a home for himself and his family, most of his groceries and utilities, maid service, etc. In addition, he received a fixed salary for his services and a share of the partnership profits, of which he owned a five per cent interest. On his tax returns for the years 1960, 1961, and 1962, Armstrong failed to report the value of the house, groceries, etc., and the Internal Revenue Service assessed a deficiency for their value. After paying the deficiency, Armstrong sued for a refund, contending that these emoluments were properly excluded from his income under section 119 of the Internal Revenue Code of 1954, which allows an employee to exclude the value of meals and lodging furnished by his employer under certain circumstances.[1] The Service rejected this contention, reasoning that a partner cannot be an employee of the partnership. The district court granted the government's motion for summary judgment. *Held, reversed*: Section 707 of the 1954 Code, which permits a partner to engage in transactions with the partnership as though he were an outsider, views the partnership as a separate entity, and a partner may be an em-

[9] H.K. Porter Co., 68 L.R.R.M. 1337, 1338 (1968).

[1] The circumstances are if the meals or lodging: (1) is furnished for the convenience of the employer and (2) is on the business premises of the employer. *See* INT. REV. CODE of 1954, § 119.

ployee of this entity, just as he may be its debtor or creditor. Therefore, the government was not entitled to judgment as a matter of law. *Armstrong v. Phinney*, 394 F.2d 661 (5th Cir. 1968).

Although fought on the battlefield of tax law, *Armstrong* is a skirmish in the old dispute over whether a partnership is an "aggregate" of the ownership interests of the partners, with no separate existence of its own, or is a separate "entity." Though widespread adoption of the Uniform Partnership Act in recent years has led to something of a truce on the question in substantive partnership law, "aggregate" and "entity" are still fighting words in tax law.[2] Like the Partnership Act, the Internal Revenue Code utilizes both theories,[3] but the Code is indefinite on which theory should govern in several troublesome areas and thus has created some confusion among the courts.[4]

Armstrong illustrates the importance of resolving these uncertainties. To be entitled to exclude meals and lodging under section 119, the partner must be an employee of the partnership.[5] Under the aggregate concept of partnership, he cannot be an employee, for the partner rendering services to the partnership is merely serving himself, like a single proprietor running his business. If the partnership is considered an entity, however, the partner logically can be an employee of this entity, just as a stockholder can be an employee of his corporation.

Under the 1939 Code the courts of appeals and the Commissioner agreed that a partner could not exclude from his income the value of meals and lodging furnished him by the partnership, because the partnership and the partners were one and the same legal entity.[6] Since no tax was imposed upon the partnership itself, the courts reasoned that the partnership could not be regarded as a separate entity for tax purposes.[7] The tax court, however, refused to adopt this reasoning and held instead that the partner could exclude meals and lodging.[8]

In 1967 the court of claims decided the first case to arise under the 1954 Code involving exclusion of meals and lodging furnished by a partnership to a partner.[9] That court, with little discussion, followed the appellate decisions under the 1939 Code and ruled that the managing partner of a ranch cannot exclude the value of food and lodging furnished by the partnership

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[2] *See* 6 J. MERTENS, THE LAW OF FEDERAL INCOME TAXATION § 35.01 (1957).

[3] *E.g.*, the imposition of tax on the individual partners rather than on the partnership is an aggregate approach, whereas the requirement that computations of partnership income and elections affecting its computation must be made by the partnership reflects the entity concept. *Compare* INT. REV. CODE of 1954, § 701 *with id.*, § 703.

[4] *Compare* Commissioner v. Whitney, 169 F.2d 562, 567-68 (2d Cir.) (Clark, J.), *cert. denied*, 335 U.S. 892 (1948) (tax law adopts the common law concept of the partnership as an aggregate of individuals) *with* Commissioner v. Lehman, 165 F.2d 383, 385 (2d Cir.) (L. Hand, J.), *cert. denied*, 334 U.S. 819 (1948) (Congress adopted the common law view that a partnership was an entity for most purposes).

[5] INT. REV. CODE of 1954, § 119.

[6] Commissioner v. Robinson, 273 F.2d 503 (3d Cir.), *cert. denied*, 363 U.S. 810 (1959); United States v. Briggs, 238 F.2d 53 (10th Cir. 1956) (per curiam); Commissioner v. Doak, 234 F.2d 704 (4th Cir. 1956).

[7] Commissioner v. Doak, 234 F.2d 704, 708 (4th Cir. 1956).

[8] *E.g.*, George A. Papineau, 16 T.C. 130 (1951), *not acquiesced in*, 1952-2 CUM. BULL. 5.

[9] Wilson v. United States, 179 Ct. Cl. 725, 376 F.2d 280 (1967) (per curiam).

while he lives on the ranch.[10] Reasoning that a partnership "is not a legal entity separate and apart from the partners,"[11] the court failed to discuss what effect differences between the 1939 and 1954 codes should have upon the applicability of previous decisions to cases arising under the 1954 Code. In *Armstrong v. Phinney*[12] the Fifth Circuit did consider the changes made by the 1954 Code and in the process departed from the previous decisions. The court noted that when the 1954 Code was enacted, the entity aspects of a partnership were more fully recognized than in the 1939 Code by the addition of section 707, which enables a partner to engage in transactions with the partnership as though he were an outsider.[13] This section permits the partnership to pay a partner a salary and to deduct it from the partnership income like the salary of any employee.[14] However, section 707 never specifically refers to a partner as an employee, and his status as a member of that category is questionable under other Code provisions.[15] Nevertheless, the Fifth Circuit ruled that section 707 is sufficient authorization for judicial recognition of an employer-employee relationship between a partner and his partnership for purposes of section 119.[16]

Because the appeal was from a summary judgment the scope of the *Armstrong* decision is uncertain, for the court's discussion goes no further than its ruling that the government was not entitled to judgment as a matter of law. Clearly, the result of the case conflicts with the 1967 court of claims decision and with decisions of other circuits under the 1939 Code, but these cases may be distinguishable on their facts. The prior cases which refused to allow exclusion of meals and lodging have involved partners owning controlling interests in the partnerships,[17] whereas Armstrong owns only a five per cent interest. Not even under section 707 of the 1954 Code may a partner owning a fifty per cent interest in the partnership engage in transactions with the partnership as an outsider.[18] Had Armstrong owned a larger interest, therefore, the reasoning behind the decision would not have been available. Thus the case could be read as no more than a recognition by the court that partnerships often grant to employees small partnership interests even though these mini-partners may have no more voice in the management and control of the partnership than an employee without such an interest.

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[10] *Id.*

[11] *Id.* at 752, 376 F.2d at 296.

[12] 394 F.2d 661 (5th Cir. 1968).

[13] Treas. Reg. § 1.707-1 (1956) provides:

> A partner who engages in a transaction with a partnership other than in his capacity as a partner shall be treated as if he were not a member of the partnership with respect to such transaction. Such transactions include . . . the rendering of services by the partnership to the partner or by the partner to the partnership.

Noting the difficulties in this area, the Senate Committee on Finance said in its report: "Because of its simplicity of operation, the 'entity' rule has been adopted by the House and your committee." S. REP. No. 1622, 83d Cong., 2d Sess. 92 (1954); *cf.* H.R. REP. No. 2543, 83d Cong., 2d Sess. 59 (1954).

[14] INT. REV. CODE of 1954, § 707(c); see note 13 *supra.*

[15] *See, e.g., id.,* §§ 101(b)(3), 105(g), 401(c), 3121(d).

[16] 394 F.2d at 663-64.

[17] *E.g.,* Commissioner v. Robinson, 273 F.2d 503 (3d Cir.), *cert. denied,* 363 U.S. 810 (1959) (husband and wife operating hotel as partners); *cf.* cases cited note 6 *supra.*

[18] INT. REV. CODE of 1954, § 707(b).

However, the Fifth Circuit did not discuss fully the countervailing considerations. Although it may be clear that a partnership is considered an entity under section 707, Congress indicated when it adopted that provision that a partnership cannot be considered an entity in all areas.[19] Thus there may well be a distinction between permitting a partner to receive a salary from the partnership (on which he pays taxes) and permitting him to exclude from his income the value of meals and lodging furnished by the partnership. If their value may be excluded, the partner has his living expenses paid tax-free, and in addition, the tax on his distributive share of partnership income is reduced, for the partnership is entitled to deduct the cost of the meals and lodging from the partnership income, thereby reducing all of the partners' taxable income. This double tax benefit suggests that tax considerations applicable to exclusions from a partner's income should be somewhat different from those applicable to transactions between the partner and the partnership which result in taxable income to one or the other.

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[19] In its report on the 1954 Code, the Conference Committee observed:

> No inference is intended, however, that a partnership is to be considered as a separate entity for the purpose of applying other provisions of the internal revenue laws if the concept of the partnership as a collection of individuals is more appropriate for such provisions.

H.R. REP. NO. 2543, 83d Cong., 2d Sess. 59 (1954). In a footnote the court considered this difficulty and rejected the argument that section 119 is a provision where the aggregate concept is more appropriate than the entity view. 394 F.2d at 663 n.8. However, the court's rather cursory treatment of this issue is considerably less than convincing.