

NOTES

CONTEMPT BY PUBLICATION*

NEWSPAPERS and radio stations,¹ in response to popular demand, devote a great deal of space and time to reports of crime, police hunts and trials. Though a sensational trial may be "good copy," a sensitive judge may see in lurid accounts and colorful comments a threat to impartial justice.² Should he cite an offending news organ for contempt, the judge will invoke the constitutional right of an accused to a fair trial.³ The news organ will invoke in return the constitutional right to free expression.⁴ When these funda-

* *Baltimore Radio Show v. Maryland*, 67 A.2d 497 (Md. 1949), *cert. denied*, 18 U.S.L. WEEK 4090 (U.S. Jan. 9, 1950).

1. Although this Note mentions specifically only the press and radio, these do not exhaust the list of "publications" which have been held in contempt. See, *c.g.*, *Ex parte McMahon*, [1936] 2 All E.R. 1514 (K.B.) (newsreels); *Ex parte Craig*, 282 Fed. 138 (2d Cir. 1922), *aff'd*, 263 U.S. 255 (1923) (private correspondence). There is no reason to think that the list cannot be extended to include such innovations as television broadcasts or courthouse picketing.

2. Even where impartial justice is not at stake, publications have been punished for threatening judicial dignity. See Niles, *Contempt of Court by Publication*, 45 TRANSACTIONS MD. STATE BAR ASS'N. 101, 138-44 (1940). The better authority, however, indicates that contempt by publication will not be sustained unless something more than personal feelings have been hurt. See *Pennekamp v. Florida*, 328 U.S. 331, 372 (1946) (concurring opinion); *Craig v. Hecht*, 263 U.S. 255, 281 (1923) (dissenting opinion). Public opinion does not seem willing to make judicial officers any more immune from personal criticism than other government officials. See results of Gallup poll, reported in Niles, *supra*, at 111.

3. The constitutional right to a fair trial must be granted by state and federal courts alike. *Moore v. Dempsey*, 261 U.S. 86 (1923). Exactly what constitutes fair trial, however, has never been entirely settled: not all the provisions of Amendments Five through Eight are applicable to the states through the Due Process Clause of the Fourteenth Amendment. See the discussion in *Adamson v. California*, 332 U.S. 46 (1947). But some requirements, such as freedom from mob domination, have been held definitely included in fair trial. *Moore v. Dempsey*, *supra*. While the states are free to work out their own methods for the administration of criminal law, when a method has been chosen, it is subject to the prohibition against denial of due process. *Ibid.* Therefore, although the right to a jury trial embodied in the Sixth Amendment is not one of the Bill of Rights provisions binding on the states, when jury trial is guaranteed in a state constitution that state must insure the fair administration of the system. See the implications of this requirement in the *Baltimore Radio* case, note 14 *infra*.

4. The free expression guaranteed in the First Amendment is also protected by the Fourteenth from impairment by the states. See *Gitlow v. New York*, 268 U.S. 652, 666 (1925). But if the First Amendment includes only the English common law prohibition against *previous* restraints on speech, it may be no bar to contempt punishment *after* publication. Recent opinion, however, regards this distinction as specious, and holds that the First Amendment prohibits *all* restraints. See CHAFFEE, *FREE SPEECH IN THE UNITED STATES* 9 *et seq.* (1941).

mental rights seem to clash head-on, where and on what basis should a line be drawn?⁵

In reviewing the use by state courts of "contempt by publication," the Supreme Court has developed the following formula: out-of-court publications can be punished summarily when they constitute a "clear and present danger" to impartial judgment of pending cases.⁶ In no case, however, has the Court found a danger "clear and present" enough to justify punishment.⁷ Thus the Supreme Court formula has been called a grant to newspapers of virtual immunity⁸ rather than a compromise of their historic struggle with the courts.⁹

Nevertheless, the actual scope of this immunity has remained somewhat uncertain. In each of the Supreme Court cases the danger asserted was to judge, not jury, deliberations.¹⁰ Although no explicit distinction was made, the

5. The direct and sometimes bewildering nature of the clash was illustrated in the lower court hearing of the *Baltimore Radio* case when the American Civil Liberties Union, supporting free press, found itself arrayed against the Maryland Civil Liberties Committee, which supported fair trial. Brief for Appellant, app. p. 54, *Baltimore Radio Show v. Maryland*, 67 A.2d 497 (Md. 1949).

6. A case may be "pending" from the time of the issuance of a warrant for arrest (in a criminal case) or the filing of a complaint (in a civil action) until the final disposition of a case on appeal. "The decisive consideration is whether the judge or jury is, or presently will be, pondering a decision that comment seeks to affect." See *Pennekamp v. Florida*, *supra*, at 369 (concurring opinion). See also *Ex parte Craig*, 282 Fed. 138, 159-60 (1922) (dissenting opinion).

7. In all the Supreme Court cases the contempt findings of the state courts were reversed. *Craig v. Harney*, 331 U.S. 367 (1947) (newspaper articles attacking judge during his repeated refusals to accept jury verdict); *Pennekamp v. Florida*, 328 U.S. 331 (1946) (articles criticizing judge for throwing out criminal indictments); *Bridges v. California*, 314 U.S. 252 (1941) (telegram and articles calculated to influence judge in determination of sentence).

8. The construction given "clear and present danger" in the *Craig* case suggested that state courts would be prevented entirely from using contempt by publication, as are the federal courts, see note 26 *infra*. See the complaint by Mr. Justice Frankfurter in *Craig v. Harney*, 331 U.S. 367, 391 (1947) (dissenting opinion): "Hereafter, states cannot deal with direct attempts to influence the disposition of a pending controversy by a summary proceeding, except when the misbehavior physically prevents proceedings from going on in court, or occurs within its immediate proximity." A similar conclusion was voiced by supporters of the decision. See, e.g., Barth, *Freedom from Contempt*, Nieman Reports, April, 1949, p. 11. See also, Note, 23 IND. L.J. 192, 203 (1948).

9. The struggle for power between press and judiciary has sometimes been intensified by their support of opposing sides in important economic issues. See, e.g., Nelles & King, *Contempt by Publication*, 28 COL. L. REV. 525, 543 (1928), discussing *Toledo Newspaper Co. v. United States*, 247 U.S. 402 (1918) (judicial management of public service corporations) and the impeachment trial of Judge James H. Peck (land speculation). See also *Ex parte Craig*, 282 Fed. 138 (2d Cir. 1922), *aff'd*, 263 U.S. 255 (1923); Hale, *Public Opinion as Contempt of Court*, 58 AM. L. REV. 481 (1924).

10. See note 7 *supra*. The judge in *Craig v. Harney*, 331 U.S. 367 (1947) was a layman holding temporary appointment rather than a regular member of the judiciary. The Supreme Court, however, still felt that he was able to resist newspaper influence. See note 18 *infra*.

opinions left room for the inference that the "clear and present danger" test might have led to different results had jury decisions been threatened. If jurors could be shown more susceptible to influence than judges, then the same comment which constituted no danger in the one instance could still be found a danger in the other.

The judge-jury distinction was advanced for the first time in the recent case of *Baltimore Radio Show v. Maryland*.¹¹ Three Baltimore radio stations, describing the capture of a Negro murder suspect, emphasized police reports of his previous criminal record and his alleged confession.¹² The defendant, claiming the broadcasts made it impossible to find impartial jurors, elected to waive his right to a jury trial.¹³ Because the defendant found this necessary, a Baltimore court concluded that the broadcasts were in fact an interference with fair trial.¹⁴ In accordance with a local rule of court,¹⁵

11. 67 A.2d 497 (Md. 1949), *cert. denied*, 18 U.S.L. WEEK 4090 (U.S. Jan. 9, 1950).

12. "After three days of unrelenting hard work on the part of every man in the department, the Baltimore police have just broken the Brill murder case—broken it wide open. Police Commissioner Hamilton R. Atkinson announced only a few moments ago that a man has been arrested and formally charged with the crime—the brutal and apparently pointless stabbing of eleven-year-old Marsha Brill in the Pimlico neighborhood Tuesday afternoon. The funeral of the little murder victim was held today and hundreds of persons attended. The man now charged with the Brill girl's murder is Eugene James, a 31-year-old Negro and convicted former offender, whose home is . . . not far from the scene of the crime.

"The police said James not only admitted the Brill murder and another recent assault in the same area but that he went over the scene of the crime with them late this afternoon and showed them where the murder weapon was buried. It turned out to be an old kitchen carving knife. Immediately after the finding of the knife the prisoner was taken downtown to police headquarters for a formal statement. The story of how James came to be charged with the Brill murder is an account of police work at its best. James was taken into custody yesterday mainly because of his record. Police remembered that he had been charged or suspected in past years with a series of assaults and that about ten years ago he was sentenced to the Maryland penitentiary for an attack on a ten-year-old child. . . ." *Baltimore Radio Show v. Maryland*, 67 A.2d 497, 500-1 (Md. 1949) (quoting one radio bulletin).

13. This right is guaranteed in Md. CONST. Art. V.

14. *In re Maryland Broadcasting Co.* (Balt. Cr. Ct., 1949), summarized in 17 U.S.L. WEEK 2381 (Feb. 22, 1949). For fuller quotation of the lower court opinion see *Maryland v. Baltimore Radio Show*, 18 U.S.L. WEEK 4090 (U.S. Jan. 9, 1950). Whether the facts of this case support a conclusion that the defendant was deprived of a fair trial in a constitutional sense is somewhat debatable. Factors which so far have been held to violate due process have been matters rather obviously prejudicial. See note 3, *supra*. Here the Baltimore Court was presented with no affirmative showing that the broadcasts actually made impartial jury trial impossible: it accepted speculation on this point by defendant's counsel as conclusive. See *Maryland v. Baltimore Radio Show*, 18 U.S.L. WEEK 4090, 4091 (U.S. Jan. 9, 1950). Furthermore, cross-examination forced the admission that defendant might have waived his jury trial right for other reasons. See Brief for Appellant, app. pp. 37-8, *Baltimore Radio Show v. Maryland*, 67 A.2d 497 (Md. 1949).

15. Rule 904 of the Rules of the Supreme Bench of Baltimore City:

"In connection with any case which may be pending in the Criminal Court of Balti-

it cited the three stations for contempt. The Court of Appeals of Maryland, reversing, held that the decision and the rule under which it was made were invalid restraints on the freedoms of speech and press.¹⁶ Following the Supreme Court formula, it expressly based its reversal on a finding that no "clear and present danger" to justice had resulted.¹⁷ In so doing, the court rejected the argument that jurors require more protection from potentially prejudicial comment than judges.¹⁸

Unfortunately, the *Baltimore Radio* case did not eliminate the possibility of a future judge-jury distinction. The Supreme Court denied certiorari in an unusual opinion disavowing any implication that it approved the Maryland decision.¹⁹ The specific refusal to affirm leaves state courts free to decide

more, or in connection with any person charged with crime and in the custody of the Police . . . whether before or after indictment, any of the following acts shall be subject to punishment as contempt:

" . . .

"C. The issuance by the police authorities, the State's Attorney, counsel for the defense, or any other person having official connection with the case, of any statement relative to the conduct of the accused, statements or admissions made by the accused, or other matter bearing upon the issues to be tried.

" . . .

"E. The publication of any matter which may prevent a fair trial, improperly influence the court or the jury, or tend in any manner to interfere with the administration of justice.

"F. The publication of any matter obtained as a result of violation of this rule."

Full quotation of the rule may be found in *Baltimore Radio Show v. Maryland*, 67 A.2d 497, 505 (Md. 1949). For a history and analysis of the rule, see Niles, *supra* note 2, at 134; Sherbow, *Contempt of Court by Publication, Broadcast, and Television*, 53 TRANSACTIONS MD. STATE BAR ASS'N. 165 (1948).

16. Only paragraph E of the rule, note 15 *supra*, was specifically declared unconstitutional. The other paragraphs fell because the court felt they were not severable. 67 A.2d 497, 505-6 (Md. 1949).

17. 67 A.2d 497, 511 (Md. 1949).

18. "Judges are not so 'angelic' as to render them immune to human influences calculated to affect the rest of mankind. Conversely, while juries represent a cross-section of the community, it cannot be denied that in every community there are citizens who by training and character are capable of the same firmness and impartiality as the judiciary." *Id.* at 508-9. The dissenting opinion, on the other hand, argued that there were valid grounds for a distinction between judges and jurors. *Id.* at 518-21.

19. "The one thing that can be said with certainty about the Court's denial of Maryland's petition in this case is that it does not remotely imply approval or disapproval of what was said by the Court of Appeals of Maryland." *Maryland v. Baltimore Radio Show*, 18 U.S.L. WEEK 4090, 4092 (U.S. Jan. 9, 1950). Justice Frankfurter's nine-page opinion, followed by a sixteen-page appendix (see N.Y. Times, Jan. 10, 1950, p. 6, col. 3) gave a number of possible reasons for the Court's refusal to grant certiorari, ranging from "narrowly technical" ones to "pertinent considerations of judicial policy." 18 U.S.L. WEEK 4090, 4092. Which of these reasons was controlling in the present case the opinion kept a jealously guarded secret. Perhaps the reasons of "judicial policy" were simply that the Court was unable to decide the case. In view of the important issue of civil liberties involved, not to mention the need of the press for a definite standard of permissible reporting, it was certainly worth a try.

for themselves what limit the "clear and present danger" test sets on their power to restrict press comment during jury cases.²⁰ Moreover, the opinion, despite what appears to be a conscientious effort to confound interpretation,²¹ drops several hints that the Court is now ready to arrest, if not actually reverse, the previous trend toward newspaper immunity in judge as well as jury cases.²² In this respect as well, the opinion encourages state courts to revive summary punishment for comments which raise only the possibility of obstructing justice.²³

The real issue, obscured but not avoided by the judge-jury distinction and the "clear and present danger" test, is whether contempt by publication as

20. But the state courts have no guide in this determination. Justice Frankfurter, concealing his hand neatly, refused to say whether "either, or neither" the majority or dissenting opinion of the Maryland Court of Appeals had applied the "clear and present danger" test correctly. 18 U.S.L. WEEK 4090, 4092. Even in judge trials, none of the previous decisions indicates what facts, if any, present a danger "clear and present" enough to support a finding of contempt. See note 7 *supra*. The ambiguity of the test is so complete that it affords no real guide even to the Supreme Court (witness its denial of certiorari). In addition, the test often obscures the real policy considerations involved. See the excellent analysis in Riesman, *Civil Liberties in a Period of Transition*, 3 PUBLIC POLICY 33, 43 (1942): "[T]he [Supreme] Court takes into account, in addition to the nearness of the danger, the various factors, including *the value of the interests threatened*, which an intelligent legislator or administrator would also consider in determining whether to adopt a measure of repression. The formula of clear and present danger may help . . . to disguise this essentially legislative and administrative task of social judgment under words that appear more precise than they actually are, but there is always the risk that the Court, fooled by its own vocabulary or under its protection, may narrow the range of inquiry that is required if it is to assist the legislatures in framing an intelligent public policy." (emphasis added). On "clear and present danger" generally, see MEIKLEJOHN, *FREE SPEECH AND ITS RELATION TO SELF-GOVERNMENT* (1948).

21. See notes 19 and 20 *supra*.

22. The opinion was written by Justice Frankfurter, who has been leader of the Court minority seeking a rule more restrictive of press comment. This suggests that the death within the last year of Justices Murphy and Rutledge, strong supporters of newspaper freedom—see their concurring opinions, in *Pennekamp v. Florida*, 328 U.S. 331, 369 and 370 (1945)—, may have altered the balance of power which in *Craig v. Harney*, 331 U.S. 367 (1947) was only 4 to 3. Justice Frankfurter's opinion, furthermore, quoted at some length the findings with which the Baltimore Court justified its contempt citation, 18 U.S.L. WEEK, 4090-2, but devoted only a single paragraph to the rationale of the Maryland Court of Appeals. *Id.* at 4092. It referred to the "mutilation and distortion" of criminal justice by "extraneous influences." *Id.* at 4093. And it concluded with reference to the English contempt rule (extremely strict in its suppression of press comment, see note 23, *infra*) followed by a lengthy catalogue of British cases. *Id.* at 4093 *et seq.*

23. Punishment for possible obstruction is the rule in England, where, once a case is pending (see note 6 *supra*) nothing may be published which might tend to prejudice an impartial trial. 7 HALSBURY, *LAWS OF ENGLAND* 280-8 (1909). Compare the support of the rule in Goodhart, *Newspapers and Contempt of Court in English Law*, 48 HARV. L. REV. 885 (1935) with the misgivings expressed by Laski, *Procedure for Constructive Contempt in England*, 41 HARV. L. REV. 1031 (1928). For citation of relevant English cases, see 18 U.S.L. WEEK 4090, 4093 *et seq.* See also the case of Silvester Bolam, editor of the London "Daily Mirror," who was sent to jail for three months after publication of

a special category of crime should be permitted at all. The argument for restricting press comment is strongest in jury trials of criminal cases. In these the interference of comment with fair trial is asserted to be greatest,²⁴ the interference of a restrictive rule with free expression to be least.²⁵ Yet even here, the federal courts²⁶ and a minority of states²⁷ leave newsmen free unless the object of their out-of-court activities is intimidation or violence.²³

confession stories in connection with the Haigh murder case. N.Y. Herald Tribune, March 26, 1949, p. 1, col. 7.

Even if a rule extremely restrictive of free press has been successful in England, there is no reason to assume that all, or part of it, could be successfully transplanted to the United States. *Pennekamp v. Florida*, 328 U.S. 331, 359 *et seq.* (1945) (concurring opinion). Differing institutions, traditions, and public attitudes should give pause to even the most notorious Anglophile. There are also differences in trial procedure in the two countries which may justify the existence of different rules. See notes 43 and 52 *infra*.

24. The main assumption behind the judge-jury distinction is the greater susceptibility of jurors to influence. And the result of a biased verdict is more serious in a criminal case.

25. Jury trials of criminal cases in general raise fewer broad social issues than now devolve upon judges. For the increasing social function performed by the latter, and the consequent need for unrestricted comment on judicial activity, see Seagle, *Contempt of Court* in 4 ENCYC. SOC. SCI. 302, 307 (1931).

26. Except for misbehavior of its officers or disobedience to its lawful command, a federal court can punish summarily only for "misbehavior of [a] person in its presence, or so near thereto as to obstruct the administration of justice." 4 STAT. 487 (1831), as amended, 18 U.S.C. §§ 401, 402, 3691 (Supp. II 1946) (emphasis added). The italicized phrase was interpreted literally for some seventy years after passage of the original Act. See *Nelles & King*, *supra* note 9, at 525-43. Then in *Toledo Newspaper Co. v. United States*, 247 U.S. 402 (1918), the phrase was given a causal rather than a geographic construction; that is, punishment was permitted for out-of-court comment whose effect was felt in court. Finally, in *Nye v. United States*, 313 U.S. 33 (1941), the Supreme Court restored the literal meaning of the phrase.

27. Contempt by publication seems permanently abolished by statute in New York, Pennsylvania, and Kentucky. For a compilation of the state laws, see *Nelles & King*, *supra* note 9, at 554-62. The New York law allows a special exception for the publication of a "false, or grossly inaccurate report" of a court proceeding. N.Y. JUDICIARY LAW § 750 (6).

28. 4 STAT. 488 (1831), as amended, 18 U.S.C. § 1503 (Supp. II 1946): "Whoever corruptly, or by threats or force . . . endeavors to influence, intimidate, or impede, any witness . . . or any grand or petit juror . . . or . . . corruptly, or by threats or force . . . influences, obstructs, or impedes, or endeavors to influence, obstruct, or impede, the due administration of justice shall be fined not more than \$5000 or imprisoned not more than five years, or both." The terms "obstruct" or "impede," as used in the Act, refer only to direct acts of violence or menace, disturbing the ordinary functions of the court. See *United States v. Seeley*, Fed. Cas. No. 16,248a (C.C.S.D.N.Y. 1844). The term "influence" has never been clearly defined, but the Act specifically confines punishment to influence which is attempted "corruptly, or by threats or force." Thus a newspaper could be prosecuted under the Act only if it sought to intimidate jurors or cause physical obstruction. Presumably, this would never occur as long as a newspaper was operating in a legitimate editorial capacity.

Of course, if newsmen misbehave in the court itself, they are subject to summary punishment in the same manner as everyone else, see note 26 *supra*.

Moreover, offenders are punished not summarily but only after indictment and trial by jury.²⁹

A contempt rule which punishes for something less than tangible interference with justice is dangerously vague. It throws upon the would-be publisher the burden of guessing in advance whether or not his story will bring down the wrath of the court. Since most newsmen are not noted for their timidity, this uncertainty by itself may not cause a substantial curtailment of harmless information. But judges are not timid either, and a loose standard can be easily abused.³⁰ Judges have sometimes gone to absurd lengths in warding off fancied dangers to justice: newspapers have been brought to bar for mentioning by way of warning the criminal record of an escaped prisoner,³¹ for alluding to a defendant's financial and domestic misfortunes,³² and for stating that a youth had reported the accidental shooting of a playmate.³³ Such absurdities are the natural results of a rule which gives complete discretion to punish for mere threats. The very narration of the bare circumstances of a crime can hardly avoid mention of some fact that may ultimately be in issue.³⁴ Carried to its logical extreme, contempt by publication would allow a news report to state only who had been arrested and for what crime; or perhaps even this alone might in some circumstances be considered prejudicial.³⁵

The rule harms the public no less than the press. A general inhibition on

29. See note 26 *supra*, and Frankfurter & Landis, *Power of Congress over Procedure in "Inferior" Federal Courts*, 37 HARV. L. REV. 1010, 1037 (1924).

The present federal requirement of indictment and jury trial for contempts committed by persons out of court was also the requirement of the early common law. See FOX, *THE HISTORY OF CONTEMPT OF COURT* (1927).

30. The decision whether or not to punish for contempt is usually that of the same judge who presided over the trial allegedly endangered by the publication. The tendency of an appellate court to accept his findings makes a single opinion decisive. See, generally, Hale, *supra* note 9, at 494.

31. *Davis v. Baillie*, [1946] V.L.R. 485, as cited in 21 AUST. L. J. 54 (1947) (newspaper held in contempt).

32. The court felt this information would arouse public sympathy. *Hatfield v. Healy*, [1911] 3 A.L.R. 327 (newspaper held in contempt), as cited in Note, *Contempt of Court by Newspapers in England and Canada*, 16 CAN. B. REV. 273, 278 (1938).

33. *In re A. A. Abell Co.* (Balt. Cr. Ct. 1947), cited in Sherbow, *supra* note 15, at 177. Fortunately this was held only a "technical" contempt and no punishment was imposed. Other harsh cases are *United States v. Sullens*, 36 F.2d 230 (S.D. Miss. 1929) (newspaper punished for suggesting that politics, not justice, might determine outcome of a prosecution); *Rex v. Editor of New Statesman*, [1928] 44 T.L.R. 301 (K.B.) (punishment for suggesting that the religious convictions of a judge influenced his judgment in suit against birth-control advocate); *Rex v. Astor*, [1913] 30 T.L.R. 10 (K.B.) (punishment for printing together reports of separate civil and criminal proceedings).

34. Newspapers, according to one view, should be made to distinguish between facts and opinions given by witnesses to a crime. Sherbow, note 15 *supra*, at 181. Considering the difficulties encountered by lawyers and judges in making such distinctions, this suggestion seems rather impractical.

35. "The mere fact of arrest, or indictment, implies that the police believe the accused

criminal reporting would keep from circulation some material vitally needed by an informed electorate; political and economic issues raised by national defense, securities, and antitrust laws are now commonly involved in criminal cases.³⁶ Furthermore, comment would be prohibited on a whole range of collateral subjects in which reference to pending criminal cases is necessary for clarity and completeness.³⁷ Even in the direct reporting of common law crimes, where legitimate public interest seems lowest, the elimination of comment would not be an unmixed benefit. Accounts of arrests or confessions may quiet community anxiety;³⁸ descriptions of fugitives may safeguard the public and aid in capture. Most important, unrestricted comment is an important check on corrupt, inadequate, abusive, or politically dominated police and judicial authority.³⁹

The harm of repression is hardly cured by the fact that matter published after a case is no longer pending is not subject to contempt. Modern criminal prosecutions last for many months, even years, and often result in several trials on one issue or related issues. When unrestricted comment finally becomes permissible, it is of little interest or utility—freedom to publish something when it no longer matters is no freedom at all.⁴⁰

to be guilty or that the Grand Jury has found a *prima facie* case." *Baltimore Radio Show v. Maryland*, 67 A.2d 497, 511 (Md. 1949).

36. Some recent illustrations of significant jury trials include the trial of the eleven Communist leaders for violation of the Smith Act, the criminal prosecution of the American Tobacco Company on antitrust charges, and the trial of Preston Tucker and his associates for fraud in management of the Tucker automobile company. In the latter case, Tucker's counsel moved to cite *Collier's* and the *Reader's Digest* for contempt because they printed articles describing the history of the enterprise. *N.Y. Times*, Oct. 4, 1949, p. 46, col. 1. However, the existence of the federal rule made the motion little more than a gesture.

37. A recent case in Pasco, Wash., provides an excellent example. Suit was brought by a construction company to collect delinquent payments on a home purchase contract. A series of illustrated newspaper articles criticizing the quality of the homes was suppressed on the ground that, although unconnected with the suit, they might influence its outcome. The restraining order was later dissolved. *N.Y. Times*, Nov. 23, 1949, p. 3, col. 4.

Another illustration was offered by novelist Rebecca West, who was forced by the English contempt rule to abandon a newspaper assignment on anti-Semitic riots in London. "The plain fact about these disturbances," she wrote, "was that they were highly artificial, being cooked up . . . to catch the Jewish and anti-Jewish votes for candidates . . . at a by-election that would occur if Mr. David Weitzman, the sitting member of Parliament . . . who was being tried for blackmarket offenses, were found guilty. About this I could not say one word, since it would be contempt of court to speculate, however indirectly, on the result of the trial." *New Yorker*, August 14, 1948, p. 28.

38. See *Baltimore Radio Show v. Maryland*, 67 A.2d 497, 511 (Md. 1949).

39. Publicity may also help to uncover the guilty or exonerate the innocent. See the examples in *Nelles & King*, *supra* note 9, at 549.

40. "Consistent and logical suppression of discussion likely to affect pending cases would mean . . . that some continuing public grievances could never be discussed at all." *Nelles & King*, *supra* note 9, at 550.

Damage to the public interest in free expression might have some justification if contempt by publication were of substantial benefit to the public interest in fair and impartial jury trials. There is no question, of course, but that press and radio comment has some effect on the operation of the judicial process.⁴¹ To the extent that mass media foster mass attitudes, they impair whatever ability the individual may have to balance law and evidence in a prejudice-proof atmosphere. More specifically, the release to jurors or potential jurors of material that may be held inadmissible at trial would seem to interfere in fact, if not in law,⁴² with impartial judgment.

Whether press and radio comment can actually alter the outcome of a particular trial, however, is doubtful. Impartial verdicts formed only on the basis of courtroom evidence are supposed to be assured by the examination of jurors,⁴³ instructions from the judge, and, in the last resort, the power to declare a mistrial. If devices such as these fail to neutralize the predispositions of jurors, the fault lies not with the press, but with the system as a whole. Jury reaction to the facts of a case is the result of long conditioning by a multitude of environmental factors. Press comment makes its strongest impression when conforming to pre-existing stereotypes in the public mind;⁴⁴

41. See *e.g.*, TAFT, LAW REFORM 140-70 (1926); Robbins, *The Hauptmann Trial in the Light of English Criminal Procedure*, 21 A.B.A.J. 301 (1935). The Lindbergh kidnapping case is often referred to as the most flagrant example of "trial by newspaper." The summation for the prosecution contained an ill-disguised attempt to bring inflamed public opinion to bear upon the jury: "I am not concerned about what the mob is clamoring for . . . but you can bet your life that if there is a clamor from the people of this country for this man's conviction I have sufficient faith in the American people to know that it is their honest belief and conviction that he is a murderer. Otherwise, there would be no clamor if there is one." *Id.* at 305. The traditional summary power to punish in-court contempts may be the most effective way of checking prejudicial publicity in a case such as this. Furthermore, when interest is nationwide, contempt by publication is inadequate to check prejudice, because out-of-state newspapers cannot be punished.

42. When evidence that might be inadmissible at trial reaches the jury through the press, this fact in itself, without a showing of actual prejudice, is not enough to prevent a trial or vitiate a verdict. *Welch v. United States*, 135 F.2d 465 (D.C. Cir. 1943); *Holt v. United States*, 218 U.S. 245, 251 (1910): "If the mere opportunity for prejudice or corruption is to raise a presumption that they exist, it will be hard to maintain jury trial under the conditions of the present day."

43. In contrast to the painstaking process of jury selection employed in the United States, English practice usually results in swearing in of the first twelve persons. Robbins, *supra* note 41, at 303. The absence of a device for weeding out bias at the impanelling stage may partly explain the severe British restriction on pre-trial newspaper comment, see note 23 *supra*.

44. See LIPPMANN, PUBLIC OPINION 61 (Pelican Books ed. 1946): "For the most part we do not first see, and then define, we define first and then see. In the great blooming, buzzing confusion of the outer world we pick out what our culture has already defined for us, and we tend to perceive that which we have picked out in the form stereotyped for us by our culture."

hence it tends to follow, rather than cause bias.⁴⁵ Viewed in this light, the suppression of news reporting during a trial cannot eliminate prejudice or even substantially reduce it. Instead it represents a crude attempt to insulate the jury from the prevailing climate of opinion.⁴⁶

The effect of inflammatory reporting in large metropolitan communities, where it is most likely to occur, is especially open to question. The daily sensations that are repeated to a sophisticated population are seldom remembered,⁴⁷ nor are they effective in shaping attitudes.⁴⁸ Given large jury lists and the lack of homogeneity of these communities, it should always be possible to find twelve persons whose minds have not been poisoned by pre-trial sensationalism.

The danger of pervasive prejudice is more serious in smaller communities.⁴⁹ But here there are better remedies than contempt by publication. If reporting results in actual courtroom obstruction or violence, those responsible can be indicted and punished.⁵⁰ For more subtle threats to justice,

45. The "pressure of the audience" is recognized in COMMITTEE ON FREEDOM OF THE PRESS, A FREE AND RESPONSIBLE PRESS 57 (1947). When the press attempts to lead opinion rather than follow, it is often unsuccessful: witness the ineffectiveness of overwhelmingly Republican newspaper opinion in the last four presidential elections.

46. "You might as well attempt to stop the flowing of the tide, lest it might overwhelm the temporary hut of the fisherman upon the shore, as to arrest the march of public opinion in this country, because in its course it might incidentally affect the merits of a cause depending between individuals." James Buchanan, quoted in STANSBURY, REPORT OF THE TRIAL OF JAMES H. PECK 448 (1833).

47. Judges in these communities find that the continuous succession of sensational reporting "in the end produces no impression. It is common experience in the most notorious cases to meet a succession of talesmen who have read nothing of the matter, and an even more frequent occurrence is it to encounter those who can recall nothing of what they have read." *People v. Broady*, 90 N.Y.S.2d 864, 865 (Sup. Ct. 1949).

48. A public opinion survey taken by Cornelius Du Bois, Inc., was attached to the motion of Alger Hiss for change of venue on grounds of newspaper-fostered prejudice in New York City. 45.1% of New Yorkers questioned said they had formed opinions on the guilt or innocence of Hiss, compared to only 33.8% of those interviewed in Rutland, Vt., to which Hiss sought to have his second trial removed. But the survey yielded some unexpected results: In New York, 21.8% of those interviewed thought Hiss guilty, 12.1% thought him innocent; in Rutland, 23.1% thought him guilty, only 5.9% thought him innocent. *United States v. Hiss*, Affidavit for Change of Venue, Exhibit B. The fact that less coverage of the case and less anti-Hiss newspaper sentiment occurred in Rutland did not support the asserted conclusion that trial there would be more fair. Apparently, the conservative predisposition of Vermonters was more effective in setting public opinion against Hiss than hostile newspaper publicity in New York. See notes 44 and 45 *supra*.

49. The most frequent opportunities for newspapers to mobilize sentiment against an accused occur in small southern communities when a Negro is defendant. For a recent example, see *Press Performance and Justice*, American Newspaper Guild Reporter, Sept. 23, 1949, p. 10, col. 2. If community prejudice is really widespread, it may reach the judge. In such a case, contempt by publication would probably be of no use anyway—the judge could decline to use it.

50. All states have laws, similar to that in the federal courts, against intimidation of jurors or witnesses, or direct incitement to violence. See note 28 *supra*.

change of venue can be employed.⁵¹ The reach of the press and the radio is rarely so wide that no community can be found where a fair trial is possible.

Even if the evils of news reporting were more real than imaginary, contempt by publication would not be an effective antidote. Prior convictions, confessions, or other allegedly prejudicial material which the rule seeks to suppress often come into evidence through authorized trial procedure.⁵² The object of the rule is further frustrated by the well-established right to report preliminary hearings, trial proceedings, and disposition of cases on appeal.⁵³ These reports of judicial activity often do the most to form attitudes toward a defendant. Details of an earlier trial linger in the minds of jurors called upon to try another case involving the same defendant. Little will be gained by suppressing facts during the subsequent trial that already have become matters of public record or common knowledge.⁵⁴

One source of outside pressure on jury trials can be eliminated, however—the release of facts and opinions, before or during litigation, by

51. Judges have recognized that the probability of all-pervasive prejudice tends to vary inversely with the size of the community—and have acted accordingly. *E.g.*, *People v. Broady*, 90 N.Y.S.2d 864 (Sup. Ct. 1949) (trial in metropolitan New York, change of venue denied); *People v. Fernandez*, 89 N.Y.S.2d 421 (Sup. Ct. 1949) (trial in Nassau County, change of venue granted).

52. This actually happened in the *Baltimore Radio* case. See *Baltimore Radio Show v. Maryland*, 67 A.2d 497, 504 (Md. 1949).

The American juror who reads of a confession in the press is usually more cynical as to its validity and more likely to learn of it eventually in court than his English counterpart. This results from the fact that the rules for admission of a confession in evidence are far more strict in England than America, and from the fact that the role of the police in obtaining confessions is more rigidly circumscribed. 3 WIGMORE, EVIDENCE 290 *et seq.* (3d ed. 1940). These differences in procedure may help explain why Britain feels the need for more severe restriction of confession disclosures by the press. See notes 23 and 43 *supra*.

53. This fact was recognized in the lower court hearing of the *Baltimore Radio* case, but was disposed of rather glibly: "We have pointed out that there can be published or broadcast, after a preliminary hearing, those matters developed at the preliminary hearing, including the admission of a confession; and that information then published could be as disastrous to a defendant as was the publication here before the preliminary hearing. Gentlemen, that is one of the respects in which the right of the defendant must yield to the paramount right to make available to the public the court proceedings." See Brief for Appellant, app. pp. 67-8. The distinction between the right to make court proceedings available to the public and the right to report the background of these proceedings is not so obvious as to justify labelling the first, but not the second, a "paramount right."

54. Two other factors point up the futility of contempt by publication as a method for keeping allegedly prejudicial material from the jury. The first is the inability of state courts to control out-of-state media of communication. Thus in the *Baltimore Radio* case the lower court was powerless to do anything about reports reaching Baltimore from newspapers and radio stations in Washington, D.C. The second factor is the possibility of rumor replacing the silenced media as an agent of communication. Circulation of distorted reports by word-of-mouth presents an even greater possibility of jury prejudice.

police,⁵⁵ parties,⁵⁶ attorneys⁵⁷ and jurors.⁵⁸ Here again, the best preventive is not contempt by publication, which strikes only at the media of communication, but rather the traditional summary power, employed against the persons who directly offend the court by releasing objectionable material.⁵⁹ If prejudicial reports do in fact threaten jury trials, then this remedy has the advantage of cutting the worst of them off at their source. It also entails less danger to free speech, because it disciplines those who owe an implied duty of silence, rather than those who only repeat public statements.⁶⁰

There seems to be no justification, then, for punishing press and radio reports unless they actually cause intimidation or violence. In most situations, contempt by publication contributes little to a fair trial. Where it could have a beneficial effect, there are better measures available as substitutes.⁶¹

55. The trading by police of confidential information in return for favorable newspaper publicity has become increasingly frequent. It seems to have occurred in the *Baltimore Radio* case, see note 12 *supra*. See also Niles, *supra* note 2, at 144. The first step to correct this practice can be taken within the police department itself. The second, summary punishment, can be used as a last resort and justified on the ground that police are court officers who owe a duty to obey judicial commands. See Rule 904(C) of the Supreme Bench of Baltimore City, note 15 *supra*.

56. The recent advertising campaign carried on by the Atlantic & Pacific Tea Co., defendant in a civil antitrust action, seems a frank attempt made by a party to affect the outcome of litigation. Perhaps advertising of this nature in a criminal jury trial should be prevented by the threat of summary punishment.

57. The most objectionable aspects of the Hauptmann Trial might have been avoided had counsel for state and defense not been permitted to argue their respective cases to the press—disclosing evidence, legal issues, and future strategy. See Robbins, *supra* note 41.

58. Release of jurors' opinions after a case can also be prejudicial if a re-trial is necessary. Thus it was unfortunate that the members of the jury in the first Hiss trial were permitted to tell the press not only how they voted, but what they thought of one another; for example, "the foreman was emotional, two were blockheads and one was a dope." N.Y. Journal-American, July 9, 1949. Some even went so far as to express their opinions on the judge's evidentiary rulings. *Five Hiss Jurors Express Belief Kaufman was Biased for Defense*, N.Y. Herald-Tribune, July 12, 1949, p. 1, col. 7.

59. Paragraph C of the Baltimore Criminal Court Rule sought to achieve this result. See notes 15 and 16 *supra*. Even in the absence of an express rule, it should be possible for a judge to punish summarily any participant in litigation who violates reasonable instructions as to permissible disclosures, such as an order to the jury not to discuss its verdict with the press.

60. This method, by preserving the maximum amount of free speech and fair trial, seems most in accord with the injunction of Chief Justice Marshall: "so to construe the constitution as to give effect to [conflicting] provisions, as far as it is possible to reconcile them, and not to permit their seeming repugnancy to destroy each other." *Cohens v. Virginia*, 6 Wheat. 264, 393 (U.S. 1821).

Cf. *Craig v. Harney*, 331 U.S. 367, 375 (1947) (referring to newspaper articles which quoted anti-judge resolutions of a citizens' group): "Whatever may be the responsibility of the group which [promulgated the resolutions], those who reported it stand in a different position. Even if the former were guilty of contempt, freedom of the press may not be denied a newspaper which brings their conduct to the public eye."

61. If the previous analysis has been correct, the abolition of contempt by publication can admit of no exception. There is little merit, for example, in the suggestion that some

The Supreme Court, instead of temporizing, should make the federal contempt rule binding on the states.⁶² Then newsmen, like others persons, will be guaranteed a jury trial for out-of-court activities alleged to be illegal, and the standard of guilt will be a concrete one of direct and tangible obstruction.⁶³ This approach would be more in accord with a constitutional tradition that has long protected the public interest in free expression.⁶⁴

power be retained to prevent the "worst" kinds of press and radio disclosures (presumably confession reports in crimes of violence). Such advance classification of permissible and non-permissible reporting offends even the "clear and present danger" test. No class of comment is so intrinsically harmful that in all circumstances its value as public information is outweighed by the injury it does to fair trial. Even supporters of restriction recognize the futility of banning only one particular class of comment. See Niles, *supra* note 2, at 136 (referring to Baltimore Rule): "The prohibition of publication of accounts of the conduct of the accused, forecasts of the future course of action of either side in the case, or 'other matter bearing upon the issues to be tried,' is simply an itemization of less obviously prejudicial publications than reports of actual confessions."

62. The federal contempt rule as now interpreted, see note 26 *supra*, not only reflects the better social policy—it is held by some to be demanded by the language of the Constitution itself. If this view is correct, then the abolition of summary punishment for out-of-court publications is not only desirable but mandatory for state courts. See note 4 *supra*. Strong support for this contention may be found in Nelles & King, *supra* note 9, at 533: "The [federal contempt statute] was more than a legislative election as to Federal policy. It expressed a decision of the whole people upon an issue of sovereignty which had arisen between them and some of their judicial ministers. It responded to an almost universal conviction as to the nature of our institutions. If freedom was a fact of American life as well as an ornament of patriotic declamation, a discretionary power of judges to annex society at large to the judicial precincts and curtail outside expressions of human interests because such expressions might affect a pending law suit was more than inexpedient. It was impossible. The supposed English common law power, being inapplicable to American conditions, *could have no status in any American jurisdiction.*" (emphasis added).

63. See note 28 *supra*.

64. "Yellow journalism" is as old as the Constitution itself, and the reason for permitting it is still the same one emphasized by Thomas Jefferson: "I deplore . . . the putrid state into which our newspapers have passed, and the malignity, the vulgarity, and the mendacious spirit of those who write them. . . . These ordures are rapidly depraving the public taste. It is, however, an evil for which there is no remedy; our liberty depends on the freedom of the press, and that cannot be limited without being lost." Quoted in PADOVER, THOMAS JEFFERSON 150-51 (1943). Compare the statement of Justice Rutledge in *Pennekamp v. Florida*, 328 U.S. 331, 371-2 (1946) (concurring opinion): "There must be some room for misstatement of fact, as well as for misjudgment, if the press and others are to function as critical agencies in our democracy concerning [the] courts as for all instruments of government."

No one questions the evil of sensationalism. The recent preoccupation of the American press with the commission of sex crimes may even be cause for alarm. Intelligent newsmen are the first to realize that by reporting criminal activity with "zestful disapproval" the press and radio may well contribute to its increase. See John Crosby, *Is Sex Necessary*, N.Y. Herald-Tribune, Dec. 9, 1949, p. 21, col. 7. But the evil is not one which can be corrected by sporadic judicial censorship. Good journalism will never be achieved by threats or legislation; it will come only with public education and reform within the profession itself. See COMMITTEE ON FREEDOM OF THE PRESS, A FREE AND RESPONSIBLE PRESS (1947) *passim*.

AMORTIZABLE PREMIUM ON CONVERTIBLE BONDS: THE SPECULATOR SEEKS A TAX LOOPHOLE*

WHEN a bond is bought for more than its face value, the purchaser may treat the transaction in one of two ways for accounting purposes. He may consider the premium as an expense of earning income and deduct a pro rata share of the total premium from the yearly interest earned by the bond.¹ Or he may consider the premium as being added to the permanent cost of the bond, so that when he redeems the bond at par, he realizes a capital loss. The former method will give a more accurate picture of the holder's earnings during the life of the bond, because it recognizes that the interest income is really not received free and clear but was bought at a price—the excess of the purchase price over face value. Section 125 of the Internal Revenue Code recognizes this preferable accounting practice by permitting an annual income deduction for “amortizable bond premium.”

While the statute sanctions any reasonable method of amortization which the holder of the bond has regularly employed,² it leaves “amortizable bond premium” undefined. Usually a purchaser will pay a premium in order to obtain a superior investment yield. But this is not the only reason premiums are paid. Many bonds are convertible into stock. These convertible bonds carry conversion features which might give them speculative value. The purchaser of these bonds is paying not for the investment yield but for the speculative features. Unfortunately, Section 125 makes no effort to distinguish between investment premium and speculative premium.³

Because no distinction is made, the prospective tax consequences under Section 125 are different for the two types of premium, and this difference can be extremely important where the bonds are callable. A purchaser of speculative premium in effect purchases stock. Convertibility ties the market value of the bond to high stock prices. Unlike normal investment premium,

* *Commissioner v. Korell*, 176 F.2d 152 (2d Cir. 1949); *Commissioner v. Shoong*, 177 F.2d 131 (9th Cir. 1949).

1. This technique, called amortization, is a familiar one, similar to the treatment of depreciation charges. By this method the entire premium has been recovered by maturity and no capital loss is suffered when the bond is redeemed at its nominal value. See PATON, ACCOUNTANTS' HANDBOOK 947 *et seq.* (3d ed. 1943); MONTGOMERY, AUDITING THEORY AND PRACTICE 201-202 (6th ed. 1940).

2. The Treasury recognizes methods of amortization required for purposes other than taxation. Thus, “A taxpayer who regularly employs a method of amortization may be one, for example, who is subject to the jurisdiction of a State or Federal regulatory agency and who, for the purposes of such agency, amortizes the bond premium on his bonds in accordance with a method prescribed or approved by such agency. . . .” U.S. Treas. Reg. 111, § 29.125-3 (1943).

3. Premium may be paid either for superior yield or for conversion features which give the bond speculative value, but not for both. No element of speculative premium is attributable to superior investment qualities. A purchaser will never pay more for the bond than the present price of the stock into which it is convertible, less the cost of conversion. See note 4 *infra*.

therefore, speculative premium does not automatically decline as the bond approaches maturity.⁴ If the convertible bond is callable on short notice, the bondholder may deduct his entire premium expense from income immediately.⁵ After taking this premium deduction out of earnings taxable as ordinary income, he may resell his bond after six months and report the amount of premium he then receives as a long-term capital gain,⁶ escaping the higher

4. An illustrative example of speculative bond behavior and the problems confronting the holder is given in GROSSMAN, *INVESTMENT PRINCIPLES AND PRACTICE* 34-5 (1939): In November, 1935, Allis-Chalmers Manufacturing Company issued \$15,000,000 of \$1000, 4% convertible debentures, due 1945 at face value. They were convertible into the common stock of the company at an exchange rate of \$35 per share, *i.e.*, each \$1000 bond was exchangeable for 28.57 shares of stock. At the time of issue the stock was selling on the New York Stock Exchange at about \$35 per share, but shortly thereafter it began a substantial advance and in March, 1936, it sold at \$45, an increase of 28%. This automatically made the price of the bonds advance proportionately to 128, or about \$1285 per \$1000 bond (\$1285.65 is the value of 28.57 shares of stock worth \$45 each). "What was the bondholder to do at this point? It was clear that the future market behavior of his bond would be determined by the action of the stock and the bond investor had, in effect, become a stock market speculator. Later, the stock advanced further and the bonds advanced as high as 219." A similar example is provided in FLYNN, *SECURITY SPECULATION* 37-8 (1934). The positions of a stock speculator and a convertible bond speculator are dissimilar only in that the latter is assured of a floor beneath his speculative purchase; his investment will never decline below the bond's redemption value.

On investment and speculative bonds in general, see, in addition to FLYNN and GROSSMAN, *supra*, CHAMBERLAIN, *THE PRINCIPLES OF BOND INVESTMENT* §§ 350, 351 (4th ed. 1911); Edwards, *Bonds* in 2 *ENCYC. SOC. SCI.* 634 (1930); Edie, *Investment*, in 8 *id.* 263 (1932); Hardy, *Speculation* in 14 *id.* 288 (1934).

As advancing stock prices alter the character of the bond from an investment to a speculative security, the terms of the conversion contract, for all practical purposes, change also. Where an issue is callable, the action of the obligor actually determines whether the conversion option will be exercised—even though the express terms of the indenture place the option solely with the holder. Thus, if the market price of the bond is above what its investment merit would ordinarily dictate and the issuing corporation decides to call the bonds, the effect of that call will be to force the holder to convert in order to salvage that portion of his capital, represented by the premium he paid, which would be lost if the bond were redeemed at its nominal value. This transfer of the option to convert from holder to obligor would seem to remove bonds in such a situation from the intended scope of the statute. The legislative reports clearly demonstrate that bonds come within § 125 only "if the option to convert the bond into stock rests with the owner of the bond. . . ." H.R. REP. NO. 2333, 77th Cong., 2d Sess. 80 (1942), 1942-2 *CUM. BULL.* 372, 433-4; SEN. REP. NO. 1631, 77th Cong., 2d Sess. 94 (1942), 1942-2 *CUM. BULL.* 504, 576.

5. In accordance with the stipulation of § 125(b) (1) that the amount of premium "shall be determined with reference . . . to the amount payable on maturity or on earlier call date," U.S. Treas. Reg. 111, § 29.125-5 (1943) provides that "in the case of a callable bond the earlier call date will be considered as the maturity date" for the purposes of determining the period over which amortization is to be spread.

6. By way of illustration: if a \$100 short-call bond is purchased at \$140, the purchaser will immediately amortize the entire \$40 and deduct it from ordinary income. Upon subsequent resale for \$140 (assuming no change in price) six months later, he will report \$40 as capital gain. The efficacy of this device depends on stable or rising stock prices. The market aspects are discussed in 63 *HARV. L. REV.* 171 (1949).

tax on ordinary income. If he converts his holding into stock, the same tax result will follow: the amortized bond premium has been deducted from income; there is no tax on conversion,⁷ and only a capital gains tax is paid on the sale of stock held for six months.

The purchaser of normal premium, on the other hand, gets no similar tax advantage from short call bonds. If the bond is callable at an early date, it will bear no more than a small premium because there is the danger that interest payments before the call date will not be sufficient to make up the premium. And even though the buyer pays a small premium and deducts it as an expense immediately, there is only a negligible probability of resale after six months at sufficient profit to make significant the conversion of ordinary income into a capital gain.⁸

The Code's failure specifically to distinguish speculative from investment premium has precipitated a conflict between the second and ninth circuits.⁹ Similar cases arising under the section involved three per cent convertible debentures of the American Telephone and Telegraph Company, callable on 30 days' notice. The conversion option was exercisable at any time, the holder to surrender one bond and pay \$40 for each share of stock desired. The bonds were purchased at an abnormally high premium and, significantly, at almost exactly \$40 below the market price of the common stock into which they were convertible. The price correlation was apparent. Both taxpayers claimed large deductions for amortizable premium under Treasury Regulations permitting immediate amortization of the entire premium paid on bonds callable on short notice.¹⁰ The Commissioner of Internal Revenue disallowed both claims.¹¹

7. The exercise of a conversion option is recognized by the Commissioner as an exception for exchanges in kind under §112(a) of the Code. The following was in Article 1563 of Regulation 45 (1920 ed.): "Where the owner of a bond exercises the right . . . of converting . . . into stock in the obligor corporation, such transaction does not result in a realization of profit or loss, the transaction not being closed . . . until such stock is sold." Although long since superseded by later Regulations, this statement has been held applicable under later acts by a series of Treasury rulings: MRM. 3156, II-2 CUM. BULL. 24 (1923); I.T. 2216, IV-2 *id.* 19 (1925); I.T. 2347, VI-1 *id.* 86 (1927); G.C.M. 18436, 1937-1 *id.* 101 (1937).

8. In its effect on investment premium, an early call date acts as a maturity date. Since the prospective total yield to maturity is the controlling factor, the ordinary bond will sell at a negligible premium as maturity, or the call date, draws near. Thus, if the non-convertible bond is called, the purchaser will have no opportunity to resell and enjoy "bootleg" capital gains. In the case of a convertible bondholder, however, calling simply forces conversion, and the fictional capital gain will follow as before on resale of his holdings, now in the form of stock.

9. Commissioner v. Korell, 176 F.2d 152 (2d Cir. 1949); Commissioner v. Shoong, 177 F.2d 131 (9th Cir. 1949).

10. See note 5 *supra*. The taxpayer's method of computation—amortizing the whole amount of premium over a 31-day period because the bonds were callable on 30 days' notice—was not challenged by the Commissioner. If the deduction were to be allowed there was no dispute as to the correct amount.

11. The Commissioner was overruled by the Tax Court. Korell v. Commissioner, 10

In *Commissioner v. Korell*,¹² the second circuit allowed the deduction. Although the court agreed that the premium had not been paid for a superior investment yield, it found nothing in the statute to justify limiting the deduction to investment premium.

In *Commissioner v. Shoong*,¹³ the ninth circuit adopted what it considered the obvious policy of Congress and disallowed the deduction. Extracting congressional policy from the act and its legislative history, the court buttressed its holding with the principle that deductions are to be construed strictly against the taxpayer.

The amendment's legislative history amply supports the ninth circuit's holding. Until 1942, the Internal Revenue Code required bondholders to deduct premium as a capital loss upon redemption, denying them the more favorable deduction of an expense out of current income.¹⁴ The adoption of Section 125 was instigated by a Treasury proposal which sought to correct this unfair tax treatment of bondholders by bringing the Code into line with sound accounting practice. The Treasury, however, evinced no concern with purely speculative bond transactions. Mr. Randolph Paul, Tax Advisor to the Secretary of the Treasury, explained to the House Ways and Means Committee the unfortunate tax position of bondholders who were taxed as though premium were a capital loss when actually it represented a reduction of income. His remarks can be applied only to investors, who are concerned with the problems of conserving the capital which yields their income in the form of interest.¹⁵

T.C. 1001 (1948); *Shoong v. Commissioner*, 7 CCH TAX COURT DEC. 367 (T.C.M. 1948), P-H 1948 TC MEM. DEC. ¶48,095 (1948).

12. 176 F.2d 152 (2d Cir. 1949).

13. 177 F.2d 131 (9th Cir. 1949).

14. "Under existing law, bond premium is treated as capital loss, sustained by the owner of the bond at the time of disposition or maturity and periodical payments on the bond at the nominal or coupon rate are treated in full as interest. The want of statutory recognition of the sound accounting practice of amortizing premium leads to incorrect tax results which in many instances are so serious that provision should be made for their avoidance." H.R. REP. No. 2333, 77th Cong., 2d Sess. 47 (1942); 1942-2 CUM. BULL. 372, 410. To the same effect is the statement of Randolph Paul, then Tax Advisor to the Secretary of the Treasury, *infra* note 15.

15. Mr. Paul's statement, which follows, indicates that the purposes of the recommended amendment were (1) to deprive holders of tax-free bonds of a tax windfall, and (2) to relieve other bondholders of an inequitable tax burden. In both cases, the problem dealt with was the relation between taxation and income production:

"(d) *Amortization of bond premium.* Holders of a tax-exempt security purchased at a premium are today in the unique position of being relieved of tax on the interest paid on the security and of receiving a deductible loss upon redemption or other disposition of the security to the extent of the premium. As the premium at which a bond is obtained represents to the holder merely an effective yield lower than the actual interest rate, the holder is entitled to tax exemption solely with respect to such effective yield. The difference between the yield and the actual interest rate is simply a return of capital and should be treated as such rather than as a capital loss. On the other hand, the holder of a taxable security purchased at a premium is in the unfortunate position of being taxed

Considerations quite apart from prospective interest yield guide a purchaser who—like taxpayers Korell and Shoong—offers a high premium for a bond whose value is hitched by a conversion option to climbing stock prices. He in effect purchases stock and calculates his capital risk by the probabilities of subsequent fluctuations in the price of the stock.¹⁶ In recognition of these economic differences, commercial usage treats investment bonds and speculative convertible bonds as separate species of securities.¹⁷ Consequently, the presumption arises that deductions for speculative premium were neither anticipated nor intended to be covered by Section 125. This presumption, moreover, is corroborated by the legislative committee reports,¹⁸ which duplicate the tenor of Mr. Paul's statement, and by survival of the substance of the Treasury proposal in final legislation.

The actual wording of the section may also indicate that the interest factor alone was meant to be significant in the operation of the law, since the section classifies bonds solely with reference to the type of interest they bear.¹⁹ The second circuit conceded that the disputed convertible bond premium bore no relation to the interest factor.²⁰ The ninth circuit, entertaining the same view,

upon the interest at high rates and of receiving a capital loss upon redemption whose deductibility is subject to the restrictions placed upon capital losses. Since the yield rather than the actual interest reflects the true income to the taxpayer, only that income should be subject to tax and the capital loss should disappear.

"Proper tax treatment in both situations may be obtained through amortization of the premium. It is suggested that such amortization be mandatory for wholly tax-exempt securities and for partially tax-exempt securities held by a corporation. For all other securities the amortization should be at the taxpayer's election." 1 *Hearings before Committee on Ways and Means on Revenue Revision of 1942*, 77th Cong., 2d Sess. 90 (1942). The statement is reprinted in full in the opinion of the ninth circuit, 177 F.2d 131, 134. In a recent communication to the YALE LAW JOURNAL, Mr. Paul confirms that his congressional statement was limited to problems of income production; he suggests, however, that others in the Treasury Department may without his knowledge have considered the broader problem at that time. Communication to the YALE LAW JOURNAL, Jan. 6, 1950, in Yale Law Library.

16. CHAMBERLAIN, *THE PRINCIPLES OF BOND INVESTMENT* c. 2, *Gambling, Speculation and Investment* (4th ed. 1911). See note 4 *supra*.

17. See FLYNN, *SECURITY SPECULATION* 34-3 (1934):

"An exception to this [that almost all security speculation takes place in common stock] is a type of bond known as a convertible bond. . . . Such bonds . . . partake of the nature of common stocks also and are often the subject of wild trading. . . ." *Id.* at 35. "[T]hese bonds are closely bound up in the fluctuations and speculative operations of the common stock. They are really not true bonds." *Id.* at 38. Similar distinction between ordinary and convertible, or speculative, bonds is made in BABSON, *INVESTMENT FUNDAMENTALS* 47, 226 (Rev. ed. 1933); BADGER, *INVESTMENT PRINCIPLES AND PRACTICES* 188-205 (1928); GRAHAM & DODD, *SECURITY ANALYSIS* 57-63, 237-93 (1934). See also note 4 *supra*.

18. H.R. REP. NO. 2333, 77th Cong., 2d Sess. 78 (1942), 1942-2 CUM. BULL. 372, 433; SEN. REP. NO. 1631, 77th Cong., 2d Sess. 92 (1942), 1942-2 CUM. BULL. 504, 574.

19. INT. REV. CODE § 125(a).

20. 176 F.2d 152, 153, 154.

found it impossible to justify the application of the section to such premium.²¹ The deduction allowed by the second circuit is inconsistent with other deductions provided in the Code. Those deductions are usually expenses incurred for the production of income. The premiums paid by taxpayers Korell and Shoong were not used to produce income; rather, they represent the purchase price of a speculative asset, and nowhere else does the Code permit deductions for such purchases.²²

Admittedly, the lack of precision in the statute may be attributable to legislative oversight. But despite the second circuit's superficially plausible argument that only the legislature should correct its own errors and supply its own omissions,²³ there is ample authority for the ninth circuit's restrictive interpretation of congressional intent. The rule that deductions are acts of legislative grace and should be construed against the taxpayer²⁴ is custom-tailored for this situation: general tax laws need its support to withstand the attacks of ingenious evasion. This rule alone should resolve the issue in favor of the Commissioner in the *Korell* and *Shoong* cases, particularly since the legislative history of the act seems clear and unambiguous.²⁵

21. 177 F.2d 131, 134.

22. INT. REV. CODE § 23.

23. 176 F.2d 152, 155. The court's rationale apparently rests on the assumption that to interpret congressional intent one way is to legislate, but to interpret it in another way is not. Since the legislators failed to define "amortizable bond premium," the problem is one of determining the meaning of the term. If that determination involves an invasion of the legislative process, it is an invasion no matter which meaning the court chooses to endorse.

Although the second circuit dismissed the government's argument which was based on legislative history, note 25 *infra*, it did rely on one isolated aspect of congressional history to support its own position. Convertible bonds had been mentioned in the Senate and House reports, see note 4 *supra*, and the second circuit erroneously considered this reference as an indication that speculative premium was intended to be covered by the deduction. 176 F.2d 152, 154. The ninth circuit pointed out, however, that the reports merely indicated that amortizable bond premium on convertible bonds was covered by the section. Neither the reports nor the statute defined amortizable bond premium, and, in the ninth circuit's view, the second circuit was incorrect in disregarding other aspects of congressional history which indicated that only investment premium and not speculative premium was meant to be covered by the phrase "amortizable bond premium." 177 F.2d 131, 135.

24. *New Colonial Ice Co. v. Helvering*, 292 U.S. 435, 440 (1934): "Whether and to what extent deductions shall be allowed depends upon legislative grace; and only as there is clear provision therefor can any particular deduction be allowed. . . ." See also *Helvering v. Northwest Steel Mills*, 311 U.S. 46, 49 (1940); *Deputy v. Dupont*, 308 U.S. 488, 493 (1940); *White v. United States*, 305 U.S. 281, 292 (1938).

25. The second circuit's summary dismissal of this feature of the controversy is perhaps the most unsatisfactory aspect of its decision. 176 F.2d 152, 154. The court rested its dismissal on the authority of *Gemsco v. Walling*, 324 U.S. 244, 260 (1945). The inappropriateness of the *Walling* case to the present situation is apparent in the following passage from that source. It reveals a totally different problem of statutory interpretation:

"The argument from the legislative history undertakes, in effect, to contradict the terms of § 8(f) by negative inferences drawn from inconclusive events occurring in the

Finally, judicial overcaution would here perpetuate an admitted loophole that may very easily, as the second circuit agreed, cause this device to become the "rage of the security markets."²⁶ With these compelling circumstances to recommend it, the result reached in the ninth circuit merits the approval of the Supreme Court.²⁷

course of consideration of the various and widely differing bills which finally, by compromise and adjustment between the two Houses of Congress, emerged from the conference as the Act. The plain words and meaning of a statute cannot be overcome by a legislative history which, through strained processes of deduction from events of wholly ambiguous significance, may furnish dubious bases for inference in every direction. This is such a case."

By comparison, the legislative history of § 125 is particularly neat, revealing a single bill proceeding from Treasury proposal through committee reports without controversy, compromise, or adjustment.

A similar misuse of authority characterizes the court's denial of the Commissioner's petition for rehearing, 176 F.2d 152, 155. Not only does the summary rejection of the government's "scholarly accountant's concept" fly in the face of the specific Congressional invocation of "sound accounting practice," see H.R. REP. No. 2333, note 14 *supra*, but the court's assertion that dissatisfaction with that concept underlay the rejection of amortization in § 6 of the UNIFORM PRINCIPAL AND INCOME ACT (regulation of estate trust administration) is also unwarranted. 176 F.2d 152, 155. Actually, amortization of premium was rejected in the Uniform Act primarily, if not entirely, for reasons of mere administrative convenience. See 39 HANDBK. NAT. CONF. COMM'RS ON UNIFORM STATE LAWS 290-92 (1929); UNIFORM PRINCIPAL AND INCOME ACT: REASONS FOR ITS ADOPTION 4, 6-7 (1933); 34 MICH. L. REV. 448, 451 n.12 (1931). The court's view that the assumption supporting amortization is a fiction, 176 F.2d 152, 155 n.1, suggests that its rejection of the Commissioner's contention is in effect a rejection of the judgment of Congress that amortization is a sound policy and should be incorporated in the tax law.

26. The second circuit frankly acknowledged the loophole:

"We shall avoid the [Commissioner's] charge of naïveté by expressing no dissent; whatever respondent may actually have done with these bonds after 1944, it certainly would be perfectly normal to expect a holder to sell them in due course after the proper interval to take advantage of the lower rates for capital gains. And the obvious advantage, taxwise, of transactions of this form might make such convertible bonds all the rage of security markets. Nevertheless the difficulties of a judicial attempt to remodel legislation to deal with such a situation at once fairly and not overdestructively remain obvious." 176 F.2d 152, 153-4.

In striking contrast is the more practical philosophy expressed by Judge McCord, dissenting, in *Farkas v. Commissioner*, 170 F.2d 201, 205-6 (5th Cir. 1948):

"I am well aware that it is not the function of courts, by judicial fiat, to attempt enactment of remedial tax legislation. I am further aware that every taxpayer has a constitutional privilege to minimize his tax liability through lawful tax avoidance. Nevertheless, I have never favored decisions which encourage loopholes in our tax laws and enable taxpayers . . . to transfer excess income and thereby retreat to lower tax brackets during prosperous and high tax years, and later to retrieve that same source of income in lean years, when income taxes are usually much lower." While the issue in the *Farkas* case was substantially different (grantor's liability for tax on the income of a ten-year trust), the type of problem facing the court was essentially the same.

27. *Commissioner v. Korell* was argued before the Supreme Court, Feb. 7, 1950. 18 U.S.L. WEEK 3232. The taxpayer's petition for certiorari in *Shoong v. Commissioner*, filed Nov. 12, 1949, is pending. 18 *id.* 3158.