bona fide purchaser. Changes that are an aid to clarity are found in the combination of the provisions of the former Section 67(c) and (f) into the new Section 67(a), and in the elimination of a reference to state law from the fraudulent transfer section. Procedurally, the most important change occurs in Section 67(a), giving the court summary jurisdiction where liens are acquired through judicial proceedings. Many problems arose under the provisions of the former Section 67. Because of this fact, and because the section is plainly of considerable importance in the trustee's collection of assets, the revision has been carried out with care and particularity, and should represent one of the most important advances in the new bankruptcy law. But it is quite likely that even under the new Section 67, problems that are now unanticipated will arise.

C. E. H.

NOTES

Discrimination Between Resident and Non-Resident Creditors in the Distribution of the Assets of an Insolvent Debtor

Forty years ago the United States Supreme Court declared invalid a Tennessee statute according resident creditors priority over non-resident creditors in the distribution of an insolvent corporation's assets.[1] The Court stated that the privileges and immunities clause of the United States Constitution forbade such discrimination.[2] Strangely enough the impli-

1. Blake v. McClung, 172 U. S. 239 (1898). But the rule of the *Blake* case does not apply to the distribution of a fund deposited in a state by a foreign corporation as a condition of doing business there under a provision that such a fund is exclusively for the benefit of local creditors. *Id.* at 257. Accord: People v. Granite State Provident Ass'n, 161 N. Y. 492, 55 N. E. 1053 (1900); Lewis v. American Savings & Loan Ass'n, 98 Wis. 203, 73 N. W. 793 (1898). But see Irwin v. Granite State Provident Ass'n, 56 N. J. Eq. 244, 38 Atl. 680 (1897). Apparently the reason offered for this exception is that the corporation must be considered as having assented to the constitutionality of a trust of this character. Lewis v. American Savings & Loan Ass'n, *supra*. Such a distinction, however, seems tenuous and the reason offered inept. The only question should be whether *non-resident creditors* have waived such protection; the corporation cannot waive it for them.

Apparently there is no constitutional objection to deferring a foreign creditor of a foreign corporation if such a creditor is also a foreign corporation, since a foreign corporation is not a citizen within the protection of the privileges and immunities clause. Blake v. McClung, *supra*, at 259.

2. The court expressly held that the word "resident" as used in the statute meant "citizen". There are, however, a number of later cases in which the Supreme Court of the United States has permitted a distinction between residents and non-residents for some purposes. La Tourette v. McMaster, 248 U. S. 465 (1919); Maxwell v. Bugbee, 250 U. S. 525 (1919); Douglas v. New York, New Haven and Hartford Ry., 279 U. S. 377 (1929). But see Travis v. Yale & Towne Mfg. Co., 252 U. S. 60 (1920). In (1934) 19 IOWA L. REV. 620, 621, the case writer suggests that the Supreme Court has completely reversed itself and has returned to Justice Brewer's dissenting opinion in Blake v. McClung, 172 U. S. 239, 262 (1898), which was to the effect that "resident" and "citizen" are not synonymous for purposes of the privileges and immunities clause. Such a conclusion, however, is not warranted by a close examination of the later cases. It is hardly likely that the Supreme Court would now uphold a preference to a resident creditor and a discrimination against a non-resident creditor simply because the latter *may be* a citizen of the same state as the resident creditor. If that were so, the same statute declared invalid by the Court in the *Blake* case would now be valid merely because it used the words residents instead of citizens, although its purpose was clearly to prefer local citizens and discriminate against citizens of other states. See Note (1923) 8 MINN. L. REV. 47; *cf.* (1930) 24 ILL. L. REV. 826.

cations of this decision are as yet unsettled and there is no firm line on which its imprints on the law can be traced. In what respect does this decision affect, if at all, the rights of a foreign assignee for the benefit of creditors as against the rights of local creditors? Is a local policy which prefers resident creditors to foreign assignees but denies such a preference to non-resident creditors an unconstitutional discrimination within this rule? Is a local policy which prefers resident creditors to foreign receivers or statutory liquidators but denies such a preference to non-resident creditors likewise an unconstitutional discrimination within this rule? Although an independent analysis would seem to compel definite, logical answers to these problems, an examination of the decisions reveals conflicts of authorities and gross indecision. The general scope of this article, then, will be an attempt to trace the effects of the rule of *Blake v. McClung* in the situations outlined above.

The first and most elementary problem arising from the *Blake* case is whether the decision outlaws a *local policy* which gives resident creditors priority in the distribution of assets of an insolvent as opposed to creditors who are citizens of other states.[3] It would seem that if a state cannot do this by statute, as the *Blake* case decided, it cannot do it by a so-called local policy, and that therefore such a policy is unconstitutional. Although the federal courts admitted this was so by way of a loosely worded opinion in *Belfast Savings Bank v. Stowe*,[4] there was no vigorous holding on the point by any court until 1916.[5] It is a very unusual situation for resident creditors to be competing against non-resident creditors and this may explain the paucity of cases handling this situation. In the ordinary case, before the race by the diligent commences, the debtor's interest will have passed to a representative of the creditors. Therefore, in most of the cases presenting the problem of discrimination, the issue arises out of an attachment made by a resident or non-resident creditor and an objection made by a foreign assignee or receiver.

In the field of foreign assignments for the benefit of creditors, the application of the rule under discussion has caused not a little difficulty.[6] To begin with, the subject of conflict of laws relating to the extraterritorial effect of these assignments is so closely connected with the problem of unconstitutional discrimination that there has resulted a mass of law which is most confusing because of the inadequate and unsatisfactory treatment of the constitutional and conflicts problems inseparably involved. Leaving aside, for the time being, the conflict of laws question, the constitutional problem will first be considered. There are two possible situations in which may be applied the rule of *Blake v. McClung* in considering the constitutionality of a local policy which prefers resident creditors to a foreign voluntary assignee. The first may be designated, for want of a better term, a direct application of the rule.[7] Thus, it may be argued

3. See Note (1929) 77 U. OF PA. L. REV. 1001, 1007, which concludes that such discrimination in the distribution of decedents' estates should be held unconstitutional.

4. 92 Fed. 100, 104 (C. C. A. 1st, 1899), *rev'g*, 92 Fed. 90 (D. Me. 1897).

5. Brunner v. York Bridge Co., 78 W. Va. 702, 90 S. E. 233 (1916).

6. See generally Notes (1894) 23 L. R. A. 33; (1904) 65 L. R. A. 353; (1932) 41 YALE L. J. 593. See also WHARTON, CONFLICT OF LAWS (3d ed. 1905) §353 *et seq.*

7. A "direct" application of the rule would be to classify the foreign representative (assignee or receiver) as a person in the same position as foreign creditors, and thus argue that any preference over the foreign representative is tantamount to a preference over the foreign creditor and is thus a *direct* discrimination between resident and non-resident creditors which is forbidden by the rule of *Blake v. McClung*.

If, however, a state chooses to prefer resident creditors to foreign representatives but will not extend these preferences to non-resident creditors as against foreign representa-

that the foreign voluntary assignee is the representative of creditors, and a preference of the local creditors is an unlawful discrimination within the rule. This position might be even stronger in the case of a statutory assignee [8] who has the power, *as representative of creditors,*[9] to sue to set aside fraudulent conveyances. Such an argument has, however, rarely been employed. It was considered in the case of *Belfast Savings Bank v. Stowe,* a federal circuit court of appeals decision handed down the year following the *Blake* case. In the *Belfast* case a voluntary assignment for the benefit of creditors was made in Massachusetts. Some property was situated in Maine where there was a local policy of preferring domestic creditors over foreign voluntary assignees. The court said that the *"sharp question* of constitutionality" [10] raised in the *Blake* case was not involved in this case because it was not shown that the creditors who assented to the assignment [11] (and thus inferentially, who were represented by the assignee) were citizens of *any* particular state. Perhaps a more exact answer to the application of the rule in this manner is that the assignee is really *not* the representative of the creditors for all purposes, and therefore, this is not a direct preference of domestic over foreign creditors, since there is nothing to prevent the creditors themselves from coming into the forum state and demanding to share on a parity with the domestic creditors under the *Blake* rule. Such reasoning, however, is not altogether satisfactory and will be considered subsequently with greater detail in connection with foreign receivers.

The second method of attacking the constitutionality of a local preference policy may be termed an indirect application of the *Blake* rule.[12] Thus in the *Belfast* case, the court apparently held as violative of the privileges and immunities clause,[13] a policy which preferred local creditors over foreign voluntary assignees, but which would deny such a preference to a creditor resident in a third state who seeks to attach in the forum state. Although there was a split on this point in the earlier foreign assignment cases, no mention was made of the constitutional argument.[14] Logically, it would seem that this conclusion is irrefutable, since such a local policy is undoubtedly discriminatory within the rule. The difficulty that the courts experienced with this was caused by their inability to consider it apart from the conflict of laws rules on foreign assignments which had developed in a discordant manner.[15] In order to understand such a criticism, a brief examination of the principles underlying the conflict of laws problem herein involved will be necessary.

Generally, a voluntary common law assignment of personal property that was valid by the law of the state where made was valid everywhere,

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tives, there would likewise seem to be an unconstitutional discrimination between resident and non-resident creditors. It is this latter type of discrimination which this paper refers to as an "indirect" application of the *Blake* rule.

8. Although weaker perhaps in the conflict of laws sense. See *infra* note 36.

9. Moore v. Williamson, 44 N. J. Eq. 496, 15 Atl. 587 (1888).

10. 92 Fed. 100, 103 (C. C. A. 1st, 1899) (italics supplied).

11. Massachusetts required the consent of *all* creditors in a common law assignment. May v. Wannemacher, 111 Mass. 202, 207 (1872).

12. See *supra* note 7.

13. The confusing language used in this opinion apparently caused Wharton trouble when he commented six years later on the effect of the holding. WHARTON, CONFLICT OF LAWS (3d ed. 1905) § 353 (b).

14. See, for example, the collection of cases in Note (1894) 23 L. R. A. 33; *cf.* Note (1929) 77 U. OF PA. L. REV. 1001, 1004.

15. See Sunderland, *Foreign Voluntary Assignments for the Benefit of Creditors* (1903) 2 MICH. L. REV. 112.

and was upheld as against a local attaching creditor.[16] The theory was that a voluntary transfer if valid where made ought generally to be valid everywhere, being the exercise of the personal right of the owner to dispose voluntarily of his property.[17] Also the dogma developed that a foreign assignment under a statute providing for discharge or involuntary proceedings, was a transfer *in invitum* and had no legal operation out of that state.[18] Hence the local attaching creditors prevailed over a foreign statutory assignee.[19]

The rule of the extraterritorial effect of voluntary common law assignments was qualified, however, by the doctrine of *Green v. Van Buskirk* [20] declaring that the assignment had no effect unless also valid by the *lex situs,* even though it was valid by the state in which it was made. This was based on the state's sovereign power to regulate the disposition of property within its borders. With these principles in mind, it is not hard to see the difficulty in applying the constitutional objections to a state policy of preferring local creditors to foreign assignees, but refusing such privileges to a non-resident creditor. So long as the assignment did not conflict with the transfer laws of the *lex situs,* it would seem that the same privileges of residents must be granted to non-residents. But in cases where the transfer laws are not fully complied with, apparently the courts were disturbed as to whether the non-resident creditors could object as well as the resident creditors.[21] Furthermore, in the foreign assignments

16. Livermore v. Jenckes, 62 U. S. 126 (1858); Roberts v. Norcross, 69 N. H. 533, 45 Atl. 560 (1898); BURRILL, ASSIGNMENTS (6th ed. 1894) § 275. *Contra:* Heyer v. Alexander, 108 Ill. 385 (1884).

17. See the elaborate discussion in Justice Allen's concurring opinion in Willits v. Waite, 25 N. Y. 577, 583 (1862). BURRILL, *op. cit. supra* note 16, § 276.

18. Harrison v. Sterry, 5 Cranch 289 (U. S. 1809); BURRILL, *op. cit. supra* note 16, § 276.

19. Taylor v. Columbian Insurance Co., 14 Allen 354 (Mass. 1867); Matter of Accounting of Waite, 99 N. Y. 433, 2 N. E. 440 (1885). But see Taylor v. Life Ass'n, 13 Fed. 493 (W. D. Tenn. 1882) (holding a foreign assignee in insolvency prevails over subsequently attaching resident creditors); *cf.* Maynard v. Granite State Provident Ass'n, 92 Fed. 435 (C. C. A. 6th, 1899). Note that Chancellor Kent in Holmes v. Remsen, 4 Johns. Ch. 460 (N. Y. 1820) first wrote an opinion holding that foreign assignees in bankruptcy took title to all the property of the bankrupt wherever situated with the same force and effect as if the bankrupt had made voluntary assignment of all of his property, and that such a title was good even against a subsequent attaching creditor. But he later admitted that the weight of American jurisprudence was the other way. 2 KENT, COMM. (14th ed. 1896) 406, 407. There is still argument being made to give this class of assignments the same effect as voluntary assignments. See Laughlin. *The Extraterritorial Powers of Receivers* (1932) 45 HARV. L. REV. 429, 462. See dictum in Martyne v. American Fire Insurance Co., 216 N. Y. 183, 194, 110 N. E. 502, 505, 506 (1915) to the effect that the rule preferring attaching creditors over assignees under insolvent laws or receivers is so well established that it should be changed only by statute.

20. 5 Wall. 307 (U. S. 1866); 7 Wall. 139 (U. S. 1868).

21. Franzen v. Hutchinson, 94 Iowa 95, 62 N. W. 698 (1895). Some states preferred resident creditors to a voluntary common law assignee even though the foreign assignment was in compliance with local law, on the grounds that it would be contrary to the "public policy" of the forum to permit all the funds of a non-resident assignor to be withdrawn from the state before his creditors residing in the state had been paid. These states, however, allowed the foreign assignee to recover as against a non-resident creditor. Heyer v. Alexander, 108 Ill. 385 (1884); Woodward v. Brooks, 128 Ill. 222, 20 N. E. 685 (1889); Happy v. Prickett, 24 Wash. 290, 64 Pac. 528 (1901). Clearly such cases express a local policy that is unconstitutional. Note that the RESTATEMENT, CONFLICT OF LAWS (1934) § 263, says (1) that a voluntary assignment is valid as to personal property wherever situated unless (2) it conflicts with local policy or local creditors. Such a statement, without expressly indicating that the same preferences must be accorded non-resident creditors, would seem to violate the equal privileges and immunities clause.

under insolvency laws, the dogma that the assignment operated only on property within the state likewise raised the discrimination question. By the overwhelming weight of authority the courts preferred their local creditors to an involuntary assignee.[22] Did the privileges and immunities clause require the same treatment to be accorded to a non-resident creditor? Although the cases were in conflict, it is obvious that the *Blake* rule should apply.[23] A further problem is then raised by these results. Since a state *must* accord the resident and non-resident creditors the same rights against the foreign assignees whether they are voluntary or insolvent assignees, may a state declare that its policy is to permit subsequent attachments by resident *or* non-resident creditors to prevail over prior foreign voluntary assignments? It would seem that there is no constitutional objection to such a procedure, although, from the standpoint of the recognized advisability of a unified administration of insolvents' assets, such a policy would be grossly undesirable. Even today with the law fairly well settled as it is with regard to the effect of foreign assignments under insolvency laws, it is argued that they should be treated in the same manner as voluntary assignments since the interest of unified administration is paramount to the securing of advantage to local claimants.[24]

The discussion so far has been limited to common law voluntary assignees, and those assignees under a statute providing for discharge or involuntary proceedings. Suppose, however, that the assignment is made pursuant to a statute which is merely regulatory and purports to codify the common law.[25] Or suppose that the bankruptcy features in an assignment statute have been held to be superseded by the Bankruptcy Act, although the rest of the assignment statute is valid.[26] The assignee under such a statute is a statutory assignee. Since he derives his title from the statute, the cases have not analyzed the nature or effect of the statute involved, and have considered him in the same class as an assignee under an insolvency statute.[27] Obviously such a classification is unfair. It can hardly be contended that a statute, regulatory in character and nothing more than a codification of the common law, should operate to cut down the rights that the assignee had at common law. The essential nature of his assignment, under such a statute, is still *voluntary*.

The law relating to the extraterritorial power of receivers as opposed to local attaching creditors is replete with dogmas which are generally

22. WHARTON, CONFLICT OF LAWS (3d ed. 1905) § 390½.

23. Reynolds v. Adden, 136 U. S. 348 (1890) (refusing to allow such discrimination). *Contra:* Witters v. Globe Savings Bank, 171 Mass. 425, 50 N. E. 932 (1898); Perkins, Goodwin & Co. v. Clear Spring Paper Co., 17 Phila. 168 (1885). There is a tendency to discriminate against attaching creditors who are citizens of the state in which the insolvency proceedings are instituted, or of the state in which the assignment was executed. Bagby v. Atlantic M. & O. Ry., 86 Pa. 291 (1878); Gilman v. Ketcham, 84 Wis. 60, 54 N. W. 395 (1893). But the distinction is expressly repudiated in Jenks v. Ludden, 34 Minn. 482, 27 N. W. 188 (1886); Barth v. Backus, 140 N. Y. 230, 35 N. E. 425 (1893). It would seem that Green v. Van Buskirk, 7 Wall. 119 (U. S. 1868), which allowed the attaching creditor of the same state where a chattel mortgage was executed to prevail over the mortgagee is conclusive on this problem. But see GLENN, CREDITORS RIGHTS AND REMEDIES (1915) 371-72, expressing the opinion that such a discrimination is *not* unconstitutional. See a criticism of solicitude to local creditors in GOODRICH, CONFLICT OF LAWS (2d ed. 1938) 514; but see First, *Extraterritorial Power of Receivers* (1932) 27 ILL. L. REV. 271, 277.

24. *Supra* note 21. See also Note (1932) 41 YALE L. J. 593, 600.

25. "The common law right of general assignment may be regulated by statute without losing its distinctive voluntary character." Note (1932) 41 YALE L. J. 593, 597.

26. Fidelity Trust Co. v. Union National Bank, 313 Pa. 467, 169 Atl. 209 (1933).

27. See, for example, the language used in Security Trust Co. v. Dodd, Mead & Co., 173 U. S. 624, 629 (1899).

analogous to the cases of foreign assignees. Thus, it is settled that an ordinary chancery receiver will not prevail against local attaching creditors.[28] Do those cases allowing local creditors priority over foreign receivers violate what has been designated as the direct application of the rule of the *Blake* case?[29] It has been argued that a recognition of the right in local creditors who have asserted it can hardly be said to amount to a denial of that right to non-resident creditors who have not asserted it. In other words, it is contended that there is no actual discrimination against non-residents because no right of a non-resident to attach the property was actually involved.[30] It is submitted however that while such a defense seems legally unassailable, non-resident creditors are, in all practicality, not actually on a parity with resident creditors. In the first place, the settlement of claims and liquidation process generally is left to the receiver by the creditors of the forum and third states. Furthermore, in spite of the fact that the foreign creditors allegedly have a "right" to come in and attach on a parity with the domestic creditors if they so choose, the practical elements of time and convenience may operate in a substantial manner to withhold from them this theoretical equality. It follows, of course, that this line of reasoning equally is applicable to the cases of foreign voluntary assignments heretofore considered. However, no court has ever applied the *Blake* rule in such a direct manner, and arrived at such a result.[31]

Does a local policy of preferring resident creditors over foreign receivers, but denying to non-resident creditors the same privilege indirectly violate the *Blake* rule? In 1893, a Pennsylvania court declared that the privileges and immunities clause compelled Pennsylvania, which preferred its local creditors to foreign equity receivers, to give such a preference to New York creditors who attached in Pennsylvania.[32] Thus, the constitutional argument in the field of foreign receivers developed even before the *Blake* case. Although there was considerable dissent from this view at the time of the Pennsylvania decision,[33] it would seem that the decision in *Blake v. McClung* and its subsequent application in the assignment cases would likewise have settled the question in regard to the receiver cases. Certainly, insofar as the actual preference itself is concerned, there is no discernible difference in theory between an application of it in either of these two cases. Hence, it is apparent that discriminatory preference of local creditors as against foreign receivers is an indirect violation of the rule of the *Blake* case, similar to the principles applicable in the assignment cases.

Suppose, however, the receiver is not an ordinary chancery receiver deriving his title from the court decree, but a so-called statutory receiver, or statutory liquidator who gets all his rights from a state statute which

28. Choctaw Coal & Mining Co. v. Williams Echols Dry Goods Co., 75 Ark. 365, 87 S. W. 632 (1905); Miller v. American Cooperative Ass'n, 110 Neb. 773, 195 N. W. 167 (1923); see Hurd v. Elizabeth, 41 N. J. L. 1, 3 (1879); Runk v. St. John, 29 Barb. 585, 587 (N. Y. 1859); Richardson v. South Florida Mortgage Co., 102 Fla. 313, 321, 136 So. 393, 396 (1931). See Note (1935) 98 A. L. R. 351. The dogma is that a foreign chancery receiver may sue only as a matter of comity in a state court, but he cannot sue at all in a federal court. First, *supra* note 23, at *272 et seq.*

29. See *supra* note 7.

30. See Note (1935) 98 A. L. R. 351, 381; Davis v. Amra Grotto, Inc., 169 Tenn. 564, 89 S. W. (2d) 754 (1936).

31. See Note (1935) 19 MARQ. L. REV. 190, 193.

32. John Ray Clark Co. v. Toby Valley Supply Co., 3 Pa. Dist. 518 (1894).

33. Weil v. Bank, 76 Mo. App. 34 (1898); Receiver v. First National Bank, 34 N. J. Eq. 450 (1881).

purports to vest him with title to the assets of the insolvent wherever they may be located.[34] What analogies may be drawn from the position of the foreign statutory assignee? As we have seen, the common law voluntary assignee has the most preferred position with regard to assets located outside the state of his appointment. As for the so-called assignees under insolvency statutes, the dogma asserts that his title "operates" only on property within the state of his appointment. However, as has been pointed out, in those cases where the statute is merely regulatory and adds to the common law such minor details as posting a bond, or where the scope of supersedure by the Bankruptcy Act leaves the other provisions of the assignment statute intact, it would seem that the foreign assignee should be given all the rights of a common law assignee since the essential nature of his transfer is still voluntary. The ordinary foreign receiver, acting under decree of court, and possessing no deed on which to predicate his title cannot compare himself to the voluntary assignee. But it would seem that the receiver who has title vested in him by statute is somewhat analogous to the statutory assignee under a regulatory type of statute, except that here again the receiver does not predicate his title on a deed. Justice Cardozo has said,[35] in making these analogies, that a statutory liquidator is more like a voluntary assignee than one deriving title under a decree in insolvency proceedings,[36] and even stronger than either in that for many purposes the corporation under which he claims has passed out of existence. Apparently courts are not clear whether the assignee under an insolvency statute derives his title from decree of court or from the statute. Actually the statute usually gives the court the right to transfer title by its decree. Ultimately then the assignee really derives title from the statute. If the latter, it is difficult to understand why full faith and credit requires a court to recognize the foreign statutory receiver,[37] although the question is merely regarded as one of comity with relation to the assignee under an insolvency statute.

In the extended litigation of *Clark v. Williard*[38] it was hoped that some of these troublesome questions would be set at rest. Unfortunately, an examination of the language used in that case does not serve to clarify the problem. Under a state statute of Iowa which purported to vest full title to all the assets of an insolvent insurance corporation in a liquidator on the dissolution of the corporation, the liquidator claimed a fund located

34. See, for example, N. C. CODE ANN. (Michie, 1935) § 1210 (ordinary statutory receiver); NEB. COMP. STAT. (1929) § 44-204 (insurance liquidator). It is not always easy to know the exact situation which will give rise to a so-called statutory receiver. See Note (1935) 19 MARQ. L. REV. 190, 195.

35. Clark v. Williard, 292 U. S. 112, 122 (1934).

36. Security Trust Co. v. Dodd, Mead & Co., 173 U. S. 624 (1899), was cited for this proposition. Notice that he uses the words "under a decree" which connotes that title passed by virtue of a court decree. But actually title was conferred in that case by the state insolvency statute under which the assignee was appointed. See HUSTON, ENFORCEMENT OF DECREES IN EQUITY (1915) 17, for a collection and analysis of statutes which give courts administering equity the right to transfer title by the decree that they render.

37. Clark v. Williard, 292 U. S. 112 (1934). Apparently the full faith and credit clause has never been used in trying to get state courts to recognize the title of the foreign statutory assignee. If the statute is an insolvency statute, the courts contend that it operates only on the property within the state. But it would seem that if the local transfer laws of the forum are satisfied, under the doctrine of Green v. Van Buskirk, 5 Wall. 307 (U. S. 1866), 7 Wall. 139 (U. S. 1868), full faith and credit should require the recognition of the statutory assignees' title in the same manner in which it is required in the case of a statutory liquidator.

38. 292 U. S. 112 (1934) (first case); 294 U. S. 211 (1935) (second case).

in Montana, in contest with a Montana creditor of the dissolved corporation. Previous to this case, some states allowed the liquidator to prevail;[39] others preferred the local creditor.[40] In the first *Clark v. Williard* case,[41] the United States Supreme Court reversed the Montana Supreme Court,[42] which had held that the Iowa receiver was only a chancery receiver deriving his power from a court decree and could not sue in Montana. The Court said that he derived his title from the Iowa statute, and a refusal to recognize such title and thus a refusal to let him sue in the Montana courts was a violation of the full faith and credit clause of the Constitution. Thereupon, the Court sent the case back to Montana to ascertain what the local policy of Montana was in reference to preferring local creditors. When Montana announced that their policy was to prefer creditors,[43] the United States Supreme Court said there was nothing unconstitutional about such preference of local creditors, and that each state had a right to determine its own policy.[44]

The difficulty of the case, and its relation to *Blake v. McClung* lies in the choice of Cardozo's language. Since the contest involves a receiver against a creditor, it is conceded that the *Blake* rule is not directly involved. Furthermore, *if Clark v. Williard* holds that because of the doctrine of *Green v. Van Buskirk,* each state has a right to regulate the transfer of property within its boundaries by its own transfer laws and not recognize foreign transfers which are at variance with its own transfer laws, no fault can be found with the case, although the hearing is not clearly predicated on this position. A possible interpretation of the language would indicate that a state may lawfully prefer its local creditors over foreign receivers, even if there be no difference in transfer laws and indeed over foreign voluntary assignees as well.[45] Conspicuous by its complete

39. Relfe v. Rundle, 103 U. S. 222 (1880); Kinsler v. Casualty Co., 103 Neb. 382, 172 N. W. 33 (1919); Martyne v. American Insurance Co., 216 N. Y. 183, 110 N. E. 502 (1915); Bockover v. Life Ass'n, 77 Va. 85 (1883); *cf.* Forgan v. Bainbridge, 34 Ariz. 408, 274 Pac. 155 (1928); Union Securities Co. v. Adams, 33 Wyo. 45, 236 Pac. 513 (1925).

40. Zacher v. Fidelity Trust Co., 106 Fed. 595 (C. C. A. 6th, 1901); Ward v. Pacific Mutual Life Ins. Co., 135 Cal. 235, 67 Pac. 124 (1901); Schloss v. Surety Co., 149 Iowa 382, 128 N. W. 384 (1910).

41. *Supra* note 33.

42. Mieyr v. Federal Surety Co., 94 Mont. 508, 23 P. (2d) 959 (1933).

43. Mieyr v. Federal Surety Co., 97 Mont. 503, 34 P. (2d) 982 (1934).

44. Clark v. Williard, 294 U. S. 211 (1935). See generally Legis. (1935) 48 HARV. L. REV. 835; (1935) 35 COL. L. REV. 604, 23 GEO. L. REV. 545. RESTATEMENT, CONFLICT OF LAWS (1934) § 161, gives the statutory successor of a dissolved corporation complete title to all personal property located in other states, but reserves its opinion as to land in other states. In commenting on the rights of foreign voluntary assignees for the benefit of creditors, § 263 (2) says that local creditors would prevail over the foreign assignee. *Query,* if the RESTATEMENT by omitting any mention of local creditors or local policy in § 161 means that the statutory successor should prevail as matter of right over subsequent attaching creditors.

45. "If title had been conveyed to an assignee for the benefit of creditors by a *common law assignment* or by insolvency proceedings, claimants in Montana might pursue their suits and remedies in derogation of the assignment when the law or policy of the locality ordained that this result should follow. So much is settled by unimpeachable authority." 294 U. S. 211, 214 (1935) (italics supplied). Seven cases are cited for this proposition but only two are applicable to the case of a common law assignment, and both of these are dicta. In the first case so cited, Security Trust Co. v. Dodd, Mead & Co., 173 U. S. 624, 628 (1899), the court said by way of dictum: ". . . voluntary assignments will be respected except so far as they come in conflict with the rights of local creditors, or with the laws or public policy of the State in which the assignment is sought to be enforced." But even *this* dictum is not well supported by the following cases which it cites to sustain its position. In Black v. Zacharie & Co., 3 How. 483 (U. S. 1845), the court held that an assignment was good

absence from the opinion is any reference to *Blake v. McClung.*[46] Thus, from a perusal of the United States Supreme Court opinion *alone,* it might seem that the discrimination which we have seen is outlawed by the privileges and immunities clause, is no longer so outlawed. That this is not so, however, is apparent only after an examination of the second opinion of the Montana Supreme Court.[47] In *that* case the discrimination argument of the *Blake* case occupied the major portion of the court's opinion. The majority of the court concluded that the policy of the state was to prefer *all* creditors, whether resident or non-resident, and thus brought itself within the rule. Justice Angstman dissented on the grounds that that court was only giving lip service to such an equitable rule in order to avoid any question of constitutionality, and if, at some future date, a non-resident creditor sought priority over a foreign liquidator, the court would back down and not grant it.[48] This then was the local policy which the Montana court announced. But Justice Cardozo makes no mention that the same privileges would extend to non-resident creditors in Montana, or *must* extend to non-residents under the *Blake* case, but merely says that each state constitutionally can decide for itself whether or not its policy is to prefer local creditors. Hence, it is difficult definitely to state the position of the United States Supreme Court; the greater probability is that it accepted the fact that Montana extended such preference to *all* creditors, and therefore indulged in no further discussion on this point.[49]

Thus, it seems clear that any state policy which prefers its own creditors over foreign assignees or foreign receivers, but denies such preference to foreign creditors is an unconstitutional discrimination. It is doubtful, however, whether the courts will ever contend that the foreign assignee or foreign receiver is such a representative of creditors so as to bring the rule of *Blake v. McClung* into play directly. Because of this, it would seem that a state, if it so desires, may initiate a policy of preferring all claimants, even as against foreign voluntary assignees without any constitutional embarrassment. Such a policy, however, would be most undesirable since it would strongly deter a unified administration of the insolvent assets. Indeed, because of this latter consideration, it appears that

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merely so long as it was not bad by the transfer laws of the state of situs. And in Livermore v. Jenckes, 21 How. 126 (U. S. 1858), even this exception was apparently disregarded. But the principle was once more asserted in Green v. Van Buskirk, 5 Wall. 307 (U. S. 1866), 7 Wall. 139 (U. S. 1868). Then in Hervey v. Rhode Island Locomotive Works, 93 U. S. 664, 672 (1876), the court, for the first time, used the words "local policy" in connection with this problem. This word usage was repeated in Cole v. Cunningham, 133 U. S. 107, 134 (1890) by way of dictum. (This was the second and only other case cited by Justice Cardozo which was applicable to his statement concerning common law assignments.) Thus it is difficult to state with any amount of certainty the position of the United States Supreme Court on this point. Apparently, however, the present attitude of the Court, by way of dictum, plus the instant "interpretation" of the second *Clark v. Williard* case, is that if a state has a policy of preferring *all* claimants (in order to avoid the rule of the *Blake* case), it may express such a policy even in preference to voluntary common law assignees.

46. See comment in STURGES, CASES ON DEBTORS' ESTATES (2d ed. 1937) 162, following the case of Clark v. Williard, 294 U. S. 211 (1935).

47. Mieyr v. Federal Surety Co., 97 Mont. 503, 34 P. (2d) 982 (1934).

48. *Id.* at 521, 34 P. (2d) 982, 991 (1934).

49. "The inconsistency in enforcing recognition of the right to sue, a right dependent on the possession of title, while permitting a state to deny all practical effect to the title itself seemed to demand an application of the full faith and credit clause to reach a result contrary to the instant case." (1935) 35 COL. L. REV. 604, 606, commenting on Clark v. Williard, 294 U. S. 211 (1935). *Cf.* "A title thus subject to defeasance would seem little better than no title at all, but it may be of some importance in several respects." (1935) 29 ILL. L. REV. 934, 936.

there is much sound thought behind the argument that assignments under insolvency proceedings should be accorded the same extraterritorial effect as voluntary assignments. Certainly, if the assignee under the insolvency statute derives his title from the statute, full faith and credit should require the recognition of such title.

Finally, the cases reveal no clear-cut line between the legitimate protection a state may accord its local creditors, and what seems to be a provincial insistence on the priority of local creditors based on the time-worn theory of the sovereign's control of property within its physical borders, and its duty to its own citizens. It would appear that the "sovereign spirit" of the state sufficiently should be appeased if it is allowed full control over the law concerning the actual transfer of such property.[50] From this point on there seems to be no moving argument why the foreign transaction should not be accorded its full strength; thus, the state of the situs of the property may retain the right to fix the details which will prevent discrimination *against* its own citizens, such as requiring a foreign assignee to post a bond for the payment of local claimants before removing any assets from the state.

R. J. B.

Taxing the Maintenance Trust

The trust has long been recognized as a simple method of evading inclusion in the higher brackets of the income tax, and yet retaining the larger incidents of ownership. Its only difficulty lay in Congressional recognition of this avenue of escape, and its provision for including in the settlor's taxable income both the income from trusts revocable by the settlor alone or in conjunction with one having no substantial adverse interest, and the income of trusts which may be accumulated for and distributed to the settlor.[1] After allowing the handwriting on the wall to appear in *Corliss v. Bowers*[2] and *Burnett v. Wells*,[3] the Supreme Court co-operated in plugging the largest remaining loophole by its decision in *Douglas v. Willcuts*.[4]

In the latter case, the taxpayer, about to get a divorce, created an irrevocable trust for the benefit of his wife. In lieu of alimony, this agreement was incorporated in the subsequent divorce decree, with the further provision that it was to provide a certain amount, the husband making up any deficiencies. The Court held that the income of the trust should be included in the income of the husband since it came within the definition of "gross income" in the Revenue Act.[5] The provisions in regard to the taxation of trusts did not apply, when, as in this case, the trust is created by the taxpayer "as the channel for the application of the income to the discharge of his obligation".[6] Here the trust did not have the effect of releasing the husband from the obligation to support the wife, but was

50. See Note (1932) 41 YALE L. J. 593, 601.

1. These provisions first appeared in § 219 (g) (h) of the Revenue Act of 1924, 43 STAT. 275 (1924). In their present form they are contained in §§ 166, 167, 52 STAT. 519, 26 U. S. C. A. §§ 166, 167 (Supp. 1938).

2. 281 U. S. 376 (1931). ". . . taxation is not so much concerned with the refinements of title as it is with the actual command over the property."

3. 289 U. S. 670 (1933).

4. 296 U. S. 1 (1935).

5. § 22. 45 STAT. 797 (1928). Changes since made do not affect this discussion. For present form, see 52 STAT. 457, 26 U. S. C. A. § 22 (Supp. 1938).

6. 296 U. S. 1, 9.

merely a way of discharging the obligation. On its precise facts, the *Douglas* case did not go very far. However, it is the purpose of the present discussion to examine the subsequent decisions which, because of the broad language employed, have extended its principle to a considerable degree.[7]

Soon after this decision, the Court decided without opinion three similar cases, holding that the settlor was taxable on trusts the income of which was to be applied to the maintenance of his children,[8] or to the payment of his debts.[9] Although it can not be denied that these cases represent a logical extension of the doctrine that a trust set up to discharge a legal obligation of the settlor is taxable to him, it is unfortunate that the opportunity to elucidate the principles of the *Douglas* case was wasted with memorandum opinions.

Following the *Douglas* case, it again was recognized that income from a trust set up by the husband in contemplation of the divorce was not taxable to the wife.[10] Where an attempt is made to make it taxable to the husband, each case presents the separate problem of whether there is a legal obligation which the trust discharges. For such to arise, the wife must be entitled to support. Thus, where the wife was the guilty party, and therefore under the laws of the domicile forfeited all marital rights, the Board of Tax Appeals held that the trust was not created to discharge a legal obligation and therefore was not taxable to the husband.[11] Two similar cases arose under the laws of Pennsylvania, where, since 1925, no obligation exists on the part of the husband to support his former wife after an absolute divorce. In the first of these, *Henry Oliver Rea,*[12] the Board decided that the income was not taxable to the husband as there was no legal obligation discharged by the trust. In the second, *Robert Glendenning,*[13] the opposite result was reached from the fact that there had been several previous agreements which the final one purported to codify and supersede, and that a support order, made while the divorce proceedings were pending,[14] was to be cancelled. The *Rea* case was distinguished on the grounds that there the trust agreement did not show on its face that it was created to provide a settlement of the rights of the parties arising from the marital relationship; nor did it refer to any contemplated separation or contain a waiver of the wife's interest in the husband's estate. Admitting this, the fact remains that the emphasis in the *Rea* case was

7. It is difficult to tell from the language of the opinion whether the court is really ignoring the presence of the trust, or whether it is recognizing it and considering the settlor as the real beneficiary—the income in theory being given to him and then paid over to his wife in accordance with the decree. This would become important in the proper allocation of taxes on gains or losses on the sale of the corpus. See 4 PAUL AND MERTENS, LAW OF FEDERAL INCOME TAXATION (Supp. 1938) § 34.168, n. 62e.

8. Helvering v. Schweitzer, 296 U. S. 551 (1935), *rev'g without opinion,* Schweitzer v. Commissioner, 75 F. (2d) 702 (C. C. A. 7th, 1935); Helvering v. Stokes, 296 U. S. 551 (1935), *rev'g without opinion,* Commissioner v. Stokes, 79 F. (2d) 256 (C. C. A. 3d, 1935).

9. Helvering v. Blumenthal, 296 U. S. 552 (1935), *rev'g without opinion,* Blumenthal v. Commissioner, 76 F. (2d) 507 (C. C. A. 2d, 1935).

10. Maud H. Bush, 33 B. T. A. 628 (1935). See Gould v. Gould, 245 U. S. 151 (1917). If the husband dies, his obligation to support the wife ceases, therefore the income should be taxed to the wife rather than to the husband's estate. *Cf.* Thomas v. Commissioner, 384 C. C. H. Fed. Tax Serv. ¶ 9606 (C. C. A. 2d, 1938).

11. Edward T. Hall, 36 B. T. A. 398 (1937). The same result was reached in Llewellyn Barry, 36 B. T. A. 1328 (Memo. Docket No. 79340, Aug. 12, 1937).

12. 35 B. T. A. 1132 (1937).

13. 36 B. T. A. 486 (1937).

14. Little emphasis was placed on the agreement that the support order should be cancelled, apparently for the reason that it would not continue beyond the final divorce decree.

placed on the absence of permanent alimony in Pennsylvania. Taken together, the two cases indicate, in the absence of a court decree, that only when the trust agreement discloses that the income involved is paid in lieu of alimony or the wife's interest in the husband's property, is it taxable to the husband. Thus it would seem that in jurisdictions which do not allow alimony, the husband could avoid taxation if the instrument is carefully drafted. The *Glendenning* case was affirmed in a short opinion in the Third Circuit.[15]

The relative importance of the decree in establishing the obligation is still a matter of contention. In the *Douglas* case, where the trust was to provide a specific income to the wife, any excess being paid to the husband, the divorce court incorporated the agreement in its decree. There is language in the opinion indicating that considerable reliance was placed on that fact. But in *Commissioner v. Hyde,*[16] where a trust was set up after[17] the divorce in accordance with an agreement made beforehand and the decree contained no provision for alimony or other means of support, the court held that the only reason for the absence of alimony was the promise to create the trust, and therefore a legal obligation was being discharged.[18] It may be contended that as the common law obligation of the husband to support the wife ceases with divorce, and is continued only by the statutory substitute of alimony, no fixed obligation exists until set by the decree. But where there has been a mutual agreement that all rights be waived in favor of a trust, an obligation arises, similar to that imposed by a decree, which is discharged by the income from the trust. A more difficult situation would be where no obligation has been fixed by previous agreements of the parties, and no decree for alimony made. No precise holding on this could be found, but it would seem from the emphasis placed on the waiver of the wife's rights due to the contemplated trust that income from such a trust would not be taxable to the husband.[19]

A further problem in the absence of a decree for a definite sum is the amount of income which can be regarded as in lieu of alimony. It would be difficult to separate the amount representing the settlor's duty from that representing his generosity. But the Board has indicated its willingness to attempt, on presentation of sufficient evidence, to permit segregation whereby less than the total income may be allocated to alimony.[20] At any rate, it would seem that where a decree for a definite sum has been made, income in excess of this amount derived from a trust set up to pay it would not be taxable to the settlor.

The Circuit Court of Appeals for the Sixth Circuit in *Commissioner v. Tuttle,*[21] arising under Michigan law, distinguished the *Douglas* case

15. 97 F. (2d) 51 (C. C. A. 3d, 1938).
16. 82 F. (2d) 174 (C. C. A. 2d, 1936).
17. In John Ernest Goldring, 36 B. T. A. 779 (1937), the same result was reached when the trust was set up before the decree.
18. To the same effect is Albert C. Whitaker, 33 B. T. A. 865 (1935), *appeal dismissed,* 87 F. (2d) 1022 (C. C. A. 4th, 1937).
19. The result in such a case might well depend on how far the court might go to find a legal obligation. If they refuse to look beyond the trust instrument, the *Rea* case, discussed *supra,* might control. However, if the court is willing to go back of the instrument, a logical result would be to put the burden on the government to prove that the trust was established shortly before the divorce and that no further settlement was made. It should then be the taxpayer's duty to prove that the trust was not in fact set up instead of alimony.
20. Thorne Donnelley, 37 B. T. A., Jan. 14, 1938. But *cf.* Frank T. Hogan, 35 B. T. A. 26 (1936).
21. 89 F. (2d) 112 (C. C. A. 6th, 1937).

on two substantial grounds, and held that the income from the trust involved, although substantially similar to the one in the *Douglas* case, was not taxable to the settlor. The court first carefully pointed out that in Michigan, the divorce court is bound, in the absence of fraud, by the agreement of the parties; the decree incorporating the agreement may not be revised; and the efficacy springs from the agreement and not from the decree. In Minnesota, where the divorce in the *Douglas* case was obtained, the divorce court can use its own discretion in adopting the agreement in its decree, can alter or revise it, and the binding effect comes from the decree and not the agreement. A second distinction made was that in the *Douglas* case the settlement provided for a specific sum, deficiencies to be made up by the settlor, and excess to be paid to him, while in the *Tuttle* case the amount was to be whatever the income of the particular property transferred happened to be. Thus, the court argued, the obligation of the settlor to support his wife did not continue. "Upon the creation of the trust, the trustor's obligation to his wife under both the contract and the decree were fully and finally liquidated." The distinction boils down to the difference between the discharge of the same obligation when it is created in different ways—by means of a private settlement or by means of a court decree. Even admitting the distinction in fact, there seems to be little reason for holding that the creation of a trust fully discharges the one, while only payment of income discharges the other. The court omitted to discuss the apparently contra cases of *Commissioner v. Hyde* [22] and *Helvering v. Brooks*.[23] At least one opportunity to follow the *Tuttle* case has been refused by the Board.[24]

A further problem in respect to the alimony trust arises with the remarriage of the wife. In *Harry S. Blumenthal*,[25] a trust was established in pursuance of the decree granting the divorce. The wife remarried three years later. The Board held that the obligation to support ceased with her remarriage, and that the income was not thereafter taxable to the husband. A contrary result was reached in *Alsop v. Commissioner*,[26] where the parties agreed, after a suggestion to that effect by the court, that the trust should be created "in lieu of alimony". The wife subsequently remarried and her second husband was still living. The Third Circuit Court of Appeals admitted that the obligation to support had disappeared but held that the income was still taxable to the settlor. This result was based on the reasoning that, as the husband created the trust in lieu of alimony, he made a bargain by which he escaped the payment of alimony; that he took a chance on it being a good or bad bargain, depending on future events, and that therefore the obligation incurred was for the duration of the trust—the lifetime of the wife. Although sanctioned by the Supreme Court, this argument seems to be neither practical, nor, as the court half admits, desirable.[27] Regardless of how the trust was created, the only reason for marking it as one of which the income is taxable to the settlor is because it discharges a legal obligation, that of supporting the wife, whether by means of alimony or not. Therefore, when support is no longer required, whether because of her remarriage or death, the income should

22. See *supra* note 16.

23. 82 F. (2d) 173 (C. C. A. 2d, 1936).

24. See Stephen J. Leonard, 36 B. T. A. 563, 571 (1937); John Ernest Goldring, 36 B. T. A. 779, 785 (1937).

25. 34 B. T. A. 994 (1936).

26. 92 F. (2d) 148 (C. C. A. 3d, 1937), *cert. denied*, 302 U. S. 767 (1938).

27. "It may seem hard that the petitioner must pay taxes on the income which supports another man's wife. . . ." *Id.* at 150.

no longer be taxed to him. The *Blumenthal* case was affirmed by a per curiam decision in the Second Circuit.[28]

In some instances, the husband, instead of creating a new trust, has assigned to the wife a portion of an existing one of which he is the beneficiary. The Board has held that although the trust was not created in contemplation of divorce, this is not sufficient to distinguish it from *Douglas v. Willcuts*. That the assignment discharges an obligation is enough.[29]

Where the husband and wife are still in a state of domestic bliss, it is much more difficult to find an obligation. In *Shanley v. Bowers*,[30] the husband set up a trust, a certain amount of the income of which was to be paid to the wife. No mention was made in the agreement of any duty which was discharged by the trust, and there was no restriction placed on the use of the money. The Second Circuit Court of Appeals spent little time in refuting the argument that the trust was in the discharge of a marital duty and therefore within the principle of the *Douglas* case. "Certainly a man must be able to make his wife a gift, if he wishes, without affecting his marital duty. No authority has been cited for the theory that every gift by a husband to his wife must be presumed to be in discharge of it. Nothing short of this will suffice to sustain the contention of the case at bar." [31]

An interesting and undecided problem would arise if, after a considerable period of time had elapsed, the Shanleys had been granted a divorce, and the decree had been silent as to alimony because of the existence of this trust. It would be difficult to say whether the courts, after all their emphasis on such phrases as "in lieu of alimony", and "set up as a discharge of marital rights", could find sufficient ground in their former opinions to hold the income taxable to the husband. But it can well be argued that the trust, although originally a gift, in fact now discharges a legal obligation and should now be taxable to the grantor as such. The same result should follow where a father, in an effort to avoid the tax, sets up a trust in favor of a straw man, and then has the latter assign his entire right to the children. No case could be found on either point.

The *Shanley* case was followed by the Board of Tax Appeals in *Merideth Wood*.[32] A further point was involved here due to the fact that the trust, although irrevocable, was only for a term of five years. Section 166 of the Revenue Act previously had stated that where the grantor at any time *during the taxable year* had the power to revest title to the corpus in himself, then the income of the trust was to be treated as his.[33] The omission of the words in the 1934 Act,[34] under which this case was decided, led to the treasury ruling that income from a trust for a term of three years or less would be taxable to the grantor.[35] Although the point may not have been pressed in this case and no definite holding was made, the Board indicated in its discussion that the term need only be more than a year for the settlor to escape.[36]

28. 91 F. (2d) 1009 (C. C. A. 2d, 1937).
29. Frank T. Hogan, 35 B. T. A. 26 (1936); Thorne Donnelley, 37 B. T. A., Jan. 14, 1938.
30. 81 F. (2d) 13 (C. C. A. 2d, 1936).
31. *Id.* at 15.
32. 37 B. T. A., June 17, 1938.
33. This was not changed until 1932. See § 166 of the 1928 Act, 45 STAT. 840 (1928).
34. 48 STAT. 729 (1934), 28 U. S. C. A. § 166 (1935).
35. U. S. Treas. Reg. 94, Art. 166-1 (c) A (1936).
36. To the same effect before the *Douglas* case, see United States v. First Nat'l Bank of Birmingham, 74 F. (2d) 360 (C. C. A. 5th, 1934).

It was recognized in two per curiam decisions soon after *Douglas v. Willcuts* that if income from a trust is to be applied to the maintenance and education of the grantor's children, such income will be taxed as the grantor's.[37] Qualifications have been added to this statement however. First, there must be either some indication in the trust instrument that the income was to be so used, especially where the trustee is the mother, or there must be evidence that the grantor asked the trustee to so use it. Secondly, the income must, in fact, have been used for the children. Unless both these factors are present, the income is not taxable to the grantor. Thus in *Henry A. B. Dunning,*[38] where there was no provision in the trust requiring the wife to use the income for any particular purpose, income in fact used to pay for the household expenses [39] and for the partial support of a minor child was held not taxable to the grantor. In two other cases the Board held that even though the terms of the trust provided that the income was to be used for the children, only so much of it as was actually used for this purpose could be taxed to the settlor.[40] Although nothing definite was said, the Board indicates that the petitioner must prove that income was not in fact used for the children when the agreement so allows it, while the government must prove in cases where there is no restriction, that the father had sufficient control over the trustee to indicate what should be done with the income.

As the mother usually has only a moral obligation to support the children, income from a trust established by her is not taxable to her.[41] It does not seem to be taxable to the father either, atlhough he is being relieved of an obligation just as if he created the trust himself. This suggests the procedure of *X* creating a trust for *Y's* children to whom, of course, he owes no legal obligation, while *Y* in return, creates a similar trust for *X's* children. Theoretically, the position is unassailable. Practically, the court would probably break down the whole arrangement. Even so, it would still be faced with the further problem, especially if the trusts varied at all in size, of deciding to whom which income should be taxed.

Thus it can be seen that in a little over three years the decisions have gone a long way beyond the strict holding of the *Douglas* case. The cases herein discussed have centered around trusts established at a time when the shadows of the present rulings were still faint. It is safe to say that

37. Helvering v. Schweitzer and Helvering v. Stokes, 296 U. S. 551 (1935), *supra* note 8. But the grantor is not taxable on income paid to an adult child because he is not obligated to support him. Stephen J. Leonard, 36 B. T. A. 563 (1937).

38. 36 B. T. A. 1222 (1937).

39. In Hill v. Commissioner, 88 F. (2d) 941 (C. C. A. 8th, 1937), a trust was set up by the husband for the express purpose of maintaining a home for his wife and three adult children. The court laid aside the common law "necessaries" which a husband must supply to his wife, and held that he was required to support her according to his estate and rank. Therefore the income was taxable to him. This indicates the substitution of a moral or social obligation for a strictly legal one in these cases. Although this has been done in the life insurance trusts, it was by benefit of statutory authority. Such result is a long way from the *Douglas* case.

40. Martin F. Tiernan, 37 B. T. A., June 14, 1938; *cf.* E. E. Black, 36 B. T. A. 346 (1937). In Ryburn G. Clay, 36 B. T. A. 1326 (Memo. Docket 86169, June 10, 1937), the father, who paid his daughter's necessaries out of his own pocket, was not taxable on income from a trust set up to pay for her luxuries. *Cf.* Hill v. Commissioner, *supra* note 39.

41. Martin F. Tiernan, 37 B. T. A., June 14, 1938. See Yolande v. Perkins, 38 B. T. A., July 28, 1937. In the latter case income from a trust established by the husband's will was payable to the wife unless she assigned it to the children. After she had exercised her power to assign, it was held that the income was no longer taxable to her when no showing was made that she had any obligation to support the children.

no case involving a trust set up since the *Douglas* case has yet reached the courts. Thus, whether the legal minds and scriveners that are pitted against the Treasury department can side-step these obstacles will be seen in the decisions of the next few years. At least a careful drafting of the trust agreement plus a little co-operation between the parties, especially the estranged husband and wife, will present many close cases. At the risk of repeating predictions of four years ago, it does not seem possible that the courts can go much further without express statutory authority. Yet even now, all the loopholes have not been closed by the present decisions.

W. F. S.