Under the Erie doctrine, federal courts are required to apply state law to determine the outcome of litigation where the matter involved is not expressly governed by the federal constitution or acts of Congress. In suits where the United States is a party to a commercial instrument, however, the exercise of a constitutional function or power may often render Erie inapplicable in determining the Government’s rights and duties. If a federal rule is thus required, state law cannot control unless incorporated as an appropriate source of federal common law. Without articulating the basis for its choice of law, the Fifth Circuit in *United States v. Yazell* held that a Texas law invalidating most married women’s contracts was a valid defense to a deficiency judgment on a loan executed to the Small Business Administration (SBA).

In *Yazell*, the defendant and her husband (trading as a partnership) had signed a promissory note to repay money borrowed as a disaster loan from the SBA. After default by the husband and defendant, the federal government foreclosed on a chattel mortgage and subsequently sued for a deficiency judgment against both

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Some courts have limited the application of Erie to diversity cases. See, e.g., United States v. View Crest Garden Apts., Inc., 268 F.2d 380, 382 (9th Cir.), cert. denied, 361 U.S. 884 (1959); American Textile Mach. Corp. v. United States, 220 F.2d 584, 587 (6th Cir. 1955); Sands v. United States, 198 F. Supp. 880, 883 (W.D. Wash. 1960), aff’d sub nom., 295 F.2d 481 (9th Cir. 1961). *Contra*, IA Moore, Federal Practice ¶ 0.305[3], at 3052-57 (1961) (the law to be applied is keyed to the nature of the issue rather than the jurisdictional basis). For non-diversity cases in which Erie was applied, see cases cited id. at 3055 n.7. For the application of federal law in a diversity case, see American Pipe & Steel Corp. v. Firestone Tire & Rubber Co., 292 F.2d 640, 644 (9th Cir. 1961).


3 384 F.2d 454 (5th Cir. 1964), cert. granted, 85 S. Ct. 651 (1965) (No. 575).

4 Id. at 456.
obligors. Although the federal district court entered a judgment against the husband, it held that under Texas law a contract to which a married woman is a party is unenforceable as to her separate property. The Court of Appeals for the Fifth Circuit affirmed on the ground that one incapable of making a contract cannot be held liable merely because the United States was a party to the instrument.

After Erie announced that there was no federal general common law, the federal courts applied state law in cases where the federal government was a party to a commercial instrument. In Clearfield Trust Co. v. United States, however, the Supreme Court decided that Erie was inapplicable in determining the rights and duties of the United States on a forged government check, because the authority to issue such checks was derived from "the Constitution and the statutes of the United States." The Court reasoned that application of state law would subject the Government's legal rights to "exceptional uncertainty," and would render identical transactions subject to the "vagaries of the laws of the several states." Thus there emerged an area of "federal common law" pursuant to the Clearfield mandate that "in absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards." In cases involving government contracts, government issue of commercial paper, and execution...
of commercial instruments to the government, the rights and liabilities of the United States acting on its own behalf or through one of its agencies has often been determined by federal common law if there is no controlling act of Congress.

In determining whether federal law should apply to these cases, the courts have considered the following criteria: whether the activity of the Government was authorized by a Constitutional function or power; the existence of relevant federal statutes; and the presence of a sufficient federal interest. In these instances, Erle has no effect on matters which vitally affect the interests, powers and relations of the United States requiring uniform national disposition. Once federal law is deemed controlling, the courts may refer to several sources to determine the appropriate federal rule, including federal case law, the Negotiable Instruments Law, the Rice Co., 323 U.S. 106 (1944); United States v. County of Allegheny, 322 U.S. 174 (1944); United States v. Taylor, 333 F.2d 633 (5th Cir. 1964); United States v. Chester Park Apartments, Inc., 332 F.2d 1 (8th Cir. 1964); Reimann v. United States, 315 F.2d 746 (9th Cir. 1963); Krupp v. Federal Housing Administration, 285 F.2d 833 (1st Cir. 1961); American Houses, Inc. v. Schneider, 211 F.2d 881 (3d Cir. 1954).

Even before Clearfield, federal law was held applicable in a few government contract cases for this reason. See Royal Indemnity Co. v. United States, 313 U.S. 289, 296 (1941) (federal right is not dependent on state remedy); Byron Jackson Co. v. United States, 33 F. Supp. 665 (S.D. Cal. 1940). See generally Polcher, supra note 8.


Uniform Sales Act, and Restatements. Provisions of state law may also be adopted or incorporated as the federal rule when considered adequate to accomplish the required federal policy or when consistent with adequate protection of the federal interest.

Since the United States was suing to enforce a promissory note to which it was a party, the result in Yazell can only be justified as either: (1) the application of Erie due to the absence of a sufficient federal interest or policy; or (2) the incorporation of Texas law as the appropriate federal rule.

Although the Fifth Circuit distinguished Clearfield on its facts,
the theory of that decision has been extended to other factual settings including those where the United States sues to enforce a promissory note executed to a federal agency. The disaster loans which the SBA administers to small business constitute the exercise of a function authorized by the Constitution and federal statutes. In *Bumb v. United States*, the Ninth Circuit held that this authorization alone was sufficient to require the application of federal common law in determining the validity of chattel mortgages executed to the SBA.

Similarly, in a suit to foreclose mortgages insured by the Federal Housing Administration (FHA), the Sixth Circuit in *United States v. Helz* also found federal law to be applicable because that agency's lending activity was authorized by statute. That decision, however, went beyond the analysis offered in *Bumb* and evaluated the federal interest in preserving the money and credit of the Government, and the policy of protecting federal investments to facilitate the building of homes. Since the FHA and SBA both operate through local offices for the benefit of financially distressed citizens, the success of both programs requires that the United States be able to collect loans and protect its investments. The only major difference between the two agencies is the ultimate use of their loans, thus, the interest and policy of the Government in enforcing repayment of FHA loans would seem to apply to the SBA as well. In light of the constitutional and statutory authorization for lending activities, the policy of aiding small business, and the federal interest in collection, the better view would appear to be that *Yazell* is not a proper case for the *Erie* requirement of state law.

The result reached by the Fifth Circuit, therefore, is justifiable only if Texas law of coverture can be incorporated as an appropriate commercial paper issued by and as an obligation of the United States," but was merely a simple case of whether a married woman could be held liable on a contract which "she was incapable of making."

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80 See cases cited notes 15 and 17 supra.

81 See, e.g., *United States v. Helz*, 314 F.2d 301 (6th Cir. 1963) (note originally executed to a bank, but subsequently acquired by the FHA, which succeeded to the bank's rights); *Hendry v. United States*, 305 F.2d 515 (9th Cir. 1962).


83 276 F.2d 729 (9th Cir. 1960).

84 314 F.2d 301 (6th Cir. 1963).
source for determining the federal rule. In deciding whether state law should be adopted instead of an independent federal rule, some lower federal courts have balanced the state and federal interests. Thus they have evaluated the federal interest in uniform rights and duties and effective remedies to protect the security of federal investments, as against state procedural safeguards and policy.

Generally, local law is deemed inconsistent with the appropriate federal rule when it frustrates the remedies of the Government as opposed to merely stipulating procedures to be followed in effectuating a valid transaction. In Bumb, therefore, the local recording statute was applied because it did not purport to preclude the Government's remedy in foreclosing a validly created security interest. The requirement of filing notice for the benefit of other creditors did not inhibit the Government's right to require security for its loans. In Helz, however, state law of coverture was rejected as a valid defense because it prohibited any recovery on a note executed by the defendant. Arguably, the Texas law in Yazell was merely a procedure and not frustration of a remedy because a mar-

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35 In United States v. Standard Oil Co., 332 U.S. 301, 309 (1947), the Court stated that state law may be applied when Congress has so consented. In Bumb v. United States, 276 F.2d 729 (9th Cir. 1960), the court found no congressional intent to exempt requirements for SBA loans from local law. Id. at 736.

36 See United States v. View Crest Garden Apts., Inc., 268 F.2d 380 (9th Cir.), cert. denied, 361 U.S. 884 (1959), where the court stated, "A court confronted with [the question of redemption, for example]...could determine it by weighing the federal interest against the particular local policy involved. If the considerations weighed by the court suggest an adoption of local law, such as the local rule on redemption, that could be done. But if on the other hand necessity requires the fashioning of a federal rule, absent a declared federal rule on the subject the federal courts are authorized to and capable of fashioning one." Id. at 383. See Bumb v. United States, note 35 supra; Wright, FEDERAL COURTS 216-17 (1963); Mishkin, The Variousness of "Federal Law": Competence & Discretion in the Choice of National & State Rules for Decision, 105 U. PA. L. REV. 797, 810-14 (1957).

37 United States v. Helz, 314 F.2d 301 (6th Cir. 1963). In United States v. View Crest Garden Apts., Inc., note 36 supra, the court stressed that when remedies are involved the federal policy to protect the Treasury and to promote the security of federal investment is paramount.

38 Bumb v. United States, 276 F.2d 729 (9th Cir. 1960); United States v. View Crest Garden Apts., Inc., 268 F.2d 380, 383 (9th Cir.), cert. denied, 361 U.S. 884 (1959) (dictum).

39 The defendant and her husband had executed two notes to a banking institution to secure a loan for improvements on their home. Prior to the making of the loan, they had provided for FHA payment insurance under the National Housing Act. After a default, the notes were assigned to the United States on behalf of the FHA. Since the husband had been discharged in bankruptcy, the United States sought to recover from the wife. 314 F.2d at 302. The court fashioned an independent federal rule which disallowed the common law defense of coverture in Michigan and provided for enforcement of the obligation. Id. at 303.
ried woman was enabled by statute to waive the contractual disabil-
ity afforded by coverture. Thus, the federal government could
have collected its loans by requiring the defendant to waive her pro-
tection. Nonetheless, the Fifth Circuit relied upon another theory
by asserting that the defendant's disability invalidated her contrac-
tual liability from its inception, in the same manner accorded con-
tracts of a person of minor age or unsound mind. Under this
rationale, the remedy-procedure dichotomy is not presented because
a legal obligation was never incurred.

This analogy to the law governing persons of minor age or unsound
mind, however, fails to satisfy the federal interest in uniform
rules governing the disposition of federal rights and duties on com-
mercial instruments. Uniformity facilitates the effective admin-
istration of federal loans by obviating the necessity of tailoring loan
programs to the law and policy of each state. A fundamental dis-
tinction between the recording requirement in Bumb, the disability
of minors and persons of unsound mind on the one hand, and the
Texas law of coverture on the other, is that the former represent
policies to which all states adhere; the disability of married women
is an archaic common law concept remaining only in a few states. Since
the SBA is involved in the extension of credit on a nationwide

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40 Under Texas law any married woman could have applied by written request to a
district court for an order removing her disability. If it appeared to the court that
waiver would have been to the applicant's advantage, the court could have entered its
decree declaring her capable of contracting for mercantile or trading purposes. 13
Vernon's Ann. Civ. St. art. 4626 (1960). The provision has since been amended, Acts
1963, ch. 472 § 6, and the repeal of article 4623 has rendered article 4626 nugatory.
See note 5 supra.

41 See, e.g., Clearfield Trust Co. v. United States, 318 U.S. 363 (1943); United States
v. Sommerville, 224 F.2d 712 (3d Cir. 1963); Sands v. United States, 198 F. Supp. 880
(W.D. Wash. 1960), aff'd sub nom. First Federal Sav. & Loan Ass'n v. United States,
295 F.2d 481 (9th Cir. 1961); Guy F. Atkinson Co. v. Merritt, Chapman & Scott Corp.,
141 F. Supp. 833 (N.D. Cal. 1956), aff'd, 295 F.2d 14 (9th Cir. 1961). The dissenter in
Yazell stated that uniform application of the Small Business Act was necessary to
insure the repayment of large sums of money. He contended that the general applica-
tion of local rules as to contractual capacity would result in "chaos which would
nullify federal programs for disaster relief..." 394 F.2d at 456. Furthermore, he
argued that the decision of the majority could not be limited to the Small Business
Act, but would frustrate a multitude of other federal programs. Ibid.

42 In Bumb the court noted the general enactment of laws requiring notice of
intent to mortgage and stated that no hardship would be imposed on the SBA under
such a rule, "in the light of the fact the policy of all states of the Union is to give to
such creditors some modicum of protection." 276 F.2d at 738.

43 See 26 Am. Jur. Husband & Wife § 20 (1940), which states that the disability of a
wife to act and contract as a legal person has been removed in practically all states.
basis, this type of variant law is a prime example of the evil which
has necessitated the application of uniform federal rules.

Nevertheless, there are compelling reasons for asserting that the
federal interest in uniformity is inconsistent with the administration
of loans by the SBA. As the Ninth Circuit recognized in Bumb,
this agency operates on a local basis with local personnel who should
be aware of laws of the state in which they work. Since the admin-
istration of such loans involves many contractual and property ques-
tions governed by state law, the agency would not be overburdened
by recognizing the Texas policy supporting coverture. Furthermore,
alert SBA officials could have easily required the defendant in
Yazell to waive her contractual disability as a condition to the
loan. Aside from these factors, the application of a well-established body
of local law would also provide the prospective borrower with a
greater degree of certainty as to his individual rights and obligations.
An independent federal rule drawn from disparate sources of law leaves both parties in doubt; many sources of law would have to be
checked to insure the protection for which each party bargains.

Much of the confusion reflected in the Yazell, Bumb and Helz
decisions could be eliminated if Congress adopted the Uniform Com-
mercial Code as the exclusive source of federal law. In those

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46 For a discussion of the Texas policy on married women's contracts see Red River Nat'l Bank v. Ferguson, 109 Tex. 287, 206 S.W. 923 (1918). The court stated, "the steady unbroken policy of the laws of Texas has been to protect the property of the wife from the debts of the husband." Id. at 924. The court explained, "if [the wife's] powers have been restricted, her property, at least, has been safeguarded. The limitations upon her authority are but the expression of a scrupulous concern for the preservation of her estate, and were imposed to that end. In that interest her authority to contract debts at all was confined to those essentially to her advantage, that is, for necessities for herself or her children and the benefit of her estate...." Id. at 925. See Tolbert v. Standard Acc. Ins. Co., 148 Tex. 235, 223 S.W.2d 617 (1949).
47 See note 46 supra.
48 For the various sources utilized see notes 23-26 supra.
49 See Friendly, In Praise of Erie—and of the New Federal Common Law, 19 Record of N.Y.C.B.A. 64 (1964), suggesting that such adoption might meet the desire for uniformity. However, Judge Friendly states that it would be difficult to determine the scope of the enactment: "Should such a federal rule apply only to transactions where the papers or the goods they represent cross state lines? Should it exhaust the commerce power by one of the traditional wordings or adopt the suggested form of covering 'every case where there is some basis for applying the law of more than one state?' Should it go even further and also include all commercial contracts with the federal government, all such contracts sought to be enforced in admiralty, even all
states which have already adopted the Code, the prospective borrower would not be faced with a different rule when dealing with federal agencies. But until the Code is adopted by legislative enactment or judicial decree, the local activities of such federal agencies as the SBA tend to justify choice of law decisions incorporating state law whenever possible.

such contracts passing through the mail. Or should Congress take the bolder step of declaring that in order to make its rule truly workable in these large areas of its enumerated powers, the small remaining enclaves must also be occupied." *Id.* at 90-91.