1965

Recent Decisions

M. M. B.

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Administrative Law — Revocation of License — Due Process

Plaintiff-licensee had been conducting a business of wholesaling cigarettes without the required meter impression, in violation of Tex. Tax-Gen. art. 7.21.1 On account of these illegal operations and without notice or hearing, the state comptroller notified the plaintiff that its permit to sell cigarettes had been forfeited. The plaintiff sought to enjoin the cancellation of the permit. The trial court denied the application for a temporary injunction, sustaining the comptroller’s action. The court of civil appeals affirmed on the ground that article 7.21 did not expressly provide for notice or hearing, and that the plaintiff in fact was given a hearing in the trial court on its application for an injunction. Held, reversed: A permit to sell cigarettes is a privilege which, once it has been granted, is a valuable right which cannot be revoked without adequate notice and hearing preceding the final administrative order. House of Tobacco, Inc. v. Robert S. Calvert, Comptroller, 394 S.W.2d 654 (Tex. 1965).

It is well settled that constitutional due process requires that an individual be given adequate notice and hearing before any property right is taken from him by governmental action. Under the doctrine of privilege, however, an individual is not afforded the same protection when there is a privilege involved as distinguished from a property right.2 Privileges are those activities which the state can deny if it so chooses, while rights are those activities which a state cannot deny completely but can only regulate.3 The majority of jurisdictions have accepted the general rule that a privilege granted under the police power of the state can be revoked at any time without notice or hearing because it is not considered to be a property right in the constitutional sense.4 The Texas courts, as well as the majority of other jurisdictions, have confused matters by adopting the rule that some privileges once acquired become valuable “rights,” protected by the due process clauses of the federal and state constitutions.5

2 For a general discussion of the doctrine of privilege, see 1 Davis, Administrative Law § 7.19, at 505-506 and § 7.11, at 452-455 (1958).
3 Ibid.
5 Francisco v. Board of Dental Examiners, 149 S.W.2d 619 (Tex. Civ. App. 1941) error ref.
It is not clear what standards the courts use in determining whether a privilege is an ordinary one granted under the police power and revocable without due process or whether it is a more valuable privilege to which constitutional protection attaches when it is granted. The revocation of a liquor or dance hall license without notice or hearing would not violate due process because these business activities are deemed by the courts to be mere privileges granted under the police power of the state. On the other hand, the courts have granted legal protection to the privileges of practicing the medical or legal professions once license is granted. In *Francisco v. Board of Dental Examiners,* involving the revocation of a dentist’s license, the court held that the privilege to practice once acquired is a valuable “right” and is entitled to protection under due process.

Some jurisdictions have placed cigarettes in the same category as liquor on the basis that both are regulated under the police power of the state for the health, safety, and welfare of the public. In Texas, however, the regulation of cigarettes is deemed an exercise of the tax power of the state rather than the police power. The court reasoned that a distributor of cigarettes is not much different from a dentist in that both have invested money in their businesses, and if their licenses are revoked, each must turn to some other occupation. Accordingly, the court decided that a permit to sell cigarettes “is a privilege which does not have to be granted; however, once it is granted it cannot be taken away except for good cause.”

Apparently, the courts in Texas will continue to follow the majority rule that a privilege which is regulated due to the need for the protection of the public under the police power is not entitled to constitutional due process of law. But the courts will grant legal protection to certain privileges that they designate to be valuable “rights” once the privileges have been granted. The privilege of selling cigarettes in Texas now demands due process of law before revocation, merely because the court has deemed this activity to be a valuable “right” (privilege). The distinction made between various types of activities has been criticized as being extremely unfair.

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7 149 S.W.2d at 622.
6 Austin v. Tennessee, 179 U.S. 243 (1900); Walker v. City of Clinton, 19 N.W.2d 785 (Iowa 1953).
5 See Harris v. Shepperd, 116 Tex. 18, 291 S.W.2d 721 (1956). Also Tex. Tax-Gen. Ann. art. 7.41 (1959) states that it was intended by the legislature for the regulation of cigarettes to be an excise or use tax.
10 194 S.W.2d at 657.
Regardless of how much capital a licensee might have invested in his business, his permit to carry on his operations may be revoked at any time without notice or hearing depending on whether his occupation has been classified by the courts as an ordinary privilege or a valuable "right." It is somewhat disturbing to note that both a liquor license and a license to practice medicine or law are privileges granted under the police power of the state, yet the latter, through some unintelligible principle, has been moved by the courts to the position of a valuable "right." The court in the instant case expressed it well when in comparing dentistry to the occupation of selling cigarettes stated that "To draw the line here on the basis of whether one is practicing a profession would seem somewhat arbitrary and unjust." The better rule, accepted in at least one jurisdiction, is that the doctrine of privilege should be abandoned and all licensees afforded notification and hearing before revocation of their licenses.

M.M.B.

Antitrust — Clayton Act Section 5(b) — Leh v. General Petroleum Corp.

In 1956 petitioners filed an action seeking damages from General Petroleum Corp. for violations of sections 1 and 2 of the Sherman Act. Defendants maintained that the suit was barred by the California one-year statute of limitations. It was admitted that the cause of action had accrued no later than 1954, and that the four-year limitation period created by Clayton Act section 4B did not apply as that section was not passed until 1955. Petitioners contended that, because of an antitrust action brought by the United States in 1950 and still pending in 1956, Clayton Act section 5(b) had tolled the running of limitations. Section 5(b) provides that during the pendency of an action instituted by the United States the statute of limitations will be suspended in respect to private actions "based in whole or in part on any matter complained of in said proceeding." The district court dismissed the complaint on the basis of the one-year statute, and stated that Clayton section 5(b) did not apply because

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13 394 S.W.2d at 617.
there was not sufficient similarity between petitioner's action and that
brought by the United States. The Court of Appeals for the Ninth
Circuit affirmed. Held, reversed: Section 5(b) will toll the statute
of limitations if "reliance upon the government proceeding is not
mere sham and that the matters complained of in the government
suit bear a real relation to the private plaintiff's claim for relief."

This decision resolves a conflict among the circuits. Previously, the
Ninth Circuit, in Steiner v. 20th Century Fox Film Corp., had
given section 5(b) a narrow construction, analogizing it to the
collateral estoppel principles used in section 5(a). Steiner states that
"greater similarity is needed than that the same conspiracies are
alleged. The same means must be used to achieve the same objectives
of the same conspiracies by the same defendants."

The Tenth Circuit in Union Carbide & Carbon Corporation v. Nisley had decided that "substantial identity of subject matter" was all that is needed to make
section 5(b) apply.

Leh presented an ideal fact pattern to resolve this conflict. The
United States action was based on an alleged violation occurring be-
tween 1936 and 1950. Leh's complaint used a period from 1948 to
1954. The defendants named in each suit were drawn from the same
group of oil companies and were substantially identical. However,
Leh did not name Shell Oil Company or the Conservation Committee
of California Oil Producers in his group of defendants, and did name
Olympic Oil Company. The United States had included Shell and
the Committee, but had excluded Olympic. Noting that Minnesota
Mining & Mfg. Co. v. New Jersey Wood had damaged the founda-
tions of the Steiner decision, and quoting extensively from Minnesota,
the Supreme Court interpreted section 5(b) broadly and found
sufficient identity of parties and actions.

The Minnesota case clearly foreshadowed the decision in Leh. The
question presented in Minnesota was whether proceedings by the
Federal Trade Commission tolled the running of limitations to the
same extent as judicial proceedings. The Court found that, "the §
5(b) advantages flow as naturally from Commission proceedings
as they do from Justice Department actions."

4 Leh v. General Petroleum Corp., 330 F.2d 288 (9th Cir. 1964).
6 232 F.2d 190 (9th Cir. 1966).
7 Id. at 196.
8 300 F.2d 561 (10th Cir. 1962).
10 Id. at 320.
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tained a comprehensive discussion of the purposes and effects of section 5 (b), however, the requisite degree of identity of parties and causes of action was not settled. The Leh opinion answers this question and provides the elastic standard "that the matters complained of in the government suit bear a real relation to the private plaintiff's claim for relief."

J.M.W.

**Constitutional Law — Freedom of Speech and of the Press — Times Rule Extended to "Public Men"**

According to press releases, Plaintiff, Maj. General Edwin A. Walker had led a charge of rioters against United States Marshals who were carrying out orders to integrate the University of Mississippi campus. Plaintiff filed this action for libel in the sum of two million dollars against defendants, Courier-Journal, Louisville Times Company, and WHAS, Inc. The court treated the factual allegations as true for the purpose of passing upon a motion to dismiss. Held: The New York Times rule, that the Constitution limits punishment for defamation of a public official in the conduct of his duties to statement proved to be knowingly or recklessly false, extends to "public men" in situations of national concern. The actual malice—i.e., knowing or reckless falsehood, necessary for punishment under the Times rule was not shown to exist on the part of the publishers. Walker v. Courier-Journal, — F. Supp. — (W.D.Ky. 1965).

The district court stated that the New York Times case created federal standards in matters of "grave national concern" involving public officials. A situation involving integration has been classified by the Supreme Court as a matter of national concern, in fact, one of the "major political issues of our time." The district court felt that in such a case extension of the Times rule to "public men" is justified by the language of the New York Times decision. In that case, the Supreme Court quoted with approval Coleman v. McLennan in which a Kansas court said, "This privilege extends to a great variety


3 78 Kan. 711, 98 P. 281 (1908).
of subjects and includes matters of public concern, public men and candidates for office."4 Furthermore, in a footnote the Court stated, "We have no occasion here . . . to specify categories or persons who would or would not be included."5 From these statements, the district court felt justified in concluding:

[T]he Supreme Court of the United States has served clear notice that the broad Constitutional protections afforded by the First and Fourteenth Amendments will not be limited to "public officials" only, for to have any meaning the protections must be extended to other categories of individuals or persons involved in the area of public debate or who have become involved in matters of public concern.6

After taking judicial notice of the fact that plaintiff's public life is well known nationally, the court mentioned vague qualifications in determining the existence of "public men":

Public debate cannot be "uninhibited, robust and wide open" if the news media are compelled to stand legally in awe of error in reporting the words, and actions of persons of national prominence and influence (not 'public officials') who are nevertheless voluntarily injecting themselves into matters of grave public concern attempting thereby through use of their leadership and influence, to mold public thought and opinion to their own way of thinking.7

The court felt that plaintiff had reasonably foreseen that his personal status would be interwoven into that of a "public one whereby he would become the subject of substantial press, radio and television news comment, thus magnifying the chance that his activities would be 'erroneously' reported. . . . Public men are, as it were, public property."8

In finding that malice did not exist under the extended rule, the court mentioned only the vaguest of guidelines for determining actual malice:

Everyone knows that news of any matter of public concern possesses a limited lifetime, for to be news it must be published with promptness and dispatch in order that the public be kept informed as to the actions of "public men." This Court is of the opinion that the Defendants (reasonably) had the right to rely upon the reputable national news sources.9

4 376 U.S. 254, 281-82 (1964). (Emphasis added.)
8 Ibid. See also Garrison v. Louisiana, 379 U.S. 64, 78 (1964).
9 Ibid.
Universality of the publication clearly negates the possible attribution of "actual malice" to any single publisher.

The decision is vastly important in that it extends the Times rule, which had been limited in scope to an area of libel seldom litigated,\textsuperscript{10} to one that is much more significant and sweeping in scope. Because suits by General Walker are pending against the Associated Press in Texas, Colorado, Louisiana and Mississippi; against newspapers in Texas, Louisiana, Georgia, Florida, Missouri, Colorado, and Wisconsin; and against Newsweek Magazine in Oklahoma, it seems certain that the Supreme Court will soon be confronted with the question of extension. If the Court extends the rule to "public men,"\textsuperscript{11} it would be desirable that it also establish specific standards for determining when an individual becomes a "public man" or what statements amount to "actual malice." The vague allusions to such standards by the district court are insufficient as guidelines for trial courts to follow.

\textit{G.B.R.}

\section*{Corporations — Beneficial Owner of Stock Allowed to Inspect Corporation’s Books}

In a division of community property upon divorce, the judgment gave the wife a beneficial interest in ten per cent of the stock of defendant corporation. The remaining ninety per cent was vested in the husband subject to a lien. All of the stock was placed in trust, with the husband having the right to vote it. The judgment provided that the wife had no legal concern as to whether dividends were paid, and "she was restricted to receipt of her part of any dividends declared or the proceeds of sale and that she should not have the right to question the propriety of management or have any other minority stockholder right. . . ."\textsuperscript{12} The wife sought a writ of mandamus ordering the corporation to allow her to inspect its books. Defendant asserted that under article 2.44 of the Texas Business Corporation Act the wife was not a stockholder "of record" and therefore she was

\textsuperscript{10} Noel, \textit{Defamation of Public Officers and Candidates}, 49 Colum. L. Rev. 873, 893 (1949).

\textsuperscript{11} For the use of the term "public figure" in this connection see Note, 48 Marq. L. Rev. 128, 133 (1964); and Note, 78 Harv. L. Rev. 201, 204 (1964).

not entitled to inspect the books. The trial court granted mandamus. Held, affirmed: The holder of a beneficial interest in stock has a right at common law, upon application to a court of competent jurisdiction and proof of a proper purpose, to inspect the company's books. *Texas Infra-Red Radiant Co. v. Erwin*, 497 S.W.2d 491 (Tex. Civ. App. 1965).

Article 2.44B of the Texas Business Corporation Act, entitled "Books and Records," reads in part as follows:

Any person who shall have been a shareholder of record for at least six (6) months immediately preceding his demand, or who shall be the holder of record of at least five per cent (5%) of all the outstanding shares of a corporation, upon written demand stating the purpose thereof, shall have the right to examine... its books...

This section clearly indicates that the person wishing to inspect the books must be a shareholder "of record." The court in *Texas Infra-Red Radiant Co.* did not rely on section B, but on a common law right that was supposedly preserved by section C. The decision states, "Section C was intended to make it clear that a shareholder's right of examination under the common-law was not restricted by said statute."

Nothing herein contained shall impair the power of any court of competent jurisdiction, upon proof by a shareholder of proper purpose, irrespective of the period of time during which such shareholder shall have been a shareholder of record, and irrespective of the number of shares held by him, to compel the production, for examination by such shareholder, of the books and records of account, minutes, and record of shareholders of a corporation.

From the wording of section C it is difficult to determine if the courts are entitled to disregard the "of record" requirement. Obviously both the time and percentage of ownership requirements can be ignored. As this portion of the Texas Act is identical to the Model Act, and there are many decisions in other states interpreting the section as intending to preserve the common law right, there can be little doubt that such a right exists. However, does it extend to beneficial owners?

No previous authority in Texas, allowing a beneficial owner of stock the right to inspect the company's books, can be found. However, the decision in *Texas Infra-Red Radiant Co.* appears to be sound.

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*Id.* at 493.

2 The wording of section C is exactly the same as a portion of section 46 of the Model Business Corporation Act.

3 Bishop's Estate v. Antilles Enterprises, Inc., 252 F.2d 498 (3d Cir. 1958), and *In re Bush Terminal Co.*, 78 F.2d 662 (2d Cir. 1935).
The pre-requisites for allowance of the common law right are ample protection for the corporation. The decision to permit inspection must be made by a court of competent jurisdiction after the showing of a "proper" purpose by the demandant. At the same time, a beneficial owner has a real interest in the management of the corporation, and should be given access to the corporate books and records.

J.M.W.

**Criminal Law — Failure to Notify Defendant of Right to Assistance of Counsel in Misdemeanor Case Invalidates Plea of Guilty**

Defendant was convicted in a county court of Florida for the misdemeanors of illegal sale and illegal possession of liquor, and, upon each count, she was sentenced to serve six months in the county jail or to pay a fine of $250. Following her incarceration defendant sought to withdraw her pleas of guilty and made a motion for a new trial on the grounds that she was without counsel at the time of her arraignment, that she was indigent and unable to employ counsel, and that she was not advised by the court of her right to counsel. Upon denial of her motions, defendant filed application for a writ of habeas corpus in the United States district court.\(^1\) The court denied defendant's habeas corpus application and defendant appealed. *Held, reversed:* Failure to notify the defendant of her right to the assistance of counsel rendered the plea of guilty and the judgment of conviction and sentence constitutionally invalid, notwithstanding the fact that both counts upon which defendant was sentenced were misdemeanors. *McDonald v. Moore*, 353 F.2d 106 (5th Cir. 1965).

The Fifth Circuit's opinion in *Harvey v. Mississippi*\(^2\) marked the first time that a federal court had ruled that an indigent defendant in a misdemeanor case was denied due process of law in a state court if he was not notified of his right to the assistance of court-appointed

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\(^1\) This decision would also affect Tex. Bus. Corp. Act Ann. art. 2.30B (1956), concerning voting agreement copies deposited with the corporation. See Comment, 12 Sw. L.J. 61, 72 (1958).

\(^2\) The district court held that state remedies, by reason of a Florida Supreme Court decision, had been pursued to an extent sufficient to warrant application for federal relief. In *Fish v. State*, 159 So.2d 866 (Fla. 1964), the court held that *Gideon* applied only to felony cases.
counsel. In the instant case, the court observes that "under Gideon, states must now provide counsel for indigent defendants in criminal cases to the same extent as the United States, under like circumstances, must [provide] . . . in Federal cases." The federal standard is codified in the Criminal Justice Act of 1964 which provides that in cases of petty offenses, an indigent defendant may be denied assistance of counsel, but the appointment of counsel is required in cases of all other crimes. A petty offense is defined as one for which the penalty does not exceed imprisonment for a period of six months or a fine of not more than $500, or both. While the court notes that it is without authority to announce a petty offense rule which would be controlling in state proceedings, it acknowledges that "such a rule would provide a rule of certainty and one which might be fair in most situations although it would be difficult to sustain on any legal ground." In this connection, it is interesting to note that had the Harvey case been a federal prosecution, the offense with which Harvey was charged would have been a petty offense.

The court indicates that they would not extend the right to counsel to a person in a municipal court charged with being drunk and disorderly, and that they would be even less likely to extend the right to a person given a ticket for a traffic violation. The rationale for this position is founded upon the great burden which would be placed upon the bar. While the court apparently favors following what Congress has deemed the federal standard, i.e., providing court-appointed counsel for indigents accused of misdemeanors other than petty offenses, the Harvey decision would indicate that the constitutional standard extends beyond this line. This much seems clear: the constitution requires state courts to provide court-appointed counsel whenever the gravity of the offense exceeds that of a federal misdemeanor. How far beyond that line the courts are willing to go must await subsequent determination.

C.W.M.

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2 McDonald v. Moore, 353 F.2d 106, 108 (5th Cir. 1965).
5 McDonald v. Moore, 353 F.2d at 109, n.4 (5th Cir. 1965).
6 Harvey was charged with possession of whiskey, a misdemeanor in Mississippi, punishable by a fine of up to $500 and up to ninety days in jail.
Family Law — Legitimation of Children of Annulled Marriages

Plaintiff, the father, instituted suit to determine custodial and other rights in his child conceived prior to marriage and born after annulment of the marriage. He and the mother had been ceremonially married, at which time the mother was pregnant with the child. After living together for a short time, the expectant mother left plaintiff and sought an annulment of the marriage. Plaintiff consented to the annulment upon assurance from the mother that she would relinquish the child into his custody. Judgment annulling the marriage became final prior to the birth of the child. After judgment the mother disappeared. When plaintiff finally located the mother, he discovered that the child had been judicially declared neglected and had been placed with an adoption agency. Plaintiff consulted with the agency regarding the child’s identity and location. However, the agency refused to give plaintiff any information, claiming that plaintiff had no rights in the child. The trial court rendered summary judgment for the defendant agency but the court of civil appeals reversed and defendant agency appealed. Held, affirmed: The child was legitimated upon the marriage of the parents and could not be bastardized merely because marriage was dissolved by annulment rather than by divorce. Home of the Holy Infancy v. Kaska, 397 S.W.2d 208 (Tex. 1965).

Under Texas law, unless the child is legitimate, the father is under no duty of support nor is his consent necessary to adoption. Therefore, without the correlative responsibilities, the father has no custodial or other rights in his child merely by virtue of being the father. However, the legal relationship existing between a father and his child, subsequently legitimated by statute, should be the same as that of a father and his legitimate child.

Section 42 of the Probate Code provides the statutory basis upon which a child is legitimated in Texas. The statute was construed in James v. James, where the court indicated that the Texas Legislature

1 See Lane v. Phillips, 69 Tex. 240, 6 S.W. 610 (1887); Beaver v. State, 96 Tex. Crim. 179, 216 S.W. 929 (1923).
5 Tex. Prob. Code Ann. § 42 (1916) "Where a man, having by a woman a child or children shall afterwards intermarry with such woman, such child or children shall thereby be legitimated and made capable of inheriting his estate."

6 213 S.W. 1112 (Tex. Civ. App. 1923) error ref.
intended the statute to provide for full legitimation and concluded that upon the marriage of the parents their child previously born was legitimated for all purposes. In the instant case, the child was born after annulment of the marriage rather than prior to the marriage as in James. However, the court relied upon an earlier decision and held that the statute operated whenever a valid marriage occurred after conception of the child.

The defendant agency, in the principal case, argued that the statute did not apply because the marriage was annulled. It reasoned that an annulment places the parties in the same position as if they had never married, and, as a consequence, would deprive the child of its legitimate status. The court, however, concluded that the legitimation statute was enacted for the humane purpose of avoiding the stigma of illegitimacy and should be liberally construed to effectuate that purpose. Therefore, even though the annulment decree may relate back to the time of the marriage as between the parties to the annulment, the decree will not be given that effect regarding the legitimacy of their child. The court made it clear that merely because the law had created a fiction concerning a voidable marriage that such fiction would not lead to an unjust result respecting the rights of a third party. The legitimacy of a child of an annulled marriage is an exception to the theory that the marriage is void ab initio.

J.W.B.

Federal Venue — Transfer Under Section 1404(a)

The plaintiffs filed suit in the federal district court of Louisiana for wrongful death resulting from the crash of petitioner’s helicopter off the Louisiana coast. Petitioner, Cessna Aircraft, answered, alleging that it was not amenable to process in Louisiana. In order to prevent the running of the statute of limitations in the event the Louisiana court lacked jurisdiction, plaintiffs then filed a similar suit in the Kansas federal district court which concededly had jurisdiction. However, before the Kansas suit proceeded to trial, the Louisiana court held that it possessed jurisdiction over Cessna, and plaintiffs moved

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the Kansas court for a transfer to the Louisiana court under 28 U.S.C. section 1404 (a).¹

The Kansas court granted the transfer, finding that both the convenience of parties and witnesses and the interests of justice required the change of venue. It held that the statutory requirement that a transfer be made only to a court where the action "might have been brought" was satisfied by the decision of the federal court in Louisiana that it had jurisdiction over Cessna. Cessna applied to the Court of Appeals for the Tenth Circuit for writ of mandamus to prevent the transfer. Held, writ granted: The transfer should be prevented to avoid complications which might result from an ultimate holding that Louisiana is without jurisdiction, and the Kansas proceeding must be stayed pending the termination of the litigation in Louisiana. Cessna Aircraft Co. v. Brown, 348 F.2d 689 (10th Cir. 1965).

The scope of review on petition for writ of mandamus to prevent a section 1404 (a) transfer is limited to the questions (1) whether the district court had power to make the transfer, i.e., whether the transferee district is one where the action might have been brought and (2) in some federal circuits, whether the district judge abused his discretion in allowing the transfer.² However, in the instant case, the court did not base its decision on either of the above grounds.

Ordinarily, a district is one where the action "might have been brought" if subject matter jurisdiction, venue, and service of process are proper there.³ The transferor court determines whether these requisites are satisfied, and the court of appeals for the transferor circuit should mandamus the lower court only if it finds that determination to be erroneous.⁴ Nevertheless, in the principle case, the court of appeals for the Tenth Circuit issued the writ to prevent the transfer even though it did not find error in the district judge's determination that the suit might have been brought in Louisiana. The court felt that the transfer should not be made in order to avoid complications which might result if the Fifth Circuit overruled the Louisiana district court on the jurisdictional issue. On first impression this would seem to be a clear usurpation of appellate authority in violation of section 1404 (a). That statute provides that "a district court may transfer . . ." if specified requisites are satisfied, and the

¹ 28 U.S.C. § 1404 (a) provides: "For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought."
² 1 Moore, Federal Practice § 0.145 [6.—1] (2d ed. 1962).
³ Id. § 0.147.
Tenth Circuit made no finding that the statutory requirements had not been met.

A significant factor in the principle case is that the Louisiana court had acquired jurisdiction of a similar action before the Kansas proceeding was instituted. The court of appeals, mindful of its duty to prevent multiple litigation, invoked the familiar rule of comity that "the first federal district court which contains jurisdiction of parties and issues should have priority, and the second court should decline consideration of the action until proceedings before the first court are terminated." By invoking this rule, the court assumed that it could properly prevent the transfer even though no finding was made that the district judge had wrongly applied the statutory criteria. But unless an appellate court should find within the limited scope of its review of a section 1404(a) transfer that the statutory requisites were not satisfied, it would seem that the transfer order should stand. A subsequent direction to stay the proceedings should have no effect on a transfer order which was properly granted under section 1404(a).

The court might have supported the writ on grounds that the district judge had abused his discretion by ordering a transfer in the face of a paramount duty to stay the proceedings in deference to the Louisiana litigation. Under such circumstances a transfer might not be "in the interest of justice." This rationale would have accomplished the court's purpose in a manner consistent with both precedent and statute.

But the court's opinion seems to indicate that mandamus is proper without regard to the propriety of the district judge's action under section 1404(a) if the writ is issued to promote "sound judicial administration." This proposition purports to enlarge the scope of review of federal transfer orders to an extent not contemplated by section 1404(a).

E.L.Y.

Insurance — Extended Coverage To Drivers Of Non-owned Vehicles

Appellee McCarty was struck and injured by a United States Air

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6 See note 1 supra.
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Force pickup truck driven by Mrs. Purser, a civilian. Mrs. Purser was accompanied by Lt. Col. Jewell, the officer to whom the truck had been assigned by the Air Force. An insurance policy on her own car extended coverage to her in a non-owned vehicle, providing she had the owner’s consent to drive it. Jewell, upon whose permission she relied, was forbidden by statute to authorize non-official use of the vehicle. McCarty obtained a judgment against Purser but her insurer refused to pay alleging that the truck was driven without the permission of its owner, the United States Government. The trial court entered judgment against the insurer, and it appealed. The issue in the court of civil appeals was whether Purser had the owner’s consent, within the meaning of the insurance policy, to drive the truck. Held, affirmed: A person driving a non-owned vehicle is covered by his own insurance policy when he reasonably believes that he has the consent of the owner to use the vehicle. American Surety Co. v. McCarty, 395 S.W.2d 665 (Tex. Civ. App. 1965).

The controlling question in the instant case was whether Mrs. Purser could rely on Jewell’s authority to allow her to drive the pickup. Jewell testified that the truck was assigned to him on a twenty-four hour basis. As an agent of the owner, Jewell presumably could freely authorize use of the truck. In fact, non-official use of the truck was prohibited by statute. However, Mrs. Purser was not charged with knowledge of the statute since it was directed to the conduct of official personnel. Mrs. Purser had no reason to question Jewell’s authority and had every right to believe that her own policy would extend its coverage to her as she drove the truck. If Mrs. Purser’s belief was reasonable, her insurance company could not assert a contrary position.

Two situations must be distinguished. If a negligent driver is seeking extended coverage from the owner’s policy, the critical determination is whether the driver in fact had the consent of the owner to drive the car. This permission may be express or implied, or given by an agent who has actual authority to do so. On the other hand, when the driver looks to his own insurance policy for extended coverage when he is operating a non-owned vehicle, the issue is whether the driver had a right to believe that he was using the vehicle with the owner’s consent.

A.D.S.

3 As the court indicates, the driver acts at his peril when he relies upon the owner’s policy for coverage. Id. at 667. Cf. Globe Indemnity Co. v. French, 382 S.W.2d 771 (Tex. Civ. App. 1964) error ref. n.r.e.
Non-negotiable Notes — Rules of Construction

Suit was brought by the payee for recovery on a ninety-day promissory note. Defendant had executed the note on a printed form provided by the payee. The amount of the obligation appeared in one place as the figure, $5,780, and in another place, written out as five thousand eighty dollars. In addition to the unconditional promise to pay printed on the form, the note contained a handwritten clause providing that the maker would make $1,000 overpayments on future deliveries until the obligation of the note was paid. In the trial court, the jury returned a verdict in favor of the plaintiff in the amount of $5,780. Held, reversed: Where there is a variance between the written words and the figures in a non-negotiable note, the written words control as a matter of law. Gutbrie v. National Homes Corp., 394 S.W.2d 494 (Tex. 1965).

The court found that the clause providing for overpayments on future deliveries burdened the note with conditions of an extrinsic agreement and rendered it non-negotiable. Thus the instrument under consideration was nothing more than a simple contract and should have been interpreted according to the rules of construction for contracts. The objective of the contract rules of construction is to determine and enforce the intent of the parties. In the instant case, the variance between the written words and the printed figures constituted a patent ambiguity. Such an ambiguity can be resolved by resort to parol evidence in an action for reformation. As Justice Griffin noted in the dissent, “Equity grants relief where, as a result of a mistake by the parties in an effort to reduce their agreement to writing, the subsequent contract does not express their real agreement. . . .”

The court in the instant case applied a rule of construction for negotiable instruments law, which is intended to aid the free flow of commercial paper. The rules of construction embodied in the Negotiable Instrument Act are designed to achieve this purpose by allowing construction of ambiguities on the face of negotiable instruments as a matter of law. The application of these rules of construction to non-negotiable paper is not justified by commercial necessity and is an

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1 394 S.W.2d 494, 495 (Tex. 1965).
2 Williston, Contracts § 600 (3d ed. 1961).
3 A patent ambiguity involves a lack of certainty that is apparent on the face of the instrument. See 23 Tex. Jur. 2d Evidence § 351 (1961).
4 394 S.W.2d 494, 498 (Tex. 1965).
5 Tex. Rev. Civ. Stat. Ann. art. 5932 § 17 (1962). The provisions of article 17 have been substantially incorporated into article 3-118 of the Uniform Commercial Code, enacted by the 59th legislature to become effective July 1, 1966.
injustice to the parties who should be permitted to enforce the written contract in accordance with their actual agreement.

J.D.T.

**Oil and Gas — Interest as Cost in Accounting to Non-consenting Cotenant.**

Davison and others, the respondents, owned 28/32 of a 13/16 working interest in a lease. Petitioners owned a 3/32 mineral interest in the same land. Respondents wished to drill for minerals, but petitioners refused to join in the proposed venture. Nevertheless, respondents drilled producing wells on the common property at their own expense. In accounting to the petitioners for their portion of the production, the respondents deducted as a development cost the interest on the non-consenting cotenants share of the drilling expenses. The trial court held that interest was a reasonable development cost, and the the court of appeals affirmed. Held, reversed: Interest charges are not a part of the reasonable costs of production and may not be recovered from a non-consenting cotenant. *Cox v. Davison*, 397 S.W.2d 200 (Tex. 1965).

A cotenant acting in good faith may develop the common property without having secured the consent of his cotenants, but if the minerals are produced the operating cotenant must make an accounting to the non-consenting and non-paying cotenants for their share of the production.¹ The operator is entitled to be reimbursed from the production for the non-joining cotenants' share of the reasonable and necessary cost of development, production, and marketing.² However, if a cotenant does not consent to the development of the mineral estate, his proportionate share of the financing charges is not a reasonable and necessary cost of development. The same is true whether the operating cotenant uses his own funds or pays interest on borrowed money.³

¹ See also, *Kuntz, Oil and Gas § 5.6, at 113 (1962); Masterson, A 1952 Survey of Basic Oil and Gas Law, 6 Sw. L.J. 1, 29 (1952).* At least three states do not permit a cotenant to produce common minerals without the consent of the other owners: Illinois, *Ziegler v. Brenneman*, 237 Ill. 15, 86 N.E. 597 (1908); Louisiana, *Gulf Refining Co. v. Carroll*, 145 La. 299, 82 So. 277 (1919); West Virginia, *Williamson v. Jones*, 43 W. Va. 562; 27 S.E. 411 (1897).

² The burden is upon the operating cotenant to prove the expense is reasonable and necessary. *Johnson v. Kansas Natural Gas Co.*, 90 Kan. 565, 135 P. 589 (1913). Once a cost is established, however, it may be difficult for the nonjoining cotenant to gather sufficient information to challenge the method of bookkeeping or the amount allegedly expended.

³ See also, *Cox v. Davison*, 397 S.W.2d at 202.
The majority of the court stated that interest was an incident of debt. Since the non-consenting cotenants' obligation to the operator was not in the nature of a debt, the court reasoned that interest could not be a reasonable cost. Justice Pope, dissenting, said that the issue was not whether a debt existed, but whether interest was a reasonable and necessary cost of development. Logically, interest paid on money borrowed to finance the development of common minerals is a cost of production, while an interest charge founded upon the use of a cotenant's own funds appears to be in the nature of a debt, at least when applied to a development of common minerals undertaken without the consent of the other cotenants.

J.B.H.

Taxation — Patent Transfer Under Section 1235 — Related Persons

The inventor of a bath oil formula sought to interest two business associates (taxpayers) in the formula which he had conceived but had not begun to develop. The proposal was accepted, and a one-third interest in the formula was transferred to each of the two taxpayers in consideration for their agreement to finance all of the development costs. Following successful development of the formula, the two taxpayers, in an arm's-length transaction, transferred their interests in the formula to a manufacturing partnership consisting of the inventor of the formula and the wives of the two taxpayers. The taxpayer-husbands and the inventor received a royalty on net sales in consideration for the transfer of their interest in the formula to the partnership. In 1958 the taxpayer-husbands each received payments of $19,484.33 pursuant to this arrangement. This amount was reported as a long-term capital gain under section 1235 of the Internal Revenue Code, which provides that a transfer of all substantial rights to a patent, or an undivided interest therein, by a holder to transferees other than related persons shall be treated as if it were a sale or exchange of a capital asset held for more than six months. The Commissioner assessed a deficiency, asserting that the transfer was between related persons, and that the royalty payments should

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4 397 S.W.2d at 204.

therefore be taxed as ordinary income. The Tax Court\(^5\) sustained the Commissioner and the taxpayers appealed. \textit{Held, affirmed:} A transfer of a patent between two partnerships, eighty per cent owned by the same or related interests, is a transfer between related persons and the consideration received for the transfer is ordinary income. \textit{Burde v. Commissioner, 352 F.2d 995 (2d Cir. 1965)}.

Section 1235(d)\(^4\) provides that capital gains treatment shall not apply to a transfer of a patent between persons specified in section 267(b).\(^4\) The congressional intent of 1235(d) was to prevent the conversion of ordinary income into capital gains by a transfer of a patent within essentially the same economic group.\(^6\) However, section 276(b) makes no mention of a partnership as a related person. To establish when a transfer to a partnership constitutes a transfer within the same economic group, the court looks to the "controlled partnership" provisions of section 707(b).\(^7\) Section 707 recognizes the partnership as a separate entity in transactions between a partner and the partnership except when a sale or exchange of property occurs between a partnership and a partner, or between two partnerships in which the same persons own directly or indirectly eighty per cent of the interest therein. As section 707(b) and section 1235(d) were both designed to prevent capital gains treatment between transfers within the same economic group, the court applied the eighty per cent test of section 707 to the instant transaction to determine whether a partnership is to be treated as an entity for purposes of the patent transfer. The court found that the original undertaking to develop the patent to commercial production by the inventor and the two taxpayer-husbands constituted a joint venture,\(^8\) and that the transfer to the partnership composed of the inventor and the wives therefore

\(^{5}\) 43 T.C. 252 (1964).
\(^{6}\) Related Persons.—Subsection (a) shall not apply to any transfer, directly or indirectly, between persons specified within any one of the paragraphs of section 267(b); except that, in applying section 267(b) and (c) for purposes of this section—
(1) the phrase "25 percent or more" shall be substituted for the phrase "more than 50 percent" each place it appears in section 267(b), and
(2) paragraph (4) of section 267(c) shall be treated as providing that the family of an individual shall include only his spouse, ancestors, and lineal descendants.
\(^{8}\) As to § 1235(d), see House Report, note 5 supra. As to § 707, see S. Rep. No. 1622, 83d Cong., 2d Sess. 94 (1954), U.S. Code Congressional and Administrative News, p. 4629.
\(^{8}\) Treas. Reg. § 1.761-1(a) states: The term "partnership" is broader in scope than the common law meaning . . . Mere co-ownership of property which is maintained, kept in repair, and leased does not constitute a partnership . . . Tenants in common, however, may be partners if they actively carry on a trade, business, financial operation, or venture and divide the profits thereof.
was a transfer between two partnerships eighty per cent owned by the same or related interests. By thus falling within the literal terms of section 707(b) (2) (B), the transferee partnership was held to be a related person pursuant to section 1235(d), and the royalty payments received in 1958 were, therefore, taxable as ordinary income.

Treating the partnership as an unrelated entity for purposes of section 1235 when it has filtered through the section 707 sieve can give rise to various tax benefits. If the holding of the instant case is to be consistently applied, the partnership form offers many advantages over the corporate form when transferring a patent to an entity in which the transferor has an interest. Section 1235(d) disqualifies transfers of patents to corporations from capital gains treatment when twenty-five per cent or more of the corporation is owned by the transferor. At the same time, if the transfer is to a partnership, the transferor may own as much as seventy-nine per cent of the transferee before losing the tax benefit. As apparently no good purpose of tax policy is served by permitting capital gains treatment for a patent transferred to a partnership when less than eighty per cent is owned by the transferor when the same transfer to a corporation owned to the extent of twenty-five per cent or more by the transferee will be subject to ordinary income treatment, remedial legislation would seem warranted.

C.W.M.

Taxation — Reorganizations — No Tax Avoidance Purpose

In 1958 Wilson’s Furniture, Inc. spun-off a corporation which was called Wil-Plan. In the transaction Wil-Plan received an automobile and a number of conditional sales contracts that had been previously obtained by Wilson’s, Inc. through the sale of furniture on deferred payment plans. All of the stock in Wil-Plan was distributed to the two taxpayers, the owners of Wilson’s, Inc. At the time of the transfer Wilson’s, Inc. had accumulated earnings and profits of $48,889.98. The Wil-Plan stock had a fair market value of $69,020.07. The two taxpayers did not include any income attributable to the Wil-Plan stock in their tax returns for 1958 on the ground

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*See note 3 *supra.*
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that the spin-off was non-taxable under section 355. The Commissioner of Internal Revenue asserted a deficiency of $11,000 against each of them. The Tax Court found that while there was no valid business purpose for the spin-off, there also was no tax avoidance purpose, and held for the taxpayers. The Commissioner appealed. Held, reversed: A valid business purpose is required for a tax free spin-off under section 355. The lack of a tax avoidance motive will not protect the transfer. Commissioner v. Wilson, 355 F.2d 184 (9th Cir. 1965).

Section 355 contains a prohibition against using spin-offs as a "device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation." Usually when a corporation distributes assets to its stockholders or sells assets and distributes the proceeds, a dividend results, and the stockholders must pay tax at ordinary income rates. However, if the corporation is permitted to transfer the assets to a new corporation and distribute the new company's shares to its (the old company's) stockholders in a tax-free spin-off, the stockholders could either liquidate the new corporation or sell its stock, thereby realizing capital gains. Section 355 is intended to prevent this. In addition to the specific requirements of section 355, the test provided by Gregory v. Helvering must be met. The Gregory case is often cited as requiring "a valid business purpose" to support the reorganization. In reaching the Gregory decision the Supreme Court also found the existence of a tax avoidance motive. From this it is possible to infer a dual test for finding a transaction invalid—the absence of a valid business purpose plus the presence of a tax avoidance motive.

In Wilson the court was "confronted with what may be a unique situation, that of a corporation reorganization which had no business reason and which had no tax avoidance purpose . . . ." The court concluded that the nonexistence of a tax avoidance motive is not controlling. It stated that "so much in the way of liability for taxes can hardly be allowed to depend solely upon what goes on in someone's mind." This decision clearly indicates that the requirement of a valid business purpose, created by Gregory v. Helvering, must be strictly applied.

J.M.W.

2 Maine S. Wilson, 42 T.C. 914 (1964).
5 Commissioner v. Wilson, 353 F.2d 184, 187 (9th Cir. 1965).
6 Ibid.
Wills — Probate Proceedings — Attorney’s Fees

Raymond Salmon, the principal beneficiary and an executor of the will of Maria Hoben, employed attorneys on a contingent fee basis to defend the will and to seek its admission to probate. Two sisters, who had been pretermitted from the will of the testatrix, contested probate on the ground that all of the beneficiaries had renounced their rights under the will in a family settlement. After two trials and an appeal, the will was admitted to probate. The attorneys hired by Raymond filed a claim for $25,000, which was allowed by the executors and approved by the county court. On appeal to the district court, a jury found that $19,200 was a reasonable fee, and a judgment was entered on the verdict ordering payment of that amount. The court of civil appeals required a remittitur of $2,200, and affirmed the judgment of the trial court as reformed. Held, reversed: Attorney’s fees allowed by section 243 of the Probate Code cannot be contingent upon the outcome of the litigation but must be for a reasonable fee certain. Salmon v. Salmon, 395 S.W.2d 29 (Tex. 1965).

Section 243 authorizes a person named in the will as executor to employ attorneys to defend the will and to prosecute actions for the purpose of having the will admitted to probate. Prior to the enactment of this section, there was no statutory authority for the payment of attorney’s fees out of an estate. The Texas courts, however, had allowed reasonable fees when the executors, acting in good faith, employed attorneys to seek admission of wills to probate. In these cases, the fees allowed were classified as expenses of administration, and were allowed whether the litigation was successful or not. The question of whether these fees could be contingent, however, had never been answered. The instant case clearly answers this question in the negative. The amount of attorney’s fees to be allowed in probate proceedings is to be determined by the reasonable value of the services rendered and not by what might be reasonable should the litigation prove successful.

D.E.W

When any person designated as executor in a will, or as administrator with the will annexed, defends it or prosecutes any proceeding in good faith, and with just cause, for the purpose of having the will admitted to probate, whether successful or not, he shall be allowed out of the estate his necessary expenses and disbursements, including reasonable attorney’s fees, in such proceedings.


3 Lang v. Shell Petroleum Corp., 138 Tex. 399, 159 S.W.2d 478 (1942).