Recent Cases

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ADVERSE POSSESSION BY HUSBAND AND WIFE—SEPARATE TITLE IN HUSBAND, TENANCY IN COMMON OR TENANCY BY ENTIRETIES?

Preston v. Smith[1]

A husband and wife occupied land jointly, without color of title, for over 40 years beginning in 1910. The husband died in 1950 and the wife continued in possession until her death four years later. Then the collateral heirs of each spouse claimed the farm. The heirs of the wife contended there had been a tenancy by the entirety by which she succeeded to the whole by survivorship, while the heirs of the husband claimed that he had gained an exclusive title by his possession. The court accepted the Chancellor's finding of fact that the possession was adverse and also his finding that the evidence indicated that the intention of the couple was that the adverse possession inure to their joint benefit. The Chancellor ruled that this was a joint adverse possession by which the spouses acquired a prescriptive title to the land as tenants in common and that the heirs of each were entitled to a one-half undivided interest. The decree was affirmed in an opinion by the Court of Appeals of Tennessee, and on certiorari affirmed without additional opinion by the supreme court of that state.

The case presents two principal problems, although the first is so well settled that it is of little more than academic interest. They are: (1) whether a husband and wife can acquire a title by joint adverse possession, and (2) if so, what type estate will be created.

First, at common law it is well settled that title by adverse possession could be acquired by a married woman, when she was either living separate from her husband, or when she occupied jointly with him under color of title in her own right,[2] or under a parol gift to her.[3] Also it has been held that the presumption that the joint occupancy of husband and wife is the possession of the husband may be rebutted by showing the wife took possession in her own right.[4] But, some cases have held that a married woman, not living separate and apart from her husband,

1. 293 S.W.2d 51 (Tenn. App. 1956).
2. Potter v. Adams, 125 Mo. 118, 28 S.W. 490 (1894); Poindexter v. Rawlings, 106 Tenn. 97, 59 S.W. 766 (1900); Ramsey v. Quillen, 5 Lea (73 Tenn.) 184 (1880).
3. Clark v. Gilbert, 39 Conn. 94 (1872).
4. Collins v. Lynch, 157 Pa. 246, 27 Atl. 721 (1893).

and having no claim in her own right to land, could not acquire title to it as her separate estate by adverse possession.[5]

The court in the principal case, conceding the point that at common law a married woman could not commit a separate act of disseisin, held that this would not prevent her and her husband from committing such an act jointly, for their joint and separate benefits. This view was based upon the fact that even at common law it was possible for a husband and wife to jointly possess land, either as tenants by the entirety or as tenants in common. Thus it was held the possession was not necessarily the possession of the husband alone. The court further supports this point by holding that the law at the time the adverse possession was perfected was controlling rather than the law in existence at the time the possession began in 1910. The Married Woman's Emancipation Act, passed in 1913, removed all disability because of coverture upon a woman's right to acquire or dispose of property.[6] It would seem that today, under the generally adopted Married Women's Acts, there should no longer be any question on the point that a husband and wife may hold property together in joint adverse possession.[7]

The second problem presented by this case is what estate will be created by such joint adverse possession of a husband and wife. The principal case held that a tenancy in common was created. It is submitted that this conclusion, while perhaps justified under a policy of strictly limiting the extent of the anachronistic tenancy by the entirety, is not reached by a sound process of logical reasoning. The main basis stated for the court's conclusion is that no authority could be found to the effect that an estate by the entirety may arise out of adverse possession; and that because all of the various text authorities state that the four unities of interest, time, title and possession must be present, arising from the same conveyancy, the estate must originate in a grant or devise and not in adverse possession.

But under the most hoary common law, these four unities may be present in a title gained by adverse possession.[8] It is well settled that joint disseisors will become joint tenants unless circumstances indicate an intention to hold as tenants in common.[9] In *American Law of Property* it is said that the usual statutory presumption for a tenancy in common is not in terms applicable to a joint title gained by adverse possession.[10] And then it states that a joint tenancy may be created

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5. Madden v. Hall, 21 Cal. App. 541, 132 Pac. 291 (1913); Marr's Heirs v. Gilliam, 41 Tenn. 488 (1859).
6. TENN. CODE ANN. § 36.601 (Williams § 8460) (1956).
7. Humphreys v. Gribble, 227 S.W.2d 235 (Tex. Civ. App. 1950); King v. Fasching, 234 S.W.2d 549 (Mo. 1950).
8. 2 AMERICAN LAW OF PROPERTY § 6.1 (1952).
9. Coke, Litt. *181a; Putney v. Dresser, 43 Mass. (2 Metc.) 583 (1841); Kauhikoa v. Hoboron, 5 Hawaii 491 (1855); Ward v. Ward, 6 Ch. App. 789 (1871); Smith v. Savage, 1 Ir. R. 469 (1905).
10. 2 AMERICAN LAW OF PROPERTY § 6.1, p. 5, n. 12 (1952); MO. REV. STAT. § 442.450 (1949) reads ". . . every interest . . . granted or devised . . ."

only by purchase, that is, by deed, will or adverse possession. This text authority also states that the statutory presumption favoring tenancy in common is generally not applicable to a conveyance to a husband and wife, and that the presumption remains in favor of creation of a tenancy by the entirety, in such a case[11] although today, if the intention of the parties so indicates, a husband and wife may take as tenants in common or even as joint tenants.[12]

The existence of a tenancy by the entirety is said in another Tennessee case to be a question purely of intention, though in the absence of an expression of a contrary intent an intention on the part of the grantor to create such an estate is presumed.[13]

The presumption applied to an instrument conveying to a husband and wife favoring creation of a tenancy by the entirety should likewise apply to a title acquired by joint adverse possession of the couple. The original basis of the rule, the idea that in law a husband and wife are one person and therefore there could be no moieties between them, should apply equally to a title under a grant or devise or to a prescriptive title. Similarly, the modern tendency to treat the presumption as a rule of construction to reach the intention of the grantor should apply with equal force to reach the intention of the husband and wife acquiring an adverse title.

So, considering that the requisite four unities may be present when two persons hold in joint adverse possession, and that the presumption is for creation of a tenancy by the entirety when title is gained by a husband and wife absent a contrary intent, it would seem that logic would have required the conclusion that a tenancy by the entirety was created in the principal case. However, the court notes that in the past courts have made strict application of the rules with respect to creation of estates by the entirety. And, in view of the strong criticism which has often been directed against this type estate and the fact that it has been abolished in almost half of the American jurisdictions, the restricted application may well be justified as a matter of policy.

It should be noted that there was no color of title in the principal case. The type of problem arising most commonly today would likely be where the husband and wife held under a defective instrument and perfected title by adverse possession. The intent with which they held, the character of their holding would likely be indicated by that instrument and the intent so indicated could be the basis for a tenancy by the entirety, a tenancy in common or an estate in severalty.

RICHARD J. SHIPLEY

11. 2 AMERICAN LAW OF PROPERTY § 6.3 (1952).
12. *Ibid.* § 6.6.
13. Bost v. Johnson, 175 Tenn. 232, 133 S.W.2d 491 (1939).

DIVORCE—AWARD FOR SUPPORT OF CHILD—CREDIT FOR PAYMENT

Steckler v. Steckler[1]

Respondent, husband, brought an action for divorce against his wife. The divorce was granted, and the wife was awarded custody of their 15 year old daughter and the sum of $40.00 per month for the daughter's support and maintenance. The respondent paid all of the support money to the wife for three or four months. The daughter allegedly complained to respondent that she was not getting any money or support from her mother, and without further investigation the respondent paid part of the money directly to the daughter and paid the remainder to the wife. He later ceased to make any payments to the wife, but he had receipts to evidence payments to the child.

The wife sought execution on the judgment for arrearages due under the decree, the child having married and the liability of the father having terminated as to any further payments. Respondent moved for an order to quash execution and claimed credit on the judgment for amounts paid directly to the child. The Circuit Court of Pemiscot County entered judgment in favor of respondent, and the wife appealed. The court of appeals held that where there was no evidence that the wife abandoned or cast out her daughter, or failed to support her, payments made by the husband directly to the daughter, as a volunteer, without knowledge of the wife, could not be claimed by the husband as a credit against execution issued on the judgment for support and maintenance. The judgment was reversed with directions to quash execution only as to amounts proved paid to the wife.

An examination of cases allowing or denying credit against the judgment or decree for expenditures or payments made by the father other than in accordance with the decree for support and maintenance discloses the following results:

Where the father has supplied support in kind the courts will usually allow credit. Thus, where the mother is awarded custody of the children and then permits them to live with and be supported by the father, credit is usually allowed.[2]

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1. 293 S.W.2d 129 (Mo. App. 1956).

2. Waldron v. Waldron, 138 Ga. 788, 76 S.E. 348 (1912); Schlom v. Schlom, 149 Miss. 111, 115 So. 197 (1928) (husband resumed custody at wife's request); Link v. Link, 262 S.W.2d 318 (Mo. App. 1953) (husband and wife lived together and he provided support although the parties were not remarried); Olbert v. Key, 93 S.W.2d 1048 (Mo. App. 1936) (While this case did not involve a decree, where the husband had given the wife a promissory note in consideration of her agreement to support and care for the children and she later returned the children to the husband and he provided their support, the husband was allowed to raise the defense of failure of consideration in the wife's suit on the note.); Ostrin v. Posner 127 Misc. 313, 215 N.Y. Supp. 259 (Sup. Ct. 1925) (oral agreement by wife to renounce payments if husband would resume custody); Chapman v. Chapman, 177 Ore. 239, 161 P.2d 917 (1945); Mason v. Mason, 148 Ore. 34, 34 P.2d 328 (1934) (abandonment by mother); State *ex rel.* Meins v. Superior Ct., 159 Wash. 277, 292

Where such custody is only temporary, such as a visit during the summer months, etc., credit is denied unless the decree provides for reduction of support payments in such an instance.[3] Where such custody is without the mother's permission or consent no credit is allowed.[4]

The cases allowing credit for money paid to third persons for support furnished to the children are chiefly cases involving payments for expenses of education while the child is away from home attending college.[5] Money expended by the father in ordering and paying for goods, merchandise, food, etc., for the children while they are living at home with the mother is usually not considered for credit since the courts feel that this would allow the father to dictate to the

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Pac. 1011 (1930) (wife and children returned to live with husband); Gainsburg v. Gabarsky, 157 Wash. 537, 289 Pac. 1000 (1930).

For cases holding contra, see: Anderson v. Anderson, 110 Utah 300, 172 P.2d 132 (1946); Creadon v. Krogh, 75 Ga. App. 675, 44 S.E.2d 136 (1947); Sampognaro v. Sampognaro, 222 La. 597, 63 So.2d 11 (1953) (where the wife was awarded custody of the children and they had been turned over to her in open court, the children voluntarily remained with the husband for three and one-half years; she making no attempt to enforce the custody provisions. The court modified the custody provisions of the decree upon the application of the husband but held that he was still liable to pay full alimony up to the date he applied for the modification, saying that such a decree remains in full force and effect until the aggrieved party applies to the court for modification. However, the question of credit on the decree for support furnished in kind was not specifically mentioned and it may be that no claim was advanced on this theory.)

3. Brummer v. Brummer, 6 N.J. Super. 401, 69 A.2d 38 (1949) (no relief in the absence of a provision in the decree, since the mother must still maintain a home for them to return to); Bradley v. Fowler, 192 P.2d 969, 2 A.L.R.2d 822 (Wash. 1948); Hyde v. Hyde, 143 Kan. 660, 56 P.2d 437 (1936). *Contra*: Testut v. Testut, 34 N.J. Super. 95, 11 A. 2d 513 (1940).

4. McCourtney v. McCourtney, 205 Ark. 111, 168 S.W.2d 200 (1943). This is in accord with the cases involving suits upon the father's common law duty and obligation to support the children. See Nelson v. Nelson, 146 Ark. 363, 225 S.W. 619 (1920), where it was held that the mother could not recover expenses of maintenance and support where she kept the children without the father's consent, the custody of the children having been awarded to him. To the same effect is Wills v. Baker, 240 Mo. App. 705, 214 S.W.2d 748 (1948). But *contra* where father permitted the mother to take the children. See Dolvin v. Schimmel, 284 S.W. 811 (Mo. App. 1926).

5. Briggs v. Briggs, 178 Ore. 193, 165 P.2d 772, 166 A.L.R. 666 (1946); Mooty v. Mooty, 131 Fla. 151, 179 So. 155 (1938) (The court commented that since the wife's expenses at home were reduced by the child's absence, the payments were in substantial compliance with the decree.); Rufner v. Rufner, 131 N.J. Eq. 193, 24 A.2d 180 (1942) (Such payments were held to be a matter of practical administration); Schlom v. Schlom, *supra* note 2 (payment at mother's request). *Contra*: Hyde v. Hyde, *supra* note 3; Moore v. Mackay, 132 N.Y.S. 2d 813 (Sup. Ct. 1954).

mother how the support money will be spent.[6] Other courts have dismissed such claims for credit by saying that a decree for support and maintenance is a judgment for the payment of money and can be satisfied only by the payment of money, unless the holder of the judgment expressly agrees to accept something else.[7]

Some cases have arisen where the father has paid out money in excess of the amount required by the decree during one period of time and then later claims credit for such excess against future payments required by the decree. In such cases credit is usually denied whether the excess was paid to the mother[8] or to some third person for support furnished to the child.[9]

In cases involving payment directly to the child, such as the case here noted, credit is usually allowed where such payments are with the consent of the mother,[10] or where the mother actually receives the money.[11] Also in the cases involving education of the child, while consent is usually present, some courts have allowed credit for such payments directly to the child in the absence of such consent.[12] Aside from these exceptions, however, the courts have usually denied credit for direct payments without the mother's consent,[13] even where it was alleged that the mother was not providing a home and proper support for the child.[14]

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6. Cotton v. Wright, 193 La. 520, 190 So. 665 (1939). However, Foote v. Foote, 68 Atl. 467 (N.J. 1908) allowed credit where the husband paid for board of the wife and children by "having it allowed in a suit brought against him." One point of distinction which may be made between the two cases is that in the Foote case the wife probably contracted for the board and thus the husband by paying for it is not dictating to the wife how it shall be spent as in the case where he orders the merchandise himself.

7. Roberts v. Roberts, 216 Ark. 453, 226 S.W.2d 579 (1950); Williams v. West, 258 S.W.2d 468 (Ky. App. 1953).

8. Hinton v. Hinton, 211 Ark. 159, 199 S.W.2d 591 (1947) (Husband's military allotment was in excess of the required sum and such excesses were sufficient to pay all arrearages from date of discharge to time of trial. The court refused to grant credit for any of the excess toward amounts accrued after date of discharge and cessation of payments.); Loomis v. Loomis, 221 Ark. 743, 255 S.W.2d 671 (1953) (similar facts and result).

In regard to military allotments, one court has refused to credit the husband with the share of the allotment contributed by the government as being payment of amount required by the decree, even as against current payments. Kipping v. Kipping, 209 S.W.2d 27 (Tenn. 1948). However, Brooks v. Brooks, 204 Ga. 412, 49 S.E.2d 881 (1948) reached the opposite result.

9. Briggs v. Briggs, *supra* note 5 (money paid to children and college for educational expenses).

10. Briggs v. Briggs, *supra* note 5; Schlom v. Schlom, *supra* note 2.

11. Cotton v. Wright, *supra* note 6.

12. Jackson v. Jackson, 306 Ky. 715, 209 S.W.2d 79 (1948); Brill v. Brill, 143 App. Div. 63, 131 N.Y. Supp. 1030 (1st Dep't. 1911) (where husband withheld $2.00 per week of $20.00 per week support money and gave it to son for lunches and carfare so that the son could continue in school); Rufner v. Rufner, *supra* note 5.

13. Openshaw v. Openshaw, 86 Utah 229, 42 P.2d 191 (1935); Fischer v. Fischer, 164 Ga. 81, 137 S.E. 821 (1927); Fussell v. State, 102 Neb. 117, 166 N.W. 197 (1918).

14. Campbell v. Campbell, 223 Ky. 836, 4 S.W.2d 1112 (1928).

The decision of the court denying credit in the instant case is sound. The Missouri Supreme Court has said, "Divorce is a statutory action, but the courts generally follow the rules of equity and apply equitable principles in determining the rights and liabilities of the parties."[15] If the father has expended money under such circumstances that it is inequitable to force him to pay a second time, the court should allow credit for such payments. However, the father should not be allowed to ignore the decree of the court and undertake to decide when, where, and how such money shall be paid, as he undertook to do in this case, especially when he has a ready remedy by application to the court for modification of the decree. The practical results of allowing such conduct are aptly pointed out in the opinion of the court.

DWIGHT L. LARISON

EVIDENCE—PRODUCTION OF GOVERNMENT RECORDS

In re *Appeal of SEC* ex rel. *Timbers*[1]

A stockholders' derivative suit and a personal action was brought against the officers of Monroe Paper Products Company for an alleged breach of their fiduciary duties and misuses of corporate funds and facilities. It appeared that the SEC had been investigating the company prior to the filing of the suit. The plaintiffs subpoenaed the Commission records dealing with the case. The commission representatives declined to produce the files, relying on SEC Rule 122:

> Information or documents obtained by officers or employees of the Commission in the course of any examination or investigation . . . shall, unless made a matter of public record, be deemed confidential. Officers and employees are hereby prohibited from making such confidential information or documents available to anyone other than a member, officer, or employee of the Commission, unless the Commission authorized the disclosure of such information or the production of such documents as not being contrary to the public interest. Any officer or employee who is served with a subpoena requiring the disclosure of such information or the production of such documents shall appear in court and unless the authorization described in the preceding sentence shall have been given, shall respectfully decline to disclose the information or produce the documents called for, basing his refusal upon this rule. Any officer or employee who is served with such subpoena shall promptly advise the

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15. Franklin v. Franklin, 283 S.W.2d 483 (Mo. 1955).

1. 226 F.2d 501 (6th Cir. 1955).

Commission of the service of such subpoena, the nature of the information or documents sought, and any circumstances which may bear upon the desirability of making available such information or documents.

The trial court adjudged the SEC witness to be in contempt of court. The appellate court reversed this finding and discharged the witness from custody.

This case represents a narrow aspect of a much broader problem, namely the question of how far the privilege of excluding government secrets as evidence should be carried. Conflicting interests are involved. On one side is the interest of the litigant in having access to documents and other information in the hands of the government. On the other hand, there is a public interest in continuing unrestrained communications between government officials, a public interest in complete and accurate filing of compulsory reports, and the public interest in the executive control of executive records. It is thought that removal of the privilege of non disclosure of government secrets would handicap the government in these matters.

At common law the privilege of refusing to disclose government records was limited to those records constituting military and diplomatic secrets of state. This rule has been followed consistently in American jurisdictions.[2] There is little conflict in this phase of the problem inasmuch as there is general agreement that the interests of the nation as a whole must be superior to those of the individual. The privilege of nondisclosure has been extended to cases in which the identity of an informer or the contents of his message are at issue. The reason for this extension of the doctrine is that it is thought that any other rule would operate as a detriment to effective law enforcement.[3]

There is greater division of opinion when a situation similar to that presented in the principal case arises. In this type of action, the government is not a party. Here it is private litigants who are trying to obtain the government records. However, when the litigants attempt to get this information, they are usually faced with a refusal by the government to produce the requested information. This refusal is based on a federal statute that provides that "the head of each department is authorized to prescribe regulations, not inconsistent with law, for the government of his department, the conduct of its officers and clerks, the distribution and performance of its business, and the custody, use, and preservations of the records, papers, and property appertaining to it."[4] On the basis of this

2. U.S. v. Reynolds, 345 U.S. 1 (1953); Totten v. U.S., 92 U.S. 105 (1875); Firth Sterling Steel Co. v. Bethlehem Steel Co., 199 Fed. 353 (E.D. Pa. 1912).

3. *In re* Quarles and Butler, 158 U.S. 532 (1894); Vogel v. Gruaz, 110 U.S. 311 (1884). There is often a controversy as to whether this privilege should be limited to nondisclosure of identity as to the informer. However, there are situations in which revealing the contents of the communication would amount to naming the informer.

4. 5 U.S.C.A. § 222.

statute most departmental heads have issued regulations instructing their subordinates to decline to produce these records when served with a subpoena.

The government has been successful in maintaining its privilege of nondisclosure of government records in this type of case. *Boske v. Comingore*[5] is the leading case in this area of the law and seems to be controlling law on the question. In that case a state court had held a United States Collector of Internal Revenue to be in contempt for refusal to file certain tax reports in his custody with a state agency. The collector had based his refusal to do so upon regulations similar to those involved in the present case. The federal courts held that the state court had no power to hold the subordinate in contempt.[6] The courts have cited *Boske v. Comingore* as controlling when presented with similar cases.[7]

This view recently was reaffirmed by the United States Supreme Court in *United States* ex rel. *Touhy v. Ragen.*[8] In that case, Roger Touhy, a prisoner in the Illinois State Penitentiary, instituted a habeas corpus proceeding against the warden of the penitentiary. In the course of the action a subpoena duces tecum was served upon a special agent of the Federal Bureau of Investigation ordering him to produce certain records and documents in his possession. The agent, relying on Justice Department rules similar to those in the present case, declined to produce the documents whereupon the trial court adjudged him to be in contempt of court. This decision was reversed by the court of appeals. The Supreme Court agreed, holding that the Justice Department regulation restricting disclosure was valid, and that, therefore, McSwain (the agent) had properly withheld the documents demanded by the subpoena.

It should be noted, however, that these cases only support the theory that a subordinate federal official, acting under agency or departmental regulations may refuse to produce these subpoenaed records in litigation between private parties. The courts have not determined the question as to whether the departmental head can be served with a subpoena. In the *Touhy* case, Justice Frankfurter in a concurring opinion indicated that the agency and departmental heads could be compelled to produce such information. As a practical matter, it is doubtful if such action would be successful. There would be obstacles in the way of the litigant resulting from territorial jurisdiction.[9]

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5. 177 U.S. 459 (1900).
6. *In re* Hirsch, 74 Fed. 928 (C.C. 1896) is the only major case contrary to this holding. Although the courts have never specifically overruled the case, it would seem that it is not controlling in view of Boske v. Comingore, *supra* note 5.
7. Harwood v. McMurty, 22 F. Supp. 572 (D.C. Ky. 1938); *Ex parte* Sackett, 74 F.2d 922 (9th Cir. 1935); *In re* Valecia Condensed Milk Co., 240 Fed. 310 (7th Cir. 1917); Stegall v. Thurman, 175 Fed. 813 (D.C. Ga. 1910); *In re* Lamberton, 124 Fed. 446 (D.C. Ark. 1903); *In re* Weeks, 82 Fed. 729 (D.C. Vt. 1897); *In re* Huttman, 70 Fed. 699 (D.C. Kan. 1895).
8. 340 U.S. 462 (1951).
9. FED. R. CIV. P. 45(e) provides that a trial subpoena may be served "at any place within the district or at any place without the district that is within 100 miles of the hearing or trial specified on the supboena."

The situation changes when the government is one of the litigants. The government is generally held to have waived the nondisclosure privilege when it brings suit.[10] Where suit is brought against the government, it has been held that the privilege is waived in regard to routine records. It is not likely that courts would hold the waiver to extend to military and diplomatic secrets in view of the fact that the collective importance of the latter secrets are likely to be greater than the interest of the individual litigant.

At this stage the law relating to a privilege of nondisclosure in regard to government records must be regarded as unsettled as to the scope of application with a probable tendency to enlarge the scope of the privilege.

ELDEN R. STERNBERG

FEDERAL TAXATION—DEDUCTION OF INSURANCE PREMIUMS AS NON-BUSINESS EXPENSES

U.S. v. John S. Mellinger[1]

In 1928 Mary Edith Giles made a loan in the amount of $25,000.00 to one Edwin Larendon. As collateral Larendon assigned to the taxpayer ten separate policies of ordinary life insurance, each in the amount of $5,000.00. The loan was later liquidated, but the policies were not reassigned. Shortly thereafter Larendon borrowed $4,000.00 from Miss Giles. A note for that amount was executed; Larendon gave second liens upon several pieces of real estate to secure this indebtedness, and there was an understanding that the life insurance policies would likewise stand as security for this loan. By the date of maturity of the $4,000.00 loan, Larendon had become a victim of the depression, was insolvent and unable to pay any part of the principal or interest. Foreclosure under prior mortgages rendered the taxpayer's second liens valueless. The only source from which any recovery could be realized was the life insurance. At the time that the policies were pledged, Larendon had borrowed the maximum permissible amount against them. As the cash surrender value was the same as the loan value, these policies did not have any present cash value over and above the amount of the loan. In 1933 five of the policies were returned to Larendon, the remaining five being retained as collateral. Thereafter, until Larendon's death in 1952, the

10. U.S. v. Andolschek, 142 F.2d 503 (2d Cir. 1944).

1. 228 F.2d 688 (5th Cir. 1956).

et al.: Recent Cases

taxpayer paid the annual premiums on the policies and the interest on the policy loans. During the period 1942 to 1948, it was necessary for the taxpayer to make cash payments of between $1400.00 and $1700.00 a year to keep the policies in force. Such payments were made by the taxpayer without any reasonable expectation that Larendon would repay them, and for the sole purpose of keeping alive the collateral, with the hope that, on the debtor's death, the insurance proceeds would be sufficient to repay the total outlay. In 1938, a point was reached when, even in the event of Larendon's death, it would not be possible to recoup the entire outlay from the collateral. From that time on the proceeds of the policy minus the amount of the policy loans, were less than the combined Larendon loan and the expense which had been necessary to keep the policy in effect. The taxpayer deducted as bad debts the amounts which she paid out in keeping the insurance in effect. These deductions were disallowed by the Commissioner, and deficiencies assessed and paid. A refund claim was filed, and though disallowed by the Commissioner, was upheld in the District Court, which found the expenditures deductible as non-business expenses under Int. Rev. Code of 1939, Section 23(a) (1) (A) (2) as amended by Section 121(a), Revenue Act of 1942, 56 Stat. 798. Appeal was taken to the Circuit Court of Appeals for the Fifth Circuit, where Tuttle, Circuit Judge, stated the problem to be this:

> We have here presented the question whether premiums paid by the taxpayer on life insurance policies on the life of her debtor, which she held as collateral for a debt which had become worthless many years prior to the payments, are deductible as non-business expense deductions under Section 23 (a) (2) of the Internal Revenue Code of 1939 . . . . .

The court found the questioned expenditures not deductible as non-business expenses under the cited section.

Section 23 (a) (2) under the provisions of which the taxpayer claimed his expenditures to be deductible provides that in computing net income there shall be allowed as deductions: "Non-trade or non-business expenses. In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the managment, conservation, or maintenance of property held for the production of income . . . ." This section was enacted in 1942 on the recommendation of the Treasury Department in order to remedy the specifically defined inequitable situation which arose in *Higgins v. The Commissioner*,[2] of an individual being taxed on investment income but being denied the right to deduct the cost of producing that income.

Taking notice of the "legislative grace" concept, which is to the effect that there can be no deductions unless such deductions are expressly authorized by the Congress,[3] the court found that the language of the section could justifiably be applied only to the restricted purpose for which it was enacted.

2. 312 U.S. 212 (1941).
3. McDonald v. Commissioner, 323 U.S. 57 (1944).

The taxpayer, however, attempted to show that subsequent regulations and decisions had broadened the scope of the allowable deductions under 23 (a)(2). As a first step the taxpayer showed that Regulation 111, Section 29.23 (a)-15[4] equates the term "expenses" as used in Section 23 (a)(2) to the term as used in Section 23 (a) (1) which covers the deduction of business expenses. The second step was to cite *First National Bank of Tulsa v. Jones*[5] which held that premium payments by a bank under somewhat similar circumstances were deductible as ordinary and necessary business expense[6] under Section 23 (a) (1). From this the taxpayer concluded that similar premium payments should also be considered "ordinary and necessary" non-business expenses under Section 23(a) (2).

The government sought to distinguish the *First National Bank* case as applicable only to the "business expense" situation. The court did not deal directly with that contention, stating,

> . . . . . We are convinced that such an expenditure is not an expense under the applicable section.

Lykes v. U.S.[7] is cited to support this assertion. The *Lykes* case emphasizes that in order to have a non-business expense deductible under Section 23(a) (2) it is not only imperative that the expenditure be an "ordinary and necessary" one, but also that the expenditure have been for "the production or collection of income . . . . ."

It was not necessary for the court in the *First National* case to find that the expenditures there dealt with met the further requirements above cited. Thus that court's finding of "ordinary and necessary" expenditures can have little influence in these non-business deduction cases.

All of the premium payments here involved were made at a time when the debtor was hopelessly insolvent, when there was no possibility that the taxpayer could ever recover an amount which would repay both the debt and the premiums already paid by the taxpayer. Since by definition "income" presupposes a gain to the taxpayer,[8] it is difficult to see how these expenditures could have been "for the production or collection of income." As the court points out, such expenditures were in effect an investment by the taxpayer in a speculative contract, no different than those payments made by any owner of a life insurance policy.

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4. Bowers v. Lumpkin, 140 F.2d 927 (4th Cir. 1944), *reversing* Lumpkin v. Bowers, 50 F. Sup. 874 (E.D. S.C. 1943), *Certiorari denied* 322 U.S. 755 (1944).
5. 143 F.2d 652 (10th Cir. 1944).
6. Welch v. Helvering, 290 U.S. 111 (1933), *affirming* 63 F.2d 976 (8th Cir. 1933).
7. 343 U.S. 118 (1951).
8. Eisner v. Macomber, 252 U.S. 189 (1920); Goodrich v. Edwards, 255 U.S. 527 (1920); Central R.R. v. Commissioner, 79 F.2d 697, 101 A.L.R. 1448 (3d Cir. 1935).

To reinforce its conclusion that the premium payments were not connected with the production or collection of income, within the narrowly defined limits of Section 23 (a) (2), the court decides that the premium payments were more in the nature of capital expenditures, which are not deductible. These annual premium payments, under actuarial rules, provided the proceeds that became due on the insured's death. Each payment made by the taxpayer contributed to the capital amount that would ultimately be recoverable. The expense of the premium was then directly related to the preservation of the collateral security for the payment of the debt, and the security, on the debtor's death, would be applied to the discharge of the debt.[9]

In the *First National* case the court determined that premium payments in a situation similar to this case were not capital expenditures but rather were deductible business expenses. However, the line between what is capital and what expense is not sharply drawn, and the fact finder may place similar items on either side of the line, if the particular accounting practice of the taxpayer justifies such treatment.[10]

The court concludes that even if the *First National Bank* and the *Hall* cases cannot be reconciled, the holding of the *Hall* case, that the payment of premiums under the circumstances here present does not constitute the payment of deductible expenses under Section 23(a) (2), is the correct one.

G. ANDY RUNGE

FEDERAL TAXATION—ISSUANCE OF STOCK BY EMPLOYER TO EMPLOYEE—GIFT OR COMPENSATION

Neville v. Brodrick[1]

The question presented in the principal case was whether the stock issued by the corporate employer to the taxpayer, its employee, constituted compensation for services rendered or to be rendered and, therefore, taxable under Section 22 (a) (2) of the Internal Revenue Code of 1939 or whether it was a gift and, therefore, not taxable under Section 22 (b) (3) of the Internal Revenue Code of 1939.

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9. Estate of Hall v. Commissioner, 17 T.C. 20 (1951); Leslie v. Commissioner, 6 T.C. 488 (1946).
10. Commissioner v. Charleston National Bank, 213 F.2d 45 (4th Cir. 1954).

1. Neville v. Brodrick, 235 F.2d 263 (10th Cir. 1956).

Section 22 (a) of the Internal Revenue Code of 1939 defines gross income: "(a) General Definition.—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, ..."[2]

Section 22 (b) (3) of the Internal Revenue Code of 1939 states: "(a) General Rule—Gross income does not include the value of property acquired by gift, bequest, devise, or inheritance."[3]

Under the trems of the Statute a bestowal of money or stock could not be both a gift and compensation for personal services.[4] It was necessary, therefore, for the court to determine which this particular issuance of stock constituted. In deciding that the stock received by the taxpayer was a gift, the court set forth what it termed "several well recognized general rules for guidance":

1. "A payment in cash or the issuance of stock may constitute additional compensation for services rendered or to be rendered or to be rendered within the purview of the statute although the payment is made or the stock is issued voluntarily and without legal obligation."[5]

2. "And if an employer issues and delivers to an employee stock for the primary purpose of vesting in the employee a proprietary interest in the business as an inducement for the rendering of better service to the employer, the employee receives compensation for personal services within the meaning of section 22 (a)"[6]

3. "An employer may make a gift to an employee without rendering it taxable but the payment of an additional sum in cash or the issuance of stock in lieu of cash by an employer to an employee carries with it a legal presumption that the transaction constitutes compensation for services as distinguished from a gift, within the meaning of the statute".[7]

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2. Int. Rev. Code of 1954, § 61.

3. Int. Rev. Code of 1954, § 102.

4. Bogardus v. Commissioner, 302 U.S. 34 (1937) where the Supreme Court held as gifts and not compensation, allowances voted by stockholders of a new corporation to employees of the old corporation whose assets the new corporation took over, the employees not being in the service of the new corporation.

5. *Id.* at 265. See also Old Colony Trust Company v. Commissioner, 279 U.S. 716 (1929); Weber v. Commissioner, 219 F.2d 834 (10th Cir. 1955); Peters v. Smith, 221 F.2d 721 (3d Cir. 1955).

6. *Ibid.* See also Commissioner of Internal Revenue v. Lo Bue, 351 U.S. 243 (1956).

7. *Ibid.* See also Wilkie v. Commissioner, 127 F.2d 953 (6th Cir. 1942), *certiorari denied* 317 U.S. 659 (1942); Carragan v. Commissioner, 197 F.2d 246 (2d Cir. 1952); Wallace v. Commissioner, 219 F.2d 855 (5th Cir. 1955); Bass v. Howle, 62 F.2d 721 (5th Cir. 1933); Fisher v. Commissioner, 59 F.2d 192 (2d Cir. 1932); Lunsford v. Commissioner, 62 F.2d 740 (6th Cir. 1933); Noel v. Parrot, 15 F.2d 669 (4th Cir. 1926); Commissioner v. Bonwit, 87 F.2d 764 (2d Cir. 1937); Anderson v. Commissioner of Internal Revenue, 31 B.T.A. 197 (1934), affirmed in 79 F.2d 979 (2d Cir. 1935).

4. "Whether an amount received by an employee either in cash or stock constitutes compensation for services or a gift depends upon the intention of the parties, principally that of the payor or the party issuing or causing the issuance of the stock; and in a case of this kind the taxpayer has the burden of proving a gift, including the donative intent."[8]

5. "Upon the conventional transfer of stock, there is an element of economic benefit to the recipient thereof. But if the motivating purpose of the transaction is that of a gift, such economic benefit is incidental and not compensatory, within the intent and meaning of Section 22. And if the transfer is intended as a gift, it is a gift nonetheless because inspired by a feeling of gratitude for past or anticipated future services."[9]

6. ". . . . it is the province and duty of this court to determine whether or not the finding of the trial court respecting such issue is supported by substantial evidence or is against the weight of the evidence and therefore clearly erroneous."[10]

It is necessary to carefully examine the particular set of facts to see how they fit into the above stated "well recognized general rules". A brief cursory examination of the facts in *Neville v. Brodrick* will reveal why the court, in applying these general rules, could arrive at the decision that the issuance and receipt of the stock was intended as a gift, and not as compensation for services rendered or to be rendered.

In the *Neville* case, Neville, the taxpayer, had been employed by the Seymour Packing Company from January, 1921, until June, 1950. Taxpayer had risen to president of the company in 1947, and retired in 1950. In 1946 Willi, an employee of the company, approached Perry, then president of Seymour, requesting 300 shares of stock in the company, implying that otherwise he would quit. Willi and taxpayer were highly respected as businessmen and were, with their families, social friends of Bowman, the majority and controlling stockholder of the Seymour Company. Bowman had daughters and no sons. He often referred to taxpayer and Willi as his boys. Bowman was also very friendly with the wife and son of the taxpayer, and the wife and son of Willi. On several occasions, Bowman stated he was going to do something very nice for the taxpayer and his wife. Taxpayer

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8. *Id.* pp. 265, 266. See also Weber v. Commissioner, 219 F.2d 834 (10th Cir. 1955); Helvering v. National Grocery Co., 304 U.S. 282 (1934); Commissioner of Internal Revenue v. Jacobson, 336 U.S. 28 (1949); Smith v. Manning, 189 F.2d 345 (3d Cir. 1951).

9. *Id.* p. 266. See also Bogardus v. Commissioner, *supra* note 4.

10. *Id.* p. 268. See also O'Malley v. Ames, 197 F.2d 256 (8th Cir. 1952), where the court held that where a finding of the trial court is challenged as being unsupported by evidence, it is not the province of the appellate court to retry the case or to substitute its judgment or conclusion for that of the trial court, but it is the province of the appellate court to determine whether the finding is supported by substantial evidence or whether it is clearly against the weight of the evidence and consequently clearly erroneous.

at that time had no knowledge of what Bowman was referring to. Investigations were made by Bowman to determine how the transactions with Willi and Neville could be handled within the framework of revenue legislation. The stock involved in this action was issued on five separate dates, part to taxpayer, part to his wife, and part to his son. Taxpayer's wife had never been employed by the company. Taxpayer's son had only worked during summer vacations for the company. The stock was issued out of the individual holding of the three major stockholders, including Bowman. During the years 1946, 1947, and 1948, when the stock in question was issued, the taxpayer earned through salary, flat bonus, and Christmas bonus, $17,038.71, $30,250.18, and $26,048.12, respectively. Taxpayer considered this full and adequate compensation for the services rendered. The stock transaction was consistently referred to as a gift. Bowman referred to it as a gift in his conversations. No one referred to the stock as representing compensation. No one testified categorically that the purpose of the issuance of the stock was to compensate the taxpayer for past or future services to the company. None of the parties ever claimed or sought any tax benefits as business expenses or otherwise on account the stock representing compensation to the taxpayer.

The court, in summing up the effect of the evidence presented, stated that "viewed in its entirety, the evidence obliges the conclusion that the motivating purpose of the issuance of the stock was to make gifts to the recipients thereof as distinguished from additional compensation for services rendered or to be rendered for the corporation, and that the finding of the trial court otherwise was clearly erroneous."[11] The court seems to say that there was no evidence from which the fact finders could find that the issuance of the stock was compensation for services rendered or to be rendered, otherwise, how could it say that the finding of the trial court was clearly erroneous. Although the evidence adduced may indicate an intent to make a gift rather than compensation for services, it would, likewise, seem that the fact finders could find an intent to compensate for services, if so, was the court correct in holding that the trial court's finding was clearly erroneous? It would seem not. The court seems to be usurping the trial court's function, *i.e.*, if there was substantial evidence to support the trial court's finding it should be sustained.[12]

A gift has been judicially defined as a valid transfer of property from one to another without consideration or compensation therefor.[13] The essential elements of a gift are as follows: (a) a donor competent to make the gift, (b) a clear and unmistakable intention on his part to make it, (c) a donor capable of taking the gift, (d) a conveyance, assignment or transfer sufficient to vest the legal title in the donee, without power of revocation at the will of the donor, and

11. *Id.* 268.
12. O'Malley v. Ames, *supra* note 10.

a relinquishment of dominion and control of the subject matter of the gift by delivery to the donee.[13]

A particular payment cannot be both a gift and compensation. It is either one or the other. No general rule can be laid down, and each case must stand on its own merits. If the employer is under legal obligations to make the payment, there is little question but that the amount received is taxable compensation. However, the fact that the employer is under no legal duty to pay the employee, or that services are performed voluntarily is not conclusive that the amount received is a non-taxable gift.[14]

If an employer takes a deduction for the payment, it is a strong indication that he considers it compensation. If he does not, it is evidence, although not conclusive, that the payment is not compensation but a gift. The length and value of the employer's service, the manner in which the amount of "additional compensation" or bonus was determined, the treatment of the payment on the books of the employer and all other pertinent evidence is to be considered in determining the intent of the parties.[15]

Evidence adduced in *Neville v. Brodrick* showing the long tenure of employment of taxpayer, the close relationship of taxpayer and the majority and controlling stockholder, the continuous reference to the stock issue as a gift, the fact that the shares were issued out of the controlling stockholder's private holdings, and that the company did not take an expense deduction would be strong arguments for holding the transaction a gift.[16] But the fact finders found the transaction to be

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13. Gray v. Barton, 55 N.Y. 68 (1873).

14. Weil, 31 B.T.A. 899 (1934); *aff'd.* 82 F.2d 561 (5th Cir. 1936), *cert. denied.*

15. O'Daniel v. Commissioner, 173 F.2d 966 (2d Cir. 1949), where severance pay was held to be compensation for past services, even though the employer had no legal obligation to make the payment.

16. Levey, 26 B.T.A. 889 (1932), *aff'd.* 68 F.2d 401 (C.A.D.C. 1933), where payment made by a corporation annually for seven years to reimburse officers for federal and state income taxes was held not a gift though so denominated in the corporate resolutions and not deducted by the corporation. There was no intent to make a gift, and the payments had a direct relationship to the services performed.

Nickelsburg v. Commissioner, 154 F.2d 70 (2d Cir. 1946), where court held that although characterized as a "wedding gift" in the director's resolution and corporate minutes, a payment received by the corporation president was held to be taxable compensation and not a gift where the resolution authorizing the payment stated that it was made in consideration of the president's previous years of service.

Van Sicklen, 33 B.T.A. 544 (1935), where Christmas bonuses paid to employees in amounts approximating a percentage of the employee's salaries were held taxable as additional compensation even though termed "gifts".

Hoefle, P-H 1938 B.T.A. MEMO. ¶ 38,163, where the court said that Christmas gifts not proportionate to salary have been held not taxable Affirmed without discussion of this point, 114 F.2d 713 (6th Cir. 1940).

compensation for services rendered. This court in holding that the transaction was a gift would in effect be saying that the lower court's finding was not supported by substantial evidence. The evidence presented indicated that Willi, the employee initially requesting the stock, might quit his employment unless issued stock. Stock issued for the purpose of retaining employees would be considered compensation. It could logically be argued that taxpayer was granted stock to encourage him to remain in the employment of the company, or, especially, to keep him from being disgruntled upon learning that Willi had been issued stock and, therefore, rendering him a less effective employee. It is the belief of the writer that the fact finders could have so reasoned and found this to be the fact. The appellate court should not disturb such finding unless not supported by substantial evidence, which does not seem to be the situation in this case.

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