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Comments

RES JUDICATA AND THE JURISDICTION OF FEDERAL COURTS IN DIVERSITY OF CITIZENSHIP CASES

The doctrine of res judicata is grounded in the need for putting an end to litigation. It is felt by the courts that ordinarily one suit which determines or gives a full and fair chance for determining causes of action and issues between litigants...
should be enough, and when this much has been given, further opportunity should be denied. An interesting application of this doctrine to a problem involving the jurisdiction of the federal district court in a case resting purely on diversity of citizenship was recently announced by the United States Supreme Court in the case of Angel v. Bullington.¹

Angel, a citizen of North Carolina, purchased land in Virginia from Bullington, a citizen of Virginia. Part of the purchase price was paid and a series of notes secured by a deed of trust was executed by Angel for the balance thereof. Subsequently one of the notes came due and Bullington, acting upon an acceleration clause in the deed, caused all other notes to become due and called upon the trustees to sell the land. The sale was duly made in Virginia, and the proceeds of the sale applied to the payment of the notes. Bullington brought suit in the state court of North Carolina in an attempt to recover the deficiency. A statute of North Carolina provided that a deficiency judgment could not be recovered in that state.² Angel demurred to the complaint on the ground that, because of the statute, it failed to state a cause of action. The demurrer was overruled and an appeal was taken to the Supreme Court of North Carolina.³ That court held that the statute operated on the adjective law of the state so as to withdraw from the jurisdiction of the courts suits of that type; that Bullington’s claim for the deficiency, and the question of constitutionality of the North Carolina statute, were matters of substantive law; and the court had no power to render judgment thereon. Bullington, without seeking review of the decision in the United States Supreme Court, began his suit anew in the Federal District Court for the Western District of North Carolina.⁴ Angel interposed the prior suit as a defense to this action, claiming that it was a bar to the suit. Judgment was given for Bullington in that court which was affirmed by the circuit court of appeals.⁵ On appeal to the United States Supreme Court, the decisions of the lower courts were reversed (three judges dissenting) on the ground that the defense of res judicata was valid.

The decision of the court points out that the prevailing rule is that an adjudication bars further litigation between the same parties not only as to all issues raised and decided, but also as to those which could have been raised. The court observed that the causes of action as presented to the North Carolina court and the federal district court were identical; that, if the action had been brought anew in another North Carolina court, rather than the federal court, the first suit would be a bar

2. "In all sales of real property by mortgagees and/or trustees under powers of sale contained in any mortgage or deed of trust hereafter executed, ... the mortgagee or trustee or holder of the notes secured by such mortgage or deed of trust shall not be entitled to a deficiency judgment on account of such mortgage, deed of trust or obligation secured by the same." N. C. Public Laws 1933, c. 36, N. C. Gen. Stats. (Mitchie, 1943) § 45-36.
5. 150 F. (2d) 679 (C.C.A. 4th, 1945).
to the second; that, for the purposes of diversity jurisdiction, a federal court is, in effect, only another court of the state. The court further asserted that the only issue in the first suit was whether or not all the courts of North Carolina were closed to this cause of action, and the determination of this issue involved questions of constitutionality; that the merits of that issue were adjudicated in the North Carolina court; that the same issue was raised in the federal district court, and the doctrine of res judicata precluded further consideration of the matter. The court also said that when a claim is refused enforcement, not on the ground that the distribution of judicial power among the various courts of the state requires the suit to be brought in another court in the state but on the inaccessibility of all the courts of the state to such litigation, the merits of the claim are disposed of. The court also emphasized that the statute of North Carolina is expressive of state public policy; that the essence of diversity jurisdiction is that it follows state law and state policy; that a federal court located in North Carolina, when invoked on the ground of diversity of citizenship, cannot give that which North Carolina has withheld.

Vigorous dissenting opinions took issue with the propositions that the merits of a claim are disposed of when refused enforcement, and that, for the purposes of diversity jurisdiction, a federal court is, in effect, only another court of the state. It was their contention that the statute of North Carolina as interpreted by the state's highest court was an expression of the adjective law of the state and, as such, did not affect the federal court; that the dismissal of Bullington's cause of action gave him no opportunity to be heard on the merits.

The court's majority opinion, while not as explicit as it might have been, seems to have applied the doctrine of res judicata in a limited way. The court did not say that the issue of the deficiency had been adjudicated but confined its discussion to this issue: Did Bullington present a cause of action cognizable by the courts of North Carolina? In order for the adjudication of this issue to affect the federal court, it was necessary to apply the doctrine expressed in the case of Erie Railroad v. Tompkins. If that doctrine had not been applied, the federal court, being the court of an independent sovereign, would be unaffected by any determination that Bullington did or did not have a cause of action cognizable by the state courts of North Carolina. In the instant case the court apparently not only applied the doctrine but also extended it, or at least further defined its application.

The "Erie doctrine" originated in a decision of the Supreme Court of the United States holding that in matters at law the federal courts must follow the substantive law of the state in which the federal forum is located. The Erie decision substantially altered the previously existing relationship of the federal courts to the law of the state in which such court happened to be located. Prior to the Erie case the federal courts had applied their own conception of the substantive general law to the cases brought before them. Thus the result of a given case might vary simply

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7. Ibid.

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by the fortuitous choice of forum. The federal courts were not required, under that decision, to apply the state's procedural rules of law. As a result the difference between substance and procedure became important in the federal courts.9

Since the decision of the *Erie*10 case the United States Supreme Court has consistently moved toward an objective under which the results of a given case will not vary simply because of the accident of citizenship. The theory seems to be that the federal court in diversity of citizenship cases sits as a court coordinate with the state court to apply the state law.11 The policy of the law as defined by the Supreme Court is expressed in *Guaranty Trust Company v. York*,12 where the court said in part as follows:

“A federal court adjudicating a State-created right solely because of diversity of citizenship of the parties is for that purpose, in effect, only another court of the State. It cannot afford recovery if the right to recover is made unavailable by the State nor can it substantially affect the enforcement of a right as given by the State.”

Examples of the steps taken by the Supreme Court in this direction may be found in the *Guaranty Trust Company*13 case in which the court held the *Erie* doctrine applicable to suits on the equity side of the court, and the case of *Griffin v. McCoach*,14 holding the local conflicts of law rules must be applied by the federal courts.15 The instant case, holding that if a state court lacks jurisdiction to hear a state-created cause of action, the federal court located within that state likewise lacks jurisdiction to hear the cause of action, is another step in that direction.

The *Erie*16 case purported to require the federal courts to follow state law in diversity of citizenship cases only in matters involving substantive law. There are numerous instances, however, where the United States Supreme Court, in order to apply the *Erie* doctrine and obtain uniformity of result in diversity of citizenship cases, has classified rules of law usually considered procedural law as substantive law. For example, the court has held that the local rules as to burden of proof17 and the local statutes of limitations18 must be applied by the federal courts when state-created rights are involved. The instant case does not profess to project the *Erie* doctrine into the realm of procedural law. The court also appears to have used the

16. See note 10 *supra*.
terms "substantive law" and "procedural law" in a different sense than that usually employed by most courts. The decision points out that the statute of North Carolina, although construed as procedural by the state court, is expressive of the policy of that state, and it is the duty of the federal courts to carry out the policy of the state in which they are sitting. This statement seems sound. Law is merely an expression of policy; a declaration by the legislature and courts of those rules of conduct which they consider most desirable. If a statute is a clear manifestation of state policy, that statute should be enforced by the federal courts within the state whether it be characterized as procedural or substantive law.\textsuperscript{10}

It is true that the North Carolina court characterized the statute as adjective in nature, but this characterization should not be conclusive on the federal courts.\textsuperscript{20} It would seem that judicial characterization of a particular matter as substantive or procedural does not furnish a criterion to determine whether the same matter is remedial for the purpose of the rule that the federal courts are bound by state laws. For the purpose of that rule, the guiding consideration is that, assuming the identity of the facts involved, the federal courts must reach the same result which a state court would have reached had the suit been instituted in a state rather than a federal forum. Characterization of a matter as remedial or procedural under analogous circumstances must give way in favor of a fundamental policy of uniformity of result.\textsuperscript{21} It seems, therefore, that the ultimate test to be used by the federal courts in determining whether state law is applicable to suits brought before them on state-created rights is not whether a given rule of law is procedural or substantive, but whether a different conclusion may result if the state law is not followed.\textsuperscript{22}

\textsuperscript{21} In Guaranty Trust Co. v. York, 326 U. S. 99, 109, 65 Sup. Ct. 1464, 160 A.L.R. 1231, 1237 (1945) the court said: "... The question is not whether a statute of limitations is deemed a matter of 'procedure' in some sense. The question is whether such a statute concerns merely the manner and the means by which a right to recover, as recognized by the State, is enforced, or whether such statutory limitation is a matter of substance in the aspect that alone is relevant to our problem, namely, does it significantly affect the result of a litigation for a federal court to disregard the law of a State that would be controlling in an action upon the same claim by the same parties in a State court?"

"It is, therefore, immaterial whether statutes of limitation are characterized either as 'substantive' or 'procedural'. ... In essence, the intent of that decision (Erie Railroad Co. v. Tompkins) was to insure that, in all cases where a federal court is exercising jurisdiction solely because of the diversity of citizenship of the parties, the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of the litigation, as it would be if tried in a State court." Holmberg v. Armbricht, 327 U. S. 392, 66 Sup. Ct. 582 (1946); Kordewick et al. v. Indiana Harbor Belt R. Co., 157 F. (2d) 735 (C.C.A. 7th, 1946); Weiss v. Routh, 149 F. (2d) 193 (C.C.A. 2d, 1945).

\textsuperscript{22} See note 21, \textit{supra}. In the instant case the court declared the case of David Lupton's Sons v. Automobile Club of America, 225 U. S. 489, 32 Sup. Ct. 711 (1912) to be obsolete. That case permitted a plaintiff who had been barred from suing in the state courts because of the non-compliance with a state foreign corporation statute to sue in the federal court sitting in the same state.
One of the chief objections expressed by the dissenting opinions to the majority decision of the instant case seems to rest on the fact that the majority holds that the state can indirectly restrict or limit the jurisdiction of the federal courts within the state simply by placing a limitation upon the jurisdiction of the state courts. The argument runs that the courts of the United States are tribunals of a different sovereign, and exercise a distinct and independent jurisdiction from that exercised by the state courts. But it does not follow that the statute here involved limits the jurisdiction of the federal courts located in North Carolina. Rather it is the law of the federal sovereign that the federal courts in enforcing state-created rights will apply the relevant laws of the state in which the court is sitting in order to insure that a different conclusion will not result simply from the choice of forum. Therefore, if the state courts are closed to a plaintiff, the federal courts likewise are closed provided he is asserting a state-created right only. Although it is true that the federal court represents an independent sovereign and is in no way subject to the control of the state, the decision of the instant case does no violence to that conception. The federal district courts were established, not only to hear controversies arising under federal law, but also to aid a citizen of another state in obtaining a fair hearing when suing in a state other than his own. These courts were not intended to give the out-of-state plaintiff an advantage not possessed by the citizens of the state in which the cause was heard. In so far as diversity of citizenship is concerned, the federal district courts were meant only to complement the existing state courts. There would seem to be no real objection to a policy that permitted a federal court to refuse to hear a state-created right because the cause of action was not cognizable in the court of the state in which the federal court was located.

Since under the decision in the instant case a federal court may take cognizance of a state-created right only when such right is actionable in the courts of the state in which the federal court is located, the doctrine of res judicata would be applicable upon an adjudication that no court within the state had jurisdiction to hear the cause of action. In the instant case the question of the accessibility of the courts

23. Mr. Justice Reed in his dissenting opinion said: "It (instant case) also departs from controlling precedents that state enactments on jurisdiction, remedies and procedures do not affect the jurisdiction, remedies or procedures of federal courts." 67 Sup. Ct. 657, 665. He also quoted from David Lupton's Sons v. Automobile Club of America, 225 U. S. 489, 500 (1912) the following passage: "The state could not prescribe the qualifications of suitors in the courts of the United States, and could not deprive of their privileges those who were entitled under the Constitution and laws of the United States to resort to the Federal courts for the enforcement of a valid contract." Mr. Justice Rutledge in his dissenting opinion said: "The Erie Rule did not purport to change the law of the federal jurisdiction in diversity cases, taking it out of the hands of Congress and the federal courts and putting it within the states' power to determine." 67 S. Ct. 657, 671.

24. In the court's opinion Mr. Justice Frankfurter said: "...Diversity jurisdiction must follow State law and policy. A federal court in North Carolina, when invoked on the grounds of diversity of citizenship, cannot give that which North Carolina has withheld." 67 S. Ct. 657, 662.

25. Ibid.
within the state of North Carolina to Bullington’s cause of action had been litigated by the North Carolina courts. This determination being conclusive on the federal courts of the state should not be relitigated in that court.

The dissenting opinion took issue with the proposition that the merits of the case were disposed of when they were refused enforcement. But it appears that the dissenting and majority opinions used the term “merits” in different senses. The term “merits” may refer to the merits of the whole case or controversy between the parties, or it may be restricted to some particular issue of law or fact. If the latter, then the doctrine of res judicata is applicable only to the issues actually adjudicated and the essential concomitants thereof. It is evident that the majority opinion used the term in the more restricted sense. The court said:

“The only issue in controversy in the first North Carolina litigation was whether or not all the courts of North Carolina were closed to that (Bulling-ton’s) litigation. The merits of that issue were adjudicated.”

There was no adjudication of the merits of the deficiency due Bullington, and the court did not purport to apply the doctrine of res judicata to this issue. The court in the instant case was not concerned with this issue since it only decided that Bullington had no cause of action cognizable in the courts of North Carolina, and he had a full determination of that issue.

It is generally recognized that if judgment is given for a defendant on the ground that the plaintiff is not entitled to maintain an action in the state in which the judgment is rendered, the judgment is on the merits to the extent that it will bar the plaintiff from maintaining a further action in that state. For example, refusal to enforce a cause of action on the grounds of public policy is a bar to further action within the state where the judgment is rendered, but not to an action brought in another state. This is also true when a statute of limitations is successfully interposed as a defense to an action. Therefore, the conclusion seems correct that, when confronted with the facts of the instant case, the court rendered a decision on the merits by refusing to enforce the cause of action.

LOUIS W. COWAN

EFFECT OF THE WILLIAMS CASES UPON RECOGNITION OF FOREIGN DIVORCE DECREES IN MISSOURI

The confusion resulting from the efforts of the courts to reconcile conflicting interests involved in the adjudication of divorce matters has resulted in one of the

26. See note 3 supra.
27. RESTATEMENT, JUDGMENTS (1942) § 49.
28. Ibid.
29. Ibid.
30. Ibid.
31. In the instant case the court said: “If an asserted federal claim is denied enforcement on a professed local ground, but a so-called local ground which is subject to review here because it is in fact the adjudication of a federal question, then the ‘merits’ of that claim were adjudicated in the only sense that adjudication of the ‘merits’ is relevant to the principles of res judicata.” 67 Sup. Ct. 657, 661.
most perplexing problems in the law. Those courts espousing recognition of foreign divorce decrees based upon constructive service, influenced by the possible unfortunate consequences of adjudging such decrees to be invalid, and the desire for uniformity in the law of divorce, find weighty support in the principles of comity and the full faith and credit clause of the Federal Constitution. Other courts, unwilling to see the laws of their respective states flouted by the domiciliaries therein, reiterate their power to question the jurisdiction of the foreign court over the person or the subject matter—unless those issues were litigated by the parties to the proceedings.

As the question of whether a state court is justified in refusing to give full faith and credit to a decree of a sister state is one to be decided ultimately by the Federal Supreme Court, the final arbiter as to the meaning of and the limitations upon the full faith and credit clause of the Federal Constitution, that court grasped the opportunity in the Williams cases to reexamine the jurisdictional basis of divorces and to construe the implementing act of Congress so as to obviate some of the uncertainties which have beset the institution of marriage.

The facts of the celebrated Williams cases have received such nation-wide attention that they may be tersely stated as follows: The petitioners, domiciliaries of North Carolina, left their respective spouses in that state and went to Nevada, where, as soon as Nevada law permitted, they obtained divorces on constructive service, wed, returned to North Carolina, and were there convicted for bigamous cohabitation. The Supreme Court, in the first Williams case, overruled the Haddock holding and held that a divorce granted in Nevada, was the highly criticized decision in Haddock v. Haddock, 201 U. S. 562, 26 Sup. Ct. 525 (1906), which held, by a vote of five to four, that where a spouse deserts the matrimonial domicile in State A and establishes a new domicile in State B, a divorce granted to such spouse in State B, based upon constructive service, is valid in State B, but is not entitled to full faith and credit in State A. An excellent criticism of this case, and the evils to which its adherence would lead, i.e., illegitimacy of children of a second marriage, bigamy prosecutions, etc., may be found in Miller v. Miller, 200 Iowa 1193, 206 N. W. 262 (1925).

8. In this action, the domicile of the petitioners in Nevada was presumed. The State, however, relied upon the Haddock case, and the petitioners upon the full faith and credit clause.


on a finding that one spouse was domiciled in Nevada, must be respected in North Carolina, where Nevada's finding of domicile was not questioned, though the other spouse had neither appeared nor been served with process in Nevada, and though recognition of such a divorce offended the policy of North Carolina.

In 1945, after a retrial in the state court had resulted in convictions grounded upon the Nevada court's lack of jurisdiction, for the reason that the petitioners had never established bona fide domiciles therein, the case again came to the Supreme Court, and the convictions were this time affirmed. The court held that where either spouse, regardless of marital fault, leaves the matrimonial domicile, establishes a domicile in another state, and secures a divorce according to local law, based upon constructive service, that divorce decree is presumptively valid and entitled to full faith and credit in every state in the Union, but in case the decree is pleaded as a defense in other state courts, although presumptively valid, it may be collaterally assailed on the ground that the party acquiring such divorce had never actually acquired a bona fide domicile within the jurisdiction of the court rendering the decree.

Before a determination of the effect, if any, of the Williams cases upon the Missouri law of jurisdiction for divorce, an understanding of Missouri case law upon this question, as it stood prior to 1942, is, of course, a prerequisite. The first time this issue was clearly presented in this state was in Gould v. Crow. The plaintiff had married in Missouri, the matrimonial domicile, and her husband had subsequently gone to Indiana, fulfilled the statutory requirements of that state, and obtained a divorce from the plaintiff based upon constructive service. After returning to Missouri, he made a conveyance of certain lots in this state, in which plaintiff did not join. Upon his death the plaintiff claimed dower in this land, alleging that the Indiana court lacked jurisdiction. In deciding in favor of the defendant, the Supreme Court of Missouri followed certain fundamental concepts. As the adjudication of the marital status is involved, the court determined that a divorce suit is a proceeding in rem, the status of husband and wife being the res. The court also

12. Italics added.
13. At first glance, this holding might seem to go almost back to the Haddock case, cited supra note 7. However, by Williams II the divorce decree is prima facie valid, and the burden is upon the party attacking the divorce to prove the absence of domicile. For an analysis of this case, and the individual opinions of each judge, see Powell, And Repent at Leisure (1943) 58 HARV. L. REV. 990. Also, Lorenzen, Extraterritorial Divorce (1945) 54 YALE L. J. 799.
14. It is suggested by Professor Stanley, in his article, The Williams Cases and Divorce in California (1945) 20 CALIF. S. B. J. 350, since the determination of the court granting the divorce, in respect to the domicile of the plaintiff, is not conclusive, and, as a result, a man may be married in some states and divorced in others, that the Supreme Court may be forced to undertake further judicial modification in order to eliminate the unfortunate uncertainties resulting from Williams II.
15. 57 Mo. 200 (1874); accord, Williams v. Williams, 53 Mo. App. 617 (1893); Hamill v. Talbott, 72 Mo. App. 22 (1897).
recognized the theory of the "divided res," declaring that each spouse may acquire a separate domicile, and, if so, this "status" attaches to each of the parties.

The court then constructed the foundation for subsequent determinations of this problem by averring that the presumption is that the husband's length of domicile had been determined by the foreign court; that every state has the right to determine the marital status of all persons having their domicile within its territory; that the decree so pronounced is a judgment in rem: and, when not affected by fraud, is valid everywhere, and is entitled to full faith and credit in every other state.

In 1906, by virtue of the unpopular holding in Haddock v. Haddock, and the refusal of the highest court in the land to maintain that there could be such a thing as a "divided res," any cherished expectations which legal scholars may have embraced of uniformity in divorce law throughout the United States were dealt a severe blow, and the subsequent decisions upon this question in each state were left to the mercy of judicial whim and the possible idiosyncrasies of particular religions embraced by the majority of any state's domiciliaries, or even by the presiding judges themselves. Missouri, however, held firm to its line of precedent, and in Howard v. Strode refused to accept the invitation to confusion tendered by the Haddock decision, even though the plaintiff, heavily relying upon that holding, averred that the full faith and credit clause could not be invoked to compel a state to recognize as valid a divorce granted by a sister state upon constructive service, where the defendant in the suit had never had a matrimonial domicile in the state granting the divorce. Conceding the contention of the plaintiff, the Missouri court ruled, however, that Haddock v. Haddock did not make it mandatory that all other states refuse to recognize a divorce decree based upon constructive service and domicile of one of the parties in a state other than that of the matrimonial domicile of the parties, and that such decree could be recognized by a sister state if it were the policy of such state to do so.

17. In Anthony v. Rice, 110 Mo. 223, 19 S.W. 423 (1892), upon almost identical facts, the Supreme Court re-iterated the pertinent principles developed in Gould v. Crow, and held that the decree of the foreign state, based on service by publication, was "presumptively valid" in all states until "overcome by proper proof of fraud and collusion." It is interesting to note the striking similarity of this language to that used in Williams II, supra note 13.
18. See note 7 supra.
20. It has been pointed out elsewhere that the strong religious convictions held by Mr. Justice Murphy and Mr. Justice Jackson, who dissented in Williams I, may have been a strong factor in their attitude toward easy divorce. Evans, Jurisdiction to Divorce—A Study in Stare Decisis (1943) 8 Mo. L. REV. 177 at 182.
Where there has been a definite showing of "fraud" on the part of the spouse obtaining the foreign decree, however, this state, prima facie, at least, has not been hesitant in its refusal to accord recognition to the out-of-state divorce. In Wagoner v. Wagoner, the wife had obtained a decree of separate maintenance in Missouri, the state of the matrimonial domicile. To defeat this decree, the husband went to Nevada, obtained a divorce on constructive service, immediately returned to Missouri, and demanded that the decree for separate maintenance be vacated. The Missouri Supreme Court, on these facts, held that the husband had never been domiciled in Nevada, and that the decree was therefore void for want of jurisdiction: "To the extent only of its own sovereignty are the records of its judicial proceedings entitled to full faith and credit in other states. When its courts act outside their territorial jurisdiction, i.e., upon persons and things having no existence within the limits of their process, their acts are without jurisdiction and void."

The case of Keena v. Keena gave the St. Louis Court of Appeals an opportunity to restate the evidence of fraud necessary to compel a Missouri court, at that time, to refuse to give full faith and credit to the decree of a sister state. In that case, the husband left Missouri, the matrimonial domicile, and moved to Chicago, where after having resided there for nine years, he obtained a divorce. To effect this result, however, the husband falsely swore at the trial that his wife had deserted him in Illinois and that her present place of residence was not known. Upon his misrepresentations, the certificate of publication was mailed to an address existing only in the husband's mind. The husband then remarried and returned to Missouri, at which time the wife sued to have the foreign decree declared invalid and, also, for separate maintenance. Influenced by the fact that the husband's

22. As used in the cases on this point, the term, "fraud" usually denotes the want of a bona fide domicile established by the spouse suing for divorce in the foreign state. Williams v. North Carolina, 325 U. S. 226, 65 Sup. Ct. 1092 (1945); Esenwein v. Pennsylvania, 65 Sup. Ct. 1118 (1945); Gould v. Crow, 57 Mo. 200 (1874). As the decree is adjudicating the status of the parties, the suit for divorce resembles an in rem proceeding, and to have jurisdiction over the subject matter, namely, the marital status, the plaintiff in the action must be a domiciliary of the state issuing the decree. Leichty v. Kansas City Bridge Co., 354 Mo. 629, 190 S.W. (2d) 201 (1945); RESTATEMENT, CONFLICT OF LAWS (1934) § 111 at 168. To gain jurisdiction over the out-of-state, non-appearing defendant most states have statutes providing for notice by publication.

23. 287 Mo. 567, 229 S.W. 1064 (1921).

24. Courts seem to be more meticulous in testing the authenticity of domicile when such foreign divorce would have the effect of setting aside a previously-rendered decree for separate maintenance. Wright v. Wright, 350 Mo. 325, 165 S.W. (2d) 870 (1942). Mr. Justice Douglas, concurring in Esenwein v. Pennsylvania, 65 Sup. Ct. 1118, 1120 (1945), even suggests that "it is not apparent that the spouse who obtained the decree can defeat an action for maintenance in another state by showing that he was domiciled in the state which awarded him the divorce. In the absence of an appearance or personal service, I am not convinced that the decree need be given full faith and credit when it comes to maintenance or support of the other spouse or children."

25. Supra note 23 at p. 594.

26. 222 Mo. App. 825, 10 S.W. (2d) 344 (1928).
acquisition of residence in Illinois was made in good faith, the court disregarded plaintiff's contention that, since Illinois was not the matrimonial domicile the full faith and credit clause did not compel recognition of such decree, and stated that the fraud for which a judgment of another state may be directly attacked is fraud entering into its very concoction and procurement, which does not include false swearing at the trial. The findings of fact, conclusions of law, and decree of such foreign court showed that that court found the husband to be a bona fide resident of that state, and that he was entitled to a decree of divorce.

Just a few weeks prior to Williams I, the Supreme Court of Missouri handed down the well-reasoned opinion of Wright v. Wright. Upon facts identical to the Wagoner case, the court held that, although it is the policy of this state on principles of comity, to recognize divorce decrees obtained in other states upon constructive notice to members of this state, in the absence of proof of lack of jurisdiction, or fraud in their procurement, yet where one spouse goes to a state, other than that of the matrimonial domicile, for the sole purpose of obtaining a divorce and then obtains a divorce under a residence simulated for that purpose and not with any intention of residing there permanently or indefinitely, the decree is not binding upon courts of other states. The court further held that the want of jurisdiction may be set up in the answer, and that, under our code, such pleading will be equivalent to a direct action by a bill in equity to set aside the judgment.

In reviewing the Missouri decisions handed down between the years 1874 and 1942, one may readily ascertain that it has been the long standing policy of this state to accord recognition to the divorce decrees of sister states, such recognition being based both upon principles of comity and the full faith and credit clause, unless the party directly attacking such decree presents cogent and convincing proof that the plaintiff in the divorce action had not established a bona fide domicile in the state rendering the decree. In two decisions the Missouri Supreme Court has refused to recognize an out-of-state divorce, but, in both instances, holding such decree to have been valid would have resulted in setting aside a decree for separate maintenance which the non-appearing spouse had previously obtained in Missouri, which fact may be of significance. It might also be noted that the only effect which the Haddock case seems to have had upon subsequent decisions in

27. Quaere, however, whether this result would have been reached had not the husband remarried. Contra: Leichty v. Kansas City Bridge Co., 354 Mo. 629, 190 S.W. (2d) 201 (1945).
29. Supra note 23.
30. An interesting problem arises when, under such facts, the other spouse appears and contests the proceedings. In Davis v. Davis, cited supra note 4, where the wife put the jurisdictional question of domicile in issue, the Federal Supreme Court held that the adjudication of this question was res adjudicata, and that the wife could not thereafter attack the decree's validity upon the ground of insufficient domicile. Missouri has reached the same result even though the wife, having appeared in person before the Nevada court, failed to raise the question of domicile. Keller v. Keller, 352 Mo. 877, 179 S.W. (2d) 728 (1944).
31. See note 24 supra.
Missouri was to force this state to place additional emphasis upon the principles of comity, rather than to rely strongly upon the full faith and credit clause. This would be the natural result of the holding in the Haddock case to the effect that the full faith and credit clause did not compel courts to recognize as valid a divorce decree of another state rendered on constructive service, where the defendant therein had never had a matrimonial domicile in that state.

It is difficult to state, with certainty, what effect the decision in Williams I has had upon Missouri law, for during the short interval between the date of this case and Williams II, no decision was handed down by the Missouri Supreme Court on facts exactly in point. It should be noted, however, that the United States Supreme Court, in Williams I, declared that the Constitution enjoined full, not some, credit to the judicial proceedings of the sister state; that, therefore, a judgment should be accorded elsewhere the same effect as it had in the state in which it was rendered; and that the question of domicile was not open to attack so long as Nevada’s requirements had been met. Had a Missouri case on this question arisen immediately following Williams I, it might be safely stated, therefore, that Missouri would have changed the grounds of its decision from “comity” to “full faith and credit,” or, at least, would have placed emphasis on each, as had been done in its decisions prior to the Haddock case. It cannot be doubted that Williams I would tend to give assurance to the courts of any state whose policy it had been to recognize the divorce decrees of sister states upon principles of comity.

To determine what effect Williams II shall have upon Missouri case law, it will be necessary to summarize briefly the essential conclusions of the Supreme Court’s holding. As a result of Williams II, a decree of divorce, rendered in a foreign state, is prima facie a valid decree, and the state or the party attacking such decree has the burden of proving that the foreign court granting the divorce lacked jurisdiction of the subject matter because of the petitioner’s fraudulent domicile. Such proof necessitates clear and cogent evidence that the petitioner in the divorce action went to the foreign state for the sole purpose of obtaining a “quick” divorce, with no present intention of remaining permanently or indefinitely therein.

In a review of the Missouri cases, however, one is struck by the realization that this has been the attitude of Missouri ever since Gould v. Crow, decided in 1874. Courts of this state have continually recognized the theory of the “divided res,” i.e., that a spouse may for purposes of divorce establish a separate domicile in

32. Supra note 9.
33. The Keller case, cited supra note 30, may be distinguished upon the facts, as, in that case, the defendant spouse appeared before the Nevada court which awarded the divorce decree.
34. Note (1943) 22 Ore. L. Rev. 362 at 365.
35. Supra note 11.
36. Thus, the development from the Haddock case may be readily perceived. In the Haddock case, the foreign decree was prima facie invalid, and the person claiming the divorce’s validity had the burden of proving that the court granting the decree had jurisdiction.
37. Supra note 15.
another state, and that a decree emanating from that foreign state based upon constructive service will be afforded prima facie validity in this state. To set aside such decree, the constant reverberations in the cases have been that the party attacking the divorce must convincingly prove that there had been "fraud in the very concoction and procurement" of the decree, or, which is substantially to the same effect, that the petitioner in the divorce suit had gone to the foreign state "for the express purpose of obtaining the decree," with no present intention of acquiring a permanent or indefinite domicile in that state. Furthermore, by virtue of its holding in *Wright v. Wright*, it would seem that the Supreme Court of Missouri had displayed the sagaciousness of the prophet, for that opinion and the holding in *Williams II* are based upon identical concepts, namely, that jurisdiction over the *res* in a suit for divorce rests entirely upon the domicile of at least one of the parties in the divorce forum, and that the full faith and credit clause does not prevent inquiry into the bona fides of that domicile. Both decisions are to the effect that the foreign decree of divorce is a conclusive adjudication of everything except the jurisdictional facts upon which it is founded, and that the question of domicile is a jurisdictional fact. However, although a cursory comparison between the language of these holdings might seem to indicate that *Williams II* would, therefore, have no effect upon the Missouri law on jurisdiction for divorce, it must be remembered that, in the *Wright* case, the foreign divorce decree was attempted to be used to set aside a decree for separate maintenance, previously rendered in this state, and all courts have shown an understandable disinclination to recognize an *ex parte* divorce in such instances.

Only one case has come before the Missouri Supreme Court subsequent to the date of *Williams II* to afford assistance in this matter. In *Leichty v. Kansas City Bridge Co.*, the plaintiff claimed to be the widow of a workman who had met his death while in the employ of the defendant, and demanded compensation under the Workmen's Compensation Act. The defendant offered in evidence a record of a divorce decree obtained by the deceased in Kansas upon service by publication. The plaintiff then proved that the deceased had obtained the order of publication by falsely swearing that he did not know plaintiff's address, and that he had given an erroneous "last known" address. The plaintiff further alleged that she was unaware of the divorce until the time of his death, for he had immediately returned to Oklahoma, the matrimonial domicile, and they had lived together as husband and wife. In refusing to accord validity to the Kansas decree, the court declared that a judgment of a sister state may be assailed collaterally on jurisdictional

42. *See note 24, supra*.
43. 354 Mo. 629, 190 S.W. (2d) 201 (1945).
grounds on evidence dehors the record, and that, although the res may be divided and exist in separate states for purposes of divorce, due process requires that reasonable and bona fide effort be made to notify the absent spouse. Upon these facts, the court, therefore, held that the Kansas proceedings were a violation of due process and constituted a fraud upon the Kansas court, vitiating the decree there rendered. *Williams II* was cited as authority.

It may quickly be perceived that the facts of the *Leichty* case bear a striking resemblance to *Keena v. Keena*, yet the Missouri Supreme Court reached a result directly opposed to that of the St. Louis Court of Appeals. Unless, therefore, the *Keena* holding can be put aside upon the bare supposition that the St. Louis court was unwilling to affect the rights of an innocent third party, namely, the petitioner’s second wife, it would seem that *Williams II* has had some effect upon Missouri policy; that the decision has resulted in Missouri’s giving a closer inspection to the decree of the foreign state; and that, if the attacking party places clear and cogent evidence before the court, discrepancies vitiating the decree will be ferreted out.

Summarizing briefly, therefore, although the language of the Missouri courts from *Gould v. Crow* to *Wright v. Wright* has been to the effect that a foreign divorce decree, based upon constructive service on one of this state’s domiciliaries, is presumptively valid and that the party attacking the divorce has the burden of proof that such decree is vitiating by fraud “going to its very procurement and concoction,” only upon two occasions prior to *Williams II* has the Supreme Court of this state refused to give recognition to a foreign decree, and in both instances, the problem of setting aside a Missouri-granted decree of separate maintenance was involved. Therefore, if it has been Missouri’s policy to follow this dictum and to refuse recognition only in fact situations in which a spouse has procured a decree of divorce in a sister state to avoid the payment of support money, it would seem that *Williams II* will have an effect upon Missouri’s later decisions. For, as the holding in the *Leichty* case seemingly indicates, Missouri’s future policy will be to lend a more attentive circumspection to the decree of the sister state being assailed, and to deny that decree recognition whenever it shall appear that the foreign state lacked jurisdiction because of a fraudulently-established “domicile,” or because the requirements of due process had not been complied with—and this, even though a previously-rendered decree of separate maintenance is absent from the statement of facts.

**CHARLES E. DAPRON**

**Provisions of the Missouri General and Business Corporation Act Relating to Treasury Stock**

In 1943 the Sixty-second General Assembly of the State of Missouri enacted a comprehensive revision of the state laws relating to business corporations. In

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44. *Restatement, Judgments* (1942) § 12.


46. See note 27 *supra*.

so doing Missouri kept pace with many other states which have found it necessary to reconsider and revise laws which were enacted before the use of the corporate mechanism became so widespread and complex. Any such act represents not only a clarification of older law, but also a cutting out of "dead wood" no longer pertinent to modern problems, and an attempt on the part of the draftsmen and the legislature to deal with many new problems which have arisen. One of the most controversial of these problems is what to do about treasury stock.

One writer has said that this problem has elicited more discussion than any other phase of corporation law, but that the discussion has all been by one side. Many courts have upheld the right of a corporation to purchase its own stock but in so doing have relied largely on precedent and have made very little effort to justify their position, while those who have discussed the issue in treatises and legal periodicals have almost without exception either condemned outright the purchase by a corporation of its own shares, or else have advocated very severe limitations thereon. The purpose of this note is to examine the adequacy of the provisions of the new Missouri law on this subject. But before discussing the new act in particular, some attention should be given to the general situation in other jurisdictions in Missouri prior to 1943.

It is generally conceded that the majority of American jurisdictions permit a corporation to purchase its own stock when this is done out of surplus or does not impair capital requirements. Professor Dodd has traced the development of the so-called American rule, and has pointed out that as late as fifty years ago it would have been hard to predict just what would become the prevailing view in this country, but that in the early part of this century more and more jurisdictions came to permit the practice. (Missouri was one of these jurisdictions as will appear from the discussion in the next paragraph.) The English courts, on the other hand, have consistently opposed the practice since the leading case of Trevor v.

2. Other states which have enacted new corporation laws in recent years include Ohio (1927), California (1931), Illinois (1933), Pennsylvania (1933), Minnesota (1933), and Nebraska (1941). In 1928 the Commissioners on Uniform State Laws recommended a Uniform Business Corporation Act (now designated a Model Act) which was substantially enacted in the following states: Louisiana (1928), Idaho (1929), Washington (1934), and Kentucky (1946). See 9 U.L.A. 71.


5. 6 Fletcher, Cyclopedia of the Law of Private Corporations, (Perm. ed.) §§ 2845, 2847, 2848, and cases cited.

Whitworth\(^7\) decided by the House of Lords in 1887. The English law on the subject was codified in Sec. 45 of the Companies Act, 1929, 19 & 20 Geo. V, c. 23. The so-called English view has also been followed in some jurisdictions in America where it is known as the "minority" rule.\(^8\) Far from being the minority rule in the field of comparative law, however, it is the almost universal rule outside this country.\(^9\)

Missouri was one of the states adhering to the English rule until 1927.\(^{10}\) In that year a Missouri corporation was given power "to purchase, hold, sell and transfer shares of its own capital stock; provided that no such corporation shall use its funds or property for the purchase of its own shares of stock when such use would cause an impairment of the capital of the corporation or perpetuate a fraud upon its creditors or other stockholders."\(^{11}\) This provision remained in effect until the enactment of the General and Business Corporation Act of 1943. This act, in Sec. 5, permits the purchase of its own stock by a corporation subject only to the limitation that no such purchase shall be made by a corporation "when its assets are less than its stated capital, or when by so doing its net assets would be reduced below its stated capital." Additional provisions permit purchases notwithstanding this limitation for certain limited purposes.

It would seem to be clear that the purpose of the legislature in these two enactments was to depart from the rule adopted by the court and to permit purchases, and yet at the same time to protect creditors. The standard device to achieve this protection is to maintain a certain amount of assets on hand to a figure designated as the stated capital requirement. This is the price which the state exacts for the privilege of doing business in a corporate capacity with immunity from personal liability. The unrestricted purchase of its own stock by a corporation can have a destructive effect on this policy of the law. Thus we find the two most common limitations on the practice are either to require all purchases to be made from surplus, or to allow them only when stated capital will not be impaired.\(^{12}\) But where treasury stock is involved the rights of creditors and stockholders can only be protected if sound law and sound accounting practices go hand in hand,\(^{13}\) since any requirement as to the maintenance of stated capital in-

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7. 12 App. Cas. 409.
8. 6 FLETCHER, op. cit. supra note 5, § 2847.
11. Mo. Laws 1927, p. 387. This section later appeared as § 4940, Mo. REV. STAT. (1929) and § 5343, Mo. REV. STAT. (1939).
12. See the summary of statutory provisions in an editorial appearing in 8 ACCGT REV. 336 (1933). The pertinent part has been quoted in MARPLE, CAPITAL SURPLUS AND CORPORATE NET WORTH (1936) 55-57.
13. For an excellent discussion of the interplay of legal and accounting principles in this field, see the address of Mr. Fletcher Lewis, chairman of the
tact is meaningless unless the treasury stock is properly accounted for. This would seem to be quite clear when one realizes that the purchase by a corporation of its own stock is actually a distribution of a portion of the assets of the corporation to particular stockholders, and that this is done in preference to creditors who have a prior claim on the assets and to other stockholders who are entitled to share pro rata. Treasury stock while held by the corporation is in no sense an asset. The crucial test would be, what is it worth to creditors upon liquidation? Obviously nothing. To be sure, if there is a ready market for the shares, they are a potential asset, but an asset that can be of value only when it is disposed of is a peculiar form of asset! Therefore, it should not be so listed on the corporate balance sheet. Neither should it be listed as a deduction from capital. To do so is to confuse the two meanings of the term. The purchase does represent a reduction of working or operating capital; it is a repayment to a stockholder of "capital" paid in; it does reduce the stockholders' equity or proprietary intereset. But no such repayment should be reflected in a reduction of the "stated" capital which is an arbitrary figure imposed by law representing the amount of the "cushion" which must be maintained for the protection of creditors before assets may be distributed to stockholders, and which should only be reduced in the manner which the legislature has specifically provided. Since the purchase of treasury stock represents a disbursement of a part of the surplus assets of the corporation as does the payment of a dividend, it would be proper to enter the transaction on the balance sheet as a reduction of surplus in the same way dividends paid out are reflected. There are other ways in which treasury shares may be accounted for, but it is essential to see that surplus is proportionately restricted so that it will not again be available for the purchase of stock or the declaration of dividends.

In view of this fact, it would seem that the definition of net assets in Sec. 2(m) of the new act is particularly unfortunate. At best it creates an ambiguous

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special drafting committee appointed by the Chicago Bar Association which prepared and sponsored the Illinois Business Corporation Act (on which the Missouri Act was based), entitled Some Legal and Accounting Questions Presented By The Michigan General Corporation Act, which was published in 8 ACCRO. Rev. 145 (1933).

14. This was expressed forcefully by Glenn, supra note 4, at 638: "Forever do we have to return to this hard realism—when a corporation gives anything for its own stock, the corporation is out an asset. Against that it has left only the possibility that some day, under some circumstances, it may succeed in again getting value back into the treasury to replace the value it has lost, by the process of again selling this 'treasury stock' which meanwhile, in actual truth, represents a void."


16. On the general subject of accounting for treasury shares, see the following: Marple, op. cit. supra note 12, c. 5; GRAHAM AND KATZ, ACCOUNTING IN LAW PRACTICE (2d. ed. 1938) § 89; Lewis, op. cit. supra note 13; Hills, Stated Capital and Treasury Shares (1934) 57 J. ACCTCY. 202; Marple, Treasury Stock (1934) 57 J. ACCTCY. 257; Katz, Accounting Problems in Corporate Distributions (1941) 89 U. OF PA. L. Rev. 764, 779.
situation, and it may impair considerably the usefulness of the limitations set out in Sec. 5. Sec. 2(m) is as follows:

"'Net assets,' for the purpose of determining the right of a corporation to purchase its own shares and of determining the right of a corporation to declare and pay dividends and the liabilities of directors therefor, shall not include shares of its own stock belonging to such corporation, but in such case stated capital shall not include the amount thereof attributable to such shares of its own stock nor shall paid-in surplus include the amount thereof attributable to such shares of its own stock." (Italics mine.)

Does this not permit, in fact almost prescribe, a method of accounting for treasury stock which will create a sort of "revolving fund" by which a surplus once accumulated will be restored over and over again, and in this way permit the purchase of an unlimited total of its own stock by a corporation subject only to the limitation that each purchase shall not exceed the amount of surplus?

The situation may be best illustrated by the use of very simple balance sheet examples. Let us suppose that the X Corporation has a capital of $500,000, that it has liabilities of $100,000, and that its assets are $750,000. This would appear somewhat as follows:

<table>
<thead>
<tr>
<th>Assets</th>
<th>$750,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Stock</td>
<td>$500,000</td>
</tr>
<tr>
<td>Debts</td>
<td>100,000</td>
</tr>
<tr>
<td>Surplus</td>
<td>$150,000</td>
</tr>
</tbody>
</table>

Thus it would appear that if this method is used, the X Corporation would have a full $150,000 to use again for the purchase of its own stock or for the declaration of dividends.

It would seem that the mere statement of such a proposition would carry its own refutation. But does not the language of Sec. 2(m) permit such a practice? If it is argued that although the amount represented by treasury shares is to be deducted from stated capital, still such deduction is only for informational purposes on the balance sheet, and that it never was the intention of the legislature to per-
mit a reduction of the amount of stated capital which the corporation must debit itself with, the answer must be that the language of the statute, when considered with the earlier clause in the same sentence dealing with the amount of assets required for the purchase of stock and the declaration of dividends, carries with it a permissive note.

This is not such a surprising conclusion when it is remembered that until very recent years the carrying of treasury stock as an asset was almost standard accounting practice.\textsuperscript{17} What difference in result is there in carrying such stock as an asset and also retaining it as liability, and doing the converse as the statute provides: not carrying it as an asset but taking a corresponding deduction from liabilities? Could it be that the draftsmen of the Missouri law were attempting to prevent the improper and dangerous practice of carrying treasury stock as an asset, but then nullified their own efforts? In addition to the requirement that treasury stock shall not be listed as an asset, the statute should affirmatively require stated capital to be maintained at its original level unless and until it is reduced in the manner specifically prescribed in Sec. 60 of the act.\textsuperscript{18}

No attempt will be made by this writer to set forth what would be an ideal accounting method since numerous excellent articles have been written in accounting and legal periodicals in recent years on the subject, and expert accountants themselves are in some disagreement as to details.\textsuperscript{19} However, this much can be said: the transaction should be reflected in the balance sheet in such a way that it is clearly shown either that an amount of the original surplus equal to the amount of stock purchased no longer exists, or, if shown as existing, is “frozen” and not available for dividends or further stock purchases until the stock which it represents is converted into a true asset by sale or has been eliminated by a reduction of stated capital in the manner formally prescribed.\textsuperscript{20} If this is kept clearly in mind, there should be no difficulty in preparing a balance sheet which would give adequate recognition to the fact that certain shares of the corporation are not outstanding in the hands of others, and yet would maintain inviolate for creditors and stockholders the prescribed minimum of property for their protection. The Missouri act as it now stands goes only half way: it prohibits carrying treasury stock as an asset, but it does not provide adequately for the maintenance of a stated capital requirement.

GEORGE E. ASHLEY.

\textsuperscript{17} For a survey of eighty corporations, see Holt and Morris, \textit{Some Aspects of Reacquired Stock} 1931-33 (1934) 12 HARV. BUS. REV. 504. Also see Hills, op. cit. supra note 16.

\textsuperscript{18} This was taken care of by the definition of net assets in the Illinois Act. See Ill. Bus. Corp. Act. § § 2 (m) and 6. Ill. Inn. Stat. (Smith-Hurd, 1945) c. 32, § § 157.2 (m) and 157.6. Sec. 2 (m) of the Missouri act is identical with Sec. 2 (m) of the Illinois act with the objectional part (italicized herein) added. Why was this done?

\textsuperscript{19} See note 16 supra.

\textsuperscript{20} See note 15 supra.