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John C. Johnston
University of Michigan Law School

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TRUSTS — RIGHTS OF SUCCESSIVE BENEFICIARIES TO CORPORATE STOCK DIVIDENDS — ORDINARY AND EXTRAORDINARY DIVIDENDS — Testatrix died in March, 1935 leaving 5,471 shares of *N* corporation stock in two trusts with directions that a portion of the income therefrom should be paid to her son during his life with remainder over to another. At the time of testatrix' death the *N* corporation had a large surplus, and had been paying regular quarterly dividends from current income. From April, 1935 to December, 1937 these quarterly dividends were continued at one dollar per share less than was customary, but because of business conditions they were paid partly from the surplus which had accumulated prior to the death of testatrix. These payments from surplus reduced the book value of the stock about seven dollars per share. The trustees petitioned the court for directions as to whether these dividends paid partly from surplus accruing before the time of the trust were to be treated as income and paid to the life beneficiary, or whether they were to be considered a return of capital and paid into the corpus of the trust. *Held*, since the will does not express testatrix' intent in this matter, these dividends are to be treated as ordinary cash dividends, and they are payable to the life tenant as income. *In re Estate of Boyle*, 235 Wis. 591, 294 N. W. 29 (1940).

In considering the question as to the rights of successive beneficiaries of a trust to dividends paid on corporate stock which constitutes the corpus of the trust, the Wisconsin court has, as this case indicates, always followed what is known as the Pennsylvania rule.[1] Under this rule a distinction is made between

[1] There are two other rules followed by American courts in this situation. Under the first, known as the Massachusetts rule, the courts look only to the form in which the dividend is paid, holding that all cash dividends are payable to the term beneficiary as income, and that all stock dividends are payable to the trust as a return of capital. Under the second rule, known as the Kentucky rule, the courts look only to the time the dividends are received, holding that if the dividend is received during the term of

an ordinary and an extraordinary dividend. If the dividend in question is found to be an ordinary dividend, it is allotted to the life beneficiary of the trust irrespective of the source from which it is paid; [2] and if the dividend is extraordinary, it is also given to the life beneficiary unless it is shown that such payment would impair the corpus of the trust, and thus reduce the value of the trust to the remainderman.[3] This rule, however, raises a problem to which the courts have given little discussion, that of distinguishing between an ordinary and an extraordinary dividend. In the *Restatement of Trusts* it is said that this distinction depends upon the facts, circumstances, and nature of each transaction,[4] and then six circumstances are listed as being important in the determination of the question.[5] The court in the present case follows this *Restatement* rule and finds that the circumstances indicate an ordinary dividend. The Pennsylvania courts have held in the same general way that ordinary dividends are those paid at more or less customary rates and uniform intervals.[6] The New York courts use the same approach,[7] although they look to the regularity of the period at which the dividends are paid [8] to see whether a continuing policy is indicated [9] and they are not influenced by the size of the dividend.[10] The courts that have followed this rule have done so for the reason that the equities of the life beneficiary and remainderman demand an exact distribution which cannot be obtained by a "rule of thumb." [11] However, the fact remains that

the life beneficiary, it is payable to him as income, and if it is received before or after his term, the dividend goes to the trust as capital. Neither of these rules makes it necessary to distinguish between an ordinary or an extraordinary dividend. 4 BOGERT, TRUSTS AND TRUSTEES, § 843 (1935).

[2] Earp's Appeal, 28 Pa. 368 (1857); McKeown's Estate, 263 Pa. 78, 106 A. 189 (1919); Waterhouse's Estate, 308 Pa. 422, 162 A. 295 (1932); McLouth v. Hunt, 154 N. Y. 179, 48 N. E. 548 (1897).

[3] Smith's Estate, 140 Pa. 344, 21 A. 438 (1891); Lueder's Estate, 337 Pa. 155, 10 A. (2d) 415 (1940); Matter of Osborne, 209 N. Y. 450, 103 N. E. 723, 823 (1913); Estate of Gerlach, 177 Wis. 251, 188 N. W. 94 (1922); Will of Jenkins, 199 Wis. 131, 225 N. W. 733 (1929).

[4] 1 TRUSTS RESTATEMENT, comment on § 236a (1935).

[5] The circumstances as listed in TRUSTS RESTATEMENT, comment on § 236a at p. 236 (1935) are: (1) whether similar dividends have been paid with regularity in the past; (2) whether such dividends are regularly paid out of current earnings; (3) the frequency with which such dividends are declared; (4) the size of the dividends in relation to the value of the shares; (5) the designation, if any, placed upon it by the directors of the corporation, and (6) the source of the earnings from which the distribution is made. In the instant case the court found that the first, fourth, fifth, and part of the sixth circumstances pointed to an ordinary dividend.

[6] Earp's Appeal, 28 Pa. 368 (1857); Nirdlinger's Estate, 290 Pa. 457 at 462, 139 A. 200 (1927); Opperman's Estate (No. 1), 319 Pa. 455, 179 A. 729 (1935).

[7] Matter of Osborne, 209 N. Y. 450, 103 N. E. 723, 823 (1913).

[8] Matter of Columbia Trust Co., 97 Misc. 566, 163 N. Y. S. 536 (1916).

[9] Matter of Postley, 251 App. Div. 469, 296 N. Y. S. 627 (1937).

[10] Lowry v. Farmers' Loan & Trust Co., 172 N. Y. 137, 64 N. E. 796 (1902); Matter of Postley, 251 App. Div. 469, 296 N. Y. S. 627 (1937).

[11] Earp's Appeal, 28 Pa. 368 (1857); Smith's Estate, 140 Pa. 344, 21 A. 438 (1891).

these very courts have adopted a "rule of thumb," for they use one in distinguishing between the ordinary and the extraordinary dividend, and by applying this terminology they decide whether or not they will make any attempt to apportion the dividend. The result of this inconsistency is that they are leaving an opening through which, by a series of dividends regularly declared at a uniform rate from surplus accumulated before the trust took effect, the remainderman may lose a sizeable portion of the book value [12] of the shares to which he is entitled under the terms of the trust.[13] The New Jersey courts alone have chosen to look through the terminology of "ordinary" and "extraordinary" and to protect the equities of the remainderman in the case of either type of dividend.[14] It must be admitted, however, that there is justification for the other courts' refusal to inquire into the source of all dividends in view of the expense which would be involved in determining rights as to relatively small amounts. So over a course of time the arbitrary result of the rule in some individual cases will be balanced by this consideration of administrative convenience.[15]

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[12] The courts, although in disagreement as to method of apportionment, do agree upon the proposition that the value of the stock to which the remainderman is entitled is not the market value, but the intrinsic or book value. Smith's Estate, 140 Pa. 344, 21 A. 438 (1891); Stoke's Estate (No. 2), 240 Pa. 288, 87 A. 975 (1913); Waterhouse's Estate, 308 Pa. 422, 162 A. 295 (1932); Matter of Osborne, 209 N. Y. 450, 103 N. E. 723, 823 (1913); Matter of Bemis's Will, 123 Misc. 255, 205 N. Y. S. 367 (1924); State ex rel. Coykendal v. Karel, 215 Wis. 505, 255 N. W. 132 (1934).

[13] Bourne v. Bourne, 240 N. Y. 172 at 176, 148 N. E. 180 (1925).

[14] Lang v. Lang's Exr., 57 N. J. Eq. 325, 41 A. 705 (1898); McCracken v. Gulick, 92 N. J. Eq. 214, 112 A. 317 (1920); Hagedorn v. Arens, 106 N. J. Eq. 377, 150 A. 5 (1930); Union County Trust Co. v. Gray, 110 N. J. Eq. 270, 159 A. 625 (1932); City Bank Farmers' Trust Co. v. McCarter, 111 N. J. Eq. 315, 162 A. 274 (1932), affd. in 114 N. J. Eq. 46, 168 A. 286 (1933); Graves v. Graves, 115 N. J. Eq. 547, 171 A. 681 (1934); Bankers' Trust Co. of New York v. Lobdell, 116 N. J. Eq. 363, 173 A. 918 (1934).

[15] The Pennsylvania court has indicated another consideration which makes this rule seem less harsh,—that the life beneficiaries of these trusts are usually the widows or children of the testator, while the remainderman is often a person more removed, and thus not so likely to be a natural object of testator's bounty. Opperman's Estate (No. 1), 319 Pa. 455, 179 A. 729 (1935).