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CORPORATIONS--CAPITAL AND STOCK-RIGHT OF EMPLOYEE TO RECEIVE STOCK DIVIDEND UNDER STOCK PURCHASE AGREEMENT

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Corporations—Capital and Stock—Right of Employee to Receive Stock Dividend under Stock Purchase Agreement—Defendant’s decedent, X, was executive vice-president and treasurer of plaintiff corporation. Intending to increase X’s compensation, plaintiff drew up a plan calling for the sale of 100 shares of plaintiff’s stock to X, plaintiff to have a lien on the stock certificate made out in X’s name and the right to credit all dividends declared on the stock against its purchase price until fully paid. X was granted the right to vote the stock and to receive the dividends declared after full payment. The agreement specifically provided that X was not entitled to possession of the certificate, that the shares were to represent a personal, non-transferable
interest of the employee, and that the plaintiff could repurchase such interest either upon X's death or the cessation of his employment. X accepted the plan, dividends were declared and credited upon the price of the stock, and a stock dividend in X's name of 300 shares was declared. X died before the purchase price of the original stock had been fully credited to him. Conceding its liability for the cash dividend credits up to the time of death, plaintiff demanded that in pursuance of the original agreement defendant administrator release his interest in the certificate representing the stock dividend. The demand was refused. On plaintiff's appeal from a decree denying specific performance of the agreement, held, reversed. W. O. Barnes Co. v. Folsinski, 337 Mich. 370, 60 N.W. (2d) 302 (1953).

A well-known distinction between a cash and a stock dividend is that the latter does not sever and transfer property from the assets of the corporation to the stockholder, but involves merely an internal readjustment of the corporation's capital structure. By use of an analogy, the court in the principal case was able to apply this distinction to decide the ownership of the stock dividend. The rationale was that X's interest in the stock for either the period of his employment or life plus his power to vote the stock were rights parallel to those of a life tenant under a trust containing corporate stock. Three views exist regarding the manner of distributing such trust dividends to the life tenant and the remainderman. Under the Kentucky view, both cash and stock dividends go to the life beneficiary. By the Pennsylvania view, dividends of both types accumulated before creation of the trust vest as corpus in the remainderman, but those representing earnings during the period of the trust belong to the life estate. However, in the principal case the court applied the Massachusetts rule, which holds categorically that cash dividends under the trust are the property of the life beneficiary, while stock dividends remain as part of the corpus. The applicability of the life tenant-remainderman analogy to this stock purchase agreement has been supported judicially. However, the court's conclusion could have been reached more directly by simply inquiring which party possessed the greater ownership interest in the original stock certificate. Such inquiry is readily answered by the apparent

2 The three approaches are discussed in 12 FLETCHER, CYC. CORP., rev. ed., §§5393, 5398, 5400 (1932), respectively. See also 36 MARQ. L. REV. 124 (1952).
3 Cox v. Gaulbert's Trustee, 48 Ky. 407 at 414, 147 S.W. 25 (1912).
4 Chauncey's Estate, 303 Pa. 441, 154 A. 814 (1931).
5 Michigan adopted the Massachusetts rule in In re Joy's Estate, 247 Mich. 418, 225 N.W. 878 (1929), a case which discusses the merits of all three views. See also 130 A.L.R. 492 (1941) for a similar analytical comparison.
6 This method of reasoning was used in Powell v. Maryland Trust Co., (4th Cir. 1942) 125 F. (2d) 260 (stock dividends held to remain with pledgee in mortgage contract which reserved right to "dividends" to pledgor); Lancaster Trust Co. v. J. B. Mason, 152 N.C. 660, 68 S.E. 235 (1910) (offer to sell shares of stock, reserving dividends to be declared at a certain date, held not to refer to any stock dividends). However, the locus of the "remainder" or corpus interest, and hence the right to stock dividends, is easily debatable in a situation like the principal case where there are two "sales," i.e., a contingent sale with a repurchase agreement.
intention in the stock purchase agreement. Assuming that the parties meant to stipulate expressly X's rights in the stock, then the absence of mention of a stock dividend militates against the defendant's claim. Of course it is arguable that omission of any stock dividend provision evidences the parties' intention to have such dividends simply follow the disposition of cash dividends. The former construction would seem the more reasonable in view of the fact that the raison d'être of the stock purchase plan was compensation for the duration of X's employment, not the transfer to him of a right to maintain a complete and permanent share in the corporate assets. It should be noted that construction of any such agreement containing ambiguity will vary in accordance with its characterization as either a pledge, mortgage, lease, or conditional sale of the stock certificate pending full payment. Specific designation of any one of these types in the agreement may therefore provide a further clue to the parties' intention as to stock ownership.

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