Corporations, Shareholders' Right to Have a Dividend Declared and Paid Out of Surplus

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CORPORATIONS, SHAREHOLDERS' RIGHT TO HAVE A DIVIDEND DECLARED AND PAID OUT OF SURPLUS.—In Dodge v. Ford Motor Co. (Mich. 1919), 170, N. W. 668, the questions were not new, and with one exception, the decision was not unusual, but the sums involved were enormous. The Motor Company was incorporated in 1903, under the general manufacturing incorporating act of Michigan (P. A. 232, 1903), for the manufacture and sale of automobiles, motors and devices incident to their construction and operation, with an authorized Capital Stock of $150,000—$100,000 then paid up, $49,000 in cash, $40,000 in letters patent issued and applied for, and $11,000 in machinery and contracts. In 1908 the stock was increased to $2,000,000 by the declaration of a stock dividend of $1,900,000. Plaintiffs own one-tenth of the stock.

By July 31, 1916, the Company had sold 1,272,986 cars at a profit of $173,895,416; it had paid regular dividends of 5% monthly, 60% or $1,200,000 per annum on its capital stock of $2,000,000, and in addition had paid special dividends of $1,000,000 in 1911; $4,000,000 in 1912; $10,000,000 in 1913; $11,000,000 in 1914; and $15,000,000 in 1915—$41,000,000 in five years. It had also accumulated a surplus in excess of Capital Stock of $14,745,095 in 1912; $28,124,173 in 1913; $48,829,032 in 1914; $59,135,770 in 1915; and $111,960,907 in 1916. Its assets were $132,088,219; and liabilities, other than Capital Stock and surplus, $18,127,312.

The selling price of the car was originally fixed at $900.00, but a policy of annually reducing this had been carried out until the price of $440 per car had been reached in 1914. This price was continued for the year 1915 in order to accumulate a larger surplus with which greatly to enlarge the Company's plant, and various investments for this purpose were made during the year. Approximately 500,000 were sold this year at the $440 price, and a net profit of nearly $60,000,000 made. The directors then proposed to reduce the price to $360 per car, although there was a greater demand at the former price than the Company could supply, and it was practically certain 600,000 cars, with a like profit, could be sold during the year at the former price; in which case the new price would cut the net profits some $48,000,000.

Plans were perfected in 1915-1916, and were about to be carried out for substantially doubling the manufacturing plant at an estimated cost of $9,805,000 for buildings, $5,150,000 for equipment, and $11,325,000 for the construction of a smelter plant to make the iron used in the construction of the cars, the evidence showing that if this was done, the cost of the iron per car could be reduced about fifty percent.

Plaintiffs brought suit to enjoin the carrying out of these projects, and to have a dividend of 50% of the accumulated profits declared and paid to shareholders. They contended:—(1) That the statute limiting the amount of Capital Stock with which a manufacturing company could be incorporated to $50,000,000 made it unlawful for a corporation to accumulate from profits, and use in its business, more than $50,000,000, and the balance over that must be distributed to shareholders. (2) That the building and operation of the smelter would be ultra vires. (3) That the reduction of the price of the car would make competition by others impossible, and thereby create a monopoly contrary to the anti-trust act; and, (4) That a failure to distribute a
large part of the surplus as a dividend to shareholders, by the directors, was a breach of duty on their part.

The trial court held with the plaintiffs upon propositions (1), (2), and (4), and ordered the distribution of one-half of the surplus (after deducting the dividends already declared), as a special dividend to the shareholders, amounting to $19,275,385. The Supreme Court reversed the lower court upon all these propositions except (4), and held there was no monopoly created contrary to the Anti-trust Law as alleged in proposition (3). In ruling as the Supreme Court did upon the first three propositions, it followed substantially all the authority there is.

In affirming the decree of the lower court on proposition (4), the court relied mainly upon facts which showed clearly that more cars could be sold at the price of $440 than the Company could make, and that Mr. Ford exercised a dominating influence over the business and had confessedly adopted an attitude toward the shareholders that, having already received great gains, they should be content with them or their continuance; that the profits were too large; and that by a reduction in the price, these profits should be shared with the public.

The court says, Ostrander, C. J., "A business corporation is organized primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the non-distribution of profits among shareholders in order to devote them to other purposes." "It is not within the lawful powers of a board of directors to shape and conduct the affairs of a corporation for the merely incidental benefit of shareholders, and for the primary purpose of benefiting others." All the judges concurred in the result.

H. L. W.