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Decedents Estates And Trusts—Trusts—Stock Dividends and Stock Splits for Purposes of Distribution Under Trust Instrument

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the funds in question are subject forever to the claims of the decedent's unknown distributees, the state is the only party affected by the Court's decision. Certainly, between the state and federal governments, the latter has, in light of the federal statute, a superior claim to the use and benefit of the funds that arose from its beneficent acts.

**Trusfs—Stock Dividends and Stock Splits for Purposes of Distribution Under Trust Instrument**

In 1918, Wood Fosdick, by deed of trust, created a trust for each of two nieces. He provided that the income from each trust should be paid to the niece for her life and upon her death to a grand niece for life, with the remainder to the settlor if he be living, or to his executor if he be dead. The deed of trust also provided that any and all stock dividends received by the trusts should be turned over to the settlor if he be living, or to his executor if he be dead. The dividends were to be free and clear of all trusts. The settlor has since died and the sole residuary legatee of his estate is the American Museum of Natural History, which, as such, has succeeded to the settlor's interest in stock dividends declared upon stock held by the trusts.

Common stock, issued by General Electric, was included in the stock held by the trusts. In 1954 that corporation wished to reduce the market value of its stock, and to establish a low par value for each share of stock in order to facilitate more frequent and less expensive transfer of its stock. To accomplish these ends the stockholders authorized the corporation to change its thirty-five million no-par shares into one hundred and five million five dollar par value common shares. This necessitated a transfer of earned surplus to capital, which more than doubled the capital account, in order to bring the total capital account up to the new total par value of the outstanding shares. The question presented to the Court in *In re Fosdick* was whether this transaction constituted a stock dividend.

When a corporation capitalizes retained surplus available for dividends instead of distributing it, a stock dividend results. The transfer from surplus to capital

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43. INT. REV. CODE OF 1954 §4321; Treas. Reg. 71 §113.32 (1941). The transfer tax on a sale of no par stock is at the rate of $.05 a share if the sale price is less than $20 per share and $.06 a share if the sale price is more than $20 per share. The transfer tax on a sale of par value stock is at the rate of $.05 per aggregate $100 of par value when the sale is at the rate of less than $20 per share and at the rate of $.06 per aggregate of $100 of par value when the sale is at the rate of more than $20 per share.
44. N.Y. STOCK CORPORATION LAW §38.
is the test of a stock dividend in New York as well as in other jurisdictions. On the other hand a stock split is said to take place when the articles of incorporation are amended to provide that the existing shares of stock be divided into additional share units, without transferring surplus to capital. This distinction is clouded when the division of existing shares is accompanied by a simultaneous or proximate transfer of surplus to capital. It is this situation that faced the Court in the present case.

The Court held that that proportion of new stock representing a transfer of earned surplus to capital constituted a dividend. That amount of the stock held by the trusts which represented the transfer of surplus to capital was therefore awarded to the residuary legatee of the estate of the settlor. The majority, notwithstanding the unusually large amount, both quantitatively and relatively, of surplus transferred to capital, refused to modify the New York rule and concluded that this was a stock dividend according to the settled law of the jurisdiction. It also pointed out that while the test used in New York might not comply with that accepted in the financial world it was not within the province of the Court to alter a definition upon which testators and settlors have relied for many years.

The dissent felt that the Court was unduly formalistic and unrealistic in denominating this corporate action a stock dividend, pointing out that the transaction was received by the financial world as a stock split and that it failed to meet the accepted accounting test for a stock dividend. The dissent

47. 4 White, New York Corporations 34, 35 (12th ed. 1948); Equitable Trust Co. v. Prentice, 250 N.Y. 1, 164 N.E. 723 (1928).
49. Ballantine, Latten, and Jennings, Cases and Materials on Corporations 785 (2d ed. 1953).
52. Ibid.
53. Accounting Research Bulletin No. 43, The American Institute of Accountants. The purpose of a stock dividend is to give the shareholders some separate evidence of their interest in the accumulated corporate earnings without a distribution of cash or other corporate assets. The purpose of a stock split-up is to increase the number of outstanding shares so as to effect a reduction in the market price and thereby obtain improved marketability of the shares. Therefore, where the number of additional shares issued is so great that it may reasonably be expected to have the effect of materially reducing the per share market value, the transaction clearly partakes of the nature of a stock split-up. Generally an issuance of more than 20 to 25 percent of the number of shares previously outstanding will materially affect market value and therefore should be classified as a stock split-up.
further reasoned that it was improbable that this result was intended by the settlor.

While the result in this case reduced the income of the income beneficiaries because of the provision in the trust instrument allocating stock dividends to the estate of the settlor, the operation of the rule of this case in the ordinary trust will cause shares issued in this manner to go to principal. Therefore, in general, this case effects no substantial harm to the beneficiaries of a trust agreement, while following the established law of this state.

DOMESTIC RELATIONS

Separation Agreements—Breach of Covenant Not to Molest

In *Borax v. Borax*, the plaintiff-wife and defendant-husband had a separation agreement containing a covenant that "neither party shall, in any manner or form whatever, molest or trouble the other." It is alleged that the defendant breached this covenant by obtaining a Mexican divorce without jurisdiction, purporting to marry another woman, and giving his name to her child. Based on this alleged breach, the plaintiff brought an action to set aside the existing separation and another action for separation on grounds of adultery or on the grounds of cruel and inhuman treatment.

The Special Term, holding that no molestation was established, dismissed the complaint on the ground that it did not state facts sufficient to constitute a cause of action. The Appellate Division assumed molestation but held that the "molestation clause" was an independent covenant and a breach of this clause was not a rescission of the separation agreement. Their judgment was, therefore, for affirmance, because an existing separation agreement containing a valid and subsisting provision for support and maintenance is a bar to a subsequent action for separation.

Historically, the "molestation clause" was used exclusively to prevent a separated spouse from compelling the restoration of conjugal rights. As the law favors resumption of marital relations, such clauses were of doubtful validity and,