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Wills--Bequest of Stock--Ademption and Rights of Legatee to Stock Dividends [*Warren v. Shoemaker*, 207 N.E.2d 419 (Ohio P Ct. 1965)]

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WILLS — BEQUEST OF STOCK — ADEMPMENT AND RIGHTS OF LEGATEE TO STOCK DIVIDENDS

Warren v. Shoemaker, 207 N.E.2d 419 (Ohio P. Ct. 1965).

A bequest of shares of corporate stock to a legatee is often affected by events occurring subsequent to the execution of a will. A testator may exchange the specific stock bequeathed for other shares of stock as a result of a corporate merger, consolidation, or stock split, or he may be issued additional shares as a stock dividend. When such an event occurs, and the testator fails to make any changes or alterations in his will as to the stock legacy, a question arises as to the distribution of the newly acquired stock upon the death of the testator.

In *Warren v. Shoemaker*,¹ testatrix owned 2,148 shares of common stock in a corporation at the time of the execution of her will. In her will she made a bequest to a legatee of all the stock of the named corporation that "I may own at the time of my death."² Between the execution of the will and the death of testatrix, the named corporation merged with another corporation. As a result of the merger 3,436 shares of common stock in the surviving corporation were issued to the testatrix in exchange for the 2,148 shares she previously held; in addition, she received 463 shares of the new stock in dividends before her death. The probate court of Franklin County held that the gift described in the will was a specific bequest which was not adeemed in this case, but that all stock dividends received subsequent to the merger were to go to the residuary legatee rather than to the legatee of the principal stock.

The court adopted a three-step approach in determining the ultimate distribution of the estate. First, it was necessary to classify the bequest as specific or general. Second, having concluded that the bequest was specific, the court had to determine whether or not it had been adeemed by the exchange of stock. Finally, having decided that the specific bequest had not been adeemed, the question was whether the stock dividends belonged to the legatee along with the principal stock. The court concluded that the shares received as dividends went to the residuary legatee and not with the principal stock. For a better understanding of how the court arrived at these conclu-

¹ 207 N.E.2d 419 (Ohio P. Ct. 1965).

² *Id.* at 420.

sions, an analysis of the common law rules would be of some assistance.

A bequest of shares of stock is usually either specific or general.³ At common law, the courts have shown a tendency to construe bequests as general rather than specific.⁴ Courts have favored general legacies because the rule of ademption⁵ does not apply to them. This follows from the fact that general legacies may be paid out of any available assets in the decedent's estate, even though the will designates a particular fund for their payment.⁶ Several criteria have been established for classifying stock legacies.⁷ Words of possession and words which indicate that the testator bequeathed all the shares in a certain corporation which he may own at the time of his death constitute a specific legacy.⁸ In the subject case, the court concluded that the legacy was specific since it was a particular portion of testatrix's personal estate and was distinct from other parts of the estate. As authority, one Ohio case was cited,⁹ but no further inquiry was made in regard to the legacy classification.

The second consideration, whether there was ademption of the bequest, depends upon a determination of whether the bequest is specific or general. An analysis of the common law cases seems to indicate that where the bequest is specific there is ademption¹⁰ but that where the bequest is general there is no ademption.¹¹ While

³ "A specific legacy is a gift of some specific article or particular fund which the will distinguishes from all the rest of the testator's estate." ATKINSON, WILLS § 132, at 732 (2d ed. 1953). "A general legacy is one which is payable out of general assets of the estate and which does not require the delivery of any specific thing or satisfaction from any designated portion of testator's property." *Id.* at 731.

⁴ See, e.g., *In re Mandelle's Estate*, 252 Mich. 375, 378, 233 N.W. 230, 231 (1930); *In re Snyder's Estate*, 217 Pa. 71, 66 Atl. 157 (1907).

⁵ "A testamentary gift of testator's specific real or personal property is adeemed, or fails completely, when the thing given does not exist as part of his estate at the time of his death." ATKINSON, *op. cit. supra* note 3, § 134, at 741.

⁶ *In re Snyder's Estate*, 217 Pa. 71, 66 Atl. 157 (1907). See also Annot., 63 A.L.R. 639 (1929).

⁷ Such criteria include: (1) the language used by the testator to describe the gift; (2) the nature of the corporation issuing the stock; (3) the amount of stock owned by the testator when the will was executed; and (4) other intrinsic and extrinsic evidence indicating the testator's intent. For a complete discussion and analysis of these criteria, see Paulus, *Special and General Legacies of Securities — Whither Testator's Intent*, 43 IOWA L. REV. 467 (1958).

⁸ *In re Hartman's Estate*, 233 Iowa 405, 9 N.W.2d 359 (1943) ("all the shares in X corporation that I may own at my decease"); *Gorham v. Chadwick*, 135 Me. 479, 200 Atl. 500 (1938) ("my stock in X corporation").

⁹ *Nagel v. Wilcox*, 104 Ohio App. 534, 150 N.E.2d 667 (1957).

¹⁰ See generally Paulus, *supra* note 7.

¹¹ *Ibid.*

the courts often pay "lip service" to the fact that the testator's intent should control in determining the legal effect due to subsequent changes in the legacy, a majority of the cases hold that the question of intent should be limited to the determination of whether the legacy is specific or general.¹² Once the determination is made, the courts apply the rule of law applicable to that classification.¹³ Where there has been a change in stock or corporate structure, a majority of the courts adopt the "substantial identity doctrine" to resolve the issue.¹⁴ Under this rule, a substantial change in the subject matter of a testamentary gift will work an ademption, but a merely nominal or formal change will not.¹⁵ In cases involving a bequest of stock in a corporation later merged or consolidated with another corporation, most courts have regarded such a bequest as specific and not to be adeemed.¹⁶ The theory in these cases is that a change in the form or description of corporate securities does not materially change the true interest of the testator in the corporation. It is generally presumed that the testator intended the new stock to be substituted for the old as the subject of the bequest so as to prevent ademption.¹⁷

In the subject case, the court pointed out that the principles of ademption of securities involved in merger, reorganization, and reconstruction of corporations are not fully settled under Ohio decisions. Following the majority view of the common law cases where such a question arose,¹⁸ the court adopted the "substantial identity doctrine" and held that the bequest was not adeemed. This holding appears to be in line with other Ohio cases¹⁹ which have followed this more modern approach to corporate stock legacies.

The third consideration was whether the specific legatee is entitled to stock dividends received by the testatrix after the merger. Essentially, this involves the more general consideration of stock

¹² See, e.g., *Gardner v. McNeal*, 117 Md. 27, 82 Atl. 988 (1911); 57 AM. JUR. *Wills* § 1405 (1948).

¹³ Ademption applies to specific legacies but not to general ones. See, e.g., *In re McLaughlin's Estate*, 97 Cal. App. 485, 275 Pac. 875 (1929); *Dillender v. Wilson*, 228 Ky. 758, 16 S.W.2d 173 (1929); 57 AM. JUR. *Wills* § 1582 (1948).

¹⁴ *Goode v. Reynolds*, 208 Ky. 441, 271 S.W. 600 (1925); *Clegg v. Lippold*, 123 N.E.2d 549 (Ohio P. Ct. 1951).

¹⁵ For discussion of the rule, see Note, 39 VA. L. REV. 1085 (1953).

¹⁶ *Ibid.*

¹⁷ *Goode v. Reynolds*, 208 Ky. 441, 271 S.W. 600 (1925); *Pope v. Hinckley*, 209 Mass. 323, 95 N.E. 798 (1911); *In re Peirce*, 25 R.I. 34, 54 Atl. 588 (1903).

¹⁸ See Note, *supra* note 15.

¹⁹ See, e.g., *Clegg v. Lippold*, 123 N.E.2d 549 (Ohio P. Ct. 1951).

dividends received after the execution of a will. According to the general common law rule, it is clear that stock dividends do not go to the legatee along with the principal stock, unless a contrary intention is indicated by the testator.²⁰ A majority of those cases which hold that the stock dividends do not go to the legatee look to the capitalization of the corporation issuing the dividend.²¹ The view is taken that the declaration of a stock dividend is nothing more than the capitalization of accumulated profits which otherwise would be paid to the shareholders in cash. As the legatee would not be entitled to receive dividends paid to the testator before death when they are paid in cash,²² he cannot receive them when they are paid in additional stock. In contrast, a minority of the cases hold that stock dividends belong to the legatee as a return of capital which follows the principal stock. One ground for this view is that a share of stock is simply representative of the proportionate interest which each shareholder has in the corporation; a stock dividend really takes nothing from the property of the corporation and adds nothing to the proportionate interest of the shareholders. Therefore, a bequest of a certain number of shares represents the testator's proportionate interest in the capital stock of the corporation, evidenced at the time of death by the shares mentioned in the will together with the new shares issued as stock dividends.²³ In other cases holding that the stock dividend follows the principal stock, the courts found evidence of the testator's intention that the new stock should be included in the bequest.²⁴

In *Warren*, the court was undoubtedly influenced by the previous case law which took the view that a stock dividend by a corporation is nothing more than the capitalization of accumulated profits which would otherwise be paid to the stockholders in cash, a specific legatee not being entitled to cash dividends.²⁵ But consider the rationale of this view if the testator receives cash dividends and reinvests them in

²⁰ *Griffith v. Adams*, 106 Conn. 19, 137 Atl. 20 (1927); *Hicks v. Kerr*, 132 Md. 693, 104 Atl. 426 (1918). See generally Annot., 172 A.L.R. 364 (1948).

²¹ *Ibid.*

²² Cash dividends are generally treated as income belonging to the residuary estate, and not as a return of capital allocable to the principal. See *Griffith v. Adams*, 106 Conn. 19, 137 Atl. 20 (1927); *Hicks v. Kerr*, 132 Md. 693, 104 Atl. 426 (1918).

²³ *Succession of Quintero*, 209 Ia. 279, 24 So. 2d 589 (1946).

²⁴ The words "my stock" or "all my stock" as used by the testatrix in specifically bequeathing stock owned by her, evidenced an intention to bequeath all the stock owned by her at the date of death. *In re Good's Estate*, 145 Misc. 431, 260 N.Y.S. 292 (Surr. Ct. 1932). *Accord*, *Heckler v. Young*, 264 Ill. App. 34 (1931); *Butler v. Dobbins*, 142 Me. 383, 53 A.2d 270 (1947).

²⁵ See note 24 *supra*.

more shares of stock in the same corporation prior to his death. If, according to the terms of the will, a legatee is entitled to all the stock a testator owns in a named corporation at the time of his death, it seems that he should be entitled to additional shares of stock purchased, even if they are purchased out of cash dividends.

A few Ohio cases have followed the common law minority view that a stock dividend is not income because it really takes nothing from the corporation and adds nothing to the interest of the shareholder.²⁶ The explanation is that each shareholder has the same proportional property interest in the corporation after the dividend that he had before the dividend. Therefore, stock dividends are really part of the principal and belong to the legatee. Ohio corporation law seems to support this view, because by statute a stock dividend may be made from any surplus, however created.²⁷

In holding that the stock dividends should go to the residuary legatee, the court in *Warren* followed the common law majority rule that stock dividends received by the testator subsequent to the execution of the will do not go to the legatee with the principal stock in the absence of a contrary intention by the testator. There is apparently some confusion among the Ohio courts as to the application of this general rule to the facts of each case.

In the instant case, the court cited only one Ohio case as authority for its holding, failing to recognize that there have been cases to the contrary.²⁸ The facts of *Central Nat'l Bank v. Cottier*,²⁹ the case cited as authority for the holding in *Warren*, can readily be distinguished. There the testatrix bequeathed a specified number of shares of stock to certain beneficiaries. The court found that the respective legatees were limited to the number of shares bequeathed to each of them, and were not entitled to additional stock dividends declared on such stock. The controlling factor in the outcome of that case was that the intent of the testatrix, as expressed in detail in the will, was that stock dividends should become part of the residuary estate

²⁶ *Millar v. Mountcastle*, 161 Ohio St. 409, 119 N.E.2d 626 (1954); *Clegg v. Lipold*, 123 N.E.2d 549 (Ohio P. Ct. 1951).

²⁷ While a stock dividend may be paid out of surplus arising from unrealized appreciation in value of assets, a cash or property dividend may not. OHIO REV. CODE § 1701.33(B).

²⁸ *E.g.*, *Miller v. Mountcastle*, 161 Ohio St. 409, 119 N.E.2d 626 (1954), where the Ohio Supreme Court followed the minority view set forth in text accompanying note 24 *supra*.

²⁹ 163 N.E.2d 709 (Ohio P. Ct. 1958).

and not go to the legatees. The court said each case must stand on the particular instrument involved in light of attendant relevant facts.

It appears, therefore, that the *Central Nat'l Bank* case does not stand for the principle for which it was cited. The final outcome of both cases is the same, but in *Warren* the court failed to make any inquiry into the general intention of the testatrix as the court did in *Central Nat'l Bank*. In the instant case, testatrix's will read: "I give and bequeath to Lulu Shoemaker all of the stock of the W. M. Ritter Lumber Company that I may own at the time of my death. . . . I give, devise, and bequeath all the rest, residue, and remainder of my estate to the North Broadway Methodist Church, or its successor, to have and to hold absolutely."³⁰ A reasonable reading of these provisions would seem to indicate that the testatrix intended to give the legatee all the stock she owned in the named corporation at the time of her death. There is no bequest of a specified number of shares to indicate a limitation on the number of shares bequeathed to the legatee. The words used to make the bequest in testatrix's will follow the standard form commonly used in Ohio to make a specific bequest of this kind.³¹ Had the court inquired into the intent of the testatrix, the result might have been that the stock dividend would have gone to the legatee along with the principal stock.

*Warren v. Shoemaker*³² demonstrates that there is confusion in Ohio probate courts in determining the rights of a legatee to receive stock dividends issued after the execution of a will on shares representing a specific bequest. If the function of the probate court is to distribute the property according to the intention of the testator as expressed in his will, the court in *Warren* seems to have failed. The court merely classified the bequest and applied a general rule of law, making no further inquiry into the intent of testatrix as expressed in the will. But the *Warren* court is not alone in this "error" as a majority of the common law cases have been disposed of in a similar manner.³³

A better policy would be to decide each case on the basis of the instrument involved and the surrounding circumstances. Words such as "my 100 shares of stock in X corporation" might very well

³⁰ *Warren v. Shoemaker*, 207 N.E.2d 419, 420 (Ohio P. Ct. 1965).

³¹ See MERRICK & RIPPNER, OHIO PROBATE LAW § F17.02 (1960).

³² 207 N.E.2d 419 (Ohio P. Ct. 1965).

³³ See note 13 *supra* and accompanying text.

limit the legatee to 100 shares and exclude stock dividends from the bequest. But the words "all my shares in X corporation at the time of my death" suggest that testator intended to include stock dividends received after the execution of the will along with the principal stock in the bequest.

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