

3047.

CORPORATION—DIVIDENDS PAID IN CASH FROM EARNED SURPLUS OF PREVIOUS YEARS CONSTITUTE "INCOME YIELD" UNDER SEC. 5389, WHEN.

SYLLABUS:

Where dividends are declared and paid in cash from the earned surplus in the assets of a corporation, which surplus has been accumulated from profits of the corporation in prior years, such dividends are legal dividends under the provisions of section 8623-38, General Code, although such dividends are paid in part from cash received on a sale of some of the physical assets of the corporation; and such dividends are "income yield" within the provisions of section 5389 and other related sections of the General Code, for the purpose of determining the tax to be paid on the share or shares of stock on which such dividends are paid.

COLUMBUS, OHIO, August 15, 1934.

The Tax Commission of Ohio, Columbus, Ohio.

GENTLEMEN:—This is to acknowledge the receipt from you of a communication which reads as follows:

"The Nivison Weiskopf Company, Reading, Ohio, was prior to the year 1931, a corporation engaged in the business of manufacturing glass, also lithographing and also other activities. During the period of its operation an earned surplus amounting to some \$500,000 was acquired and created.

In the year 1931 the said Nivison Weiskopf Company sold its glass making business for \$150,000, such sum being paid \$60,000 in cash and the remainder in notes due at various dates in the future. Under the terms of this contract the Nivison Weiskopf Company sold all of its licenses, patents and rights relating to the glass manufacturing business, and further covenanted not to engage in the glass making business for a period of ten years from the date of the execution of the contract. The sale, however, did not include the conveyance of the physical assets owned by the said Nivison Weiskopf Company and used prior to that time in the glass manufacturing business. Neither did the sale affect the other activities of the said company and they continued to, and are presently engaged in such other activities.

Subsequent to that sale and in the year 1932 the said Nivison Weiskopf Company declared a dividend to its stockholders payable by the terms of the declaration from the proceeds of that sale. It developed, however, that the cash position of the Nivison Weiskopf Company would not permit the payment of the entire amount of the declared dividend, and for the purpose of securing cash with which to pay such dividend a portion of the physical assets owned by the Nivison Weiskopf Company and used theretofore in the glass making business were sold and the dividend paid from the cash thus received.

As stated above the Nivison Weiskopf Company prior to the time of this sale and prior to the declaration of the dividend in question, had accumulated a substantial earned surplus and after deducting the amount

of the dividend in question from the surplus account, the said Nivison Weiskopf Company still retained an earned surplus of some \$300,000.

The Commission assessed the shares of stock of the stockholders resident of this State for the year 1933, on an "income yield" basis of the amount of the dividend so declared and paid. It is contended, however, by the said the Nivison Weiskopf Company, that the dividend so declared and paid was a liquidating dividend or a return of capital. This contention is based principally on the fact situation existing, and on the theory that the dividend was declared and paid from cash received from the sale of its right to manufacture glass and from the further sale of assets which it had theretofore used in the glass making business, and because of the further fact that the resolution passed by the Board of Directors declaring such dividend, recited that such dividend was paid from the cash received from the sale of such business and such physical assets.

We, therefore, respectfully request your informal opinion as to whether or not the dividend so declared and paid is to be considered "income yield" within the meaning of Section 5389 G. C., or whether such dividend is to be considered one in liquidation or a return of capital, and hence not taxable as "income yield" within the meaning of the above quoted section."

The question presented in your communication is whether the dividends declared and paid to its stockholders by the Nivison Weiskopf Company in the year 1932 are to be considered as "income yield" under the provisions of Sections 5388 and 5389, General Code, with respect to the assessment for taxes for the year 1933 on the shares of stock upon which these dividends were paid.

Under the provisions of Section 5389, General Code, "income yield," as used in Section 5388 and other sections of the General Code relating to the taxation of investments, means in the case of shares of stock, "the cash dividends so paid."

The dividends here in question were paid in cash and the question presented in your communication arises, apparently, solely by reason of the contention of the Nivison Weiskopf Company that the dividend declared and paid by it, in the manner stated in your communication, was a liquidating dividend or return of capital. I cannot agree with this contention made by the company. It quite clearly appears from the facts stated in your communication that this dividend was paid out of earned profits which had been carried into the surplus of this company. Apparently, a very considerable part of the net profits of this company in years past was carried into the surplus of the company instead of being paid out as dividends and that such surplus had taken the form of assets used by the company in the conduct of its business. In this connection it appears that at the time of the declaration of these dividends in the year 1932, the company had in its assets a surplus over capital stock and liabilities of \$450,000 or more, and that after the payment of such dividends, it still had a surplus of \$300,000.00.

Section 8623-38 General Code, which section in a large measure is declaratory of the common law relating to the declaration and payment of dividends by the corporations, provides that a corporation may declare dividends, payable in cash, shares or other property out of the excess of the aggregate of its assets, less the deductions provided for in this section, over the aggregate of its liabilities, plus stated capital. This section further provides that no corporation shall declare or pay a dividend in cash or other property when there is reasonable ground for believing that it is unable, or by the payment of the dividend may be rendered unable, to satisfy its obligations and liabilities.

There is nothing in your communication to suggest any limitation of the right of the corporation at the time here in question, to declare and pay these dividends under the authority of the section of the General Code above noted.

As pointed out by the court in the case of *Mente, Trustee, vs. Groff*, 10 N. P. (n. s.), 148, "the restriction upon the authority of directors to declare dividends out of surplus alone, even in the absence of a specific statute, such as herein, is recognized by practically all of the textbook writers upon corporations and stockholders, and is supported by numerous decisions in other states."

In the opinion of the court in the case above cited, it is further said:

"It is not intended, however, that all of the surplus profits of any year shall be distributed as dividends, that being a matter of discretion with the directors having full knowledge of the condition of the business and its future necessities, nor, on the other hand, are the directors prohibited from declaring dividends out of accumulated surplus profits of previous years, even when there has been no surplus profits for the particular year in which the dividend was declared."

The court in this connection, quoting from Section 546 of Cook on Stock and Stockholder, said:

"Profits earned and accumulative in times of prosperity may properly be paid out of dividends subsequently at a time when no dividends have been earned."

There is nothing in the facts stated in your communication to lead to the view that the business of this corporation has at any time been other than prosperous. However this may be, the fact remains that the dividends here in question were legal dividends paid out of the profits of the company which had been accumulated as a surplus; and such dividends are, accordingly, to be considered as "income yield" for the purpose of assessing for taxes the shares of stock of this company upon which such dividends were paid.

Respectfully,

JOHN W. BRICKER,
Attorney General.

3048.

COUNTY—MAY NOT PAY COLLECTION FEE TO DEPOSITORY ON CHECKS DRAWN ON OTHER BANKS WHEN—PLEDGING OF SECURITIES BY SAID DEPOSITORY.

SYLLABUS:

1. *A county may not legally pay to a depository bank a collection fee on checks drawn upon other banks and received by the county treasurer for taxes, where the depository bank accepts such checks for collection only.*
2. *There is no authority for the pledging of securities by a depository bank with the county to cover such checks during the process of collection.*