is, by its very terms, applicable to goods not yet at Evansville, when the contract takes effect.

We are of opinion that the argument of the defendants in error, upon which the judgment below was based, that the exemption from liability by fire was limited to fire occurring after the cotton had been received at and shipped from Evansville, was erroneous. The exemption covers the entire route.

JUDGMENT REVERSED, and judgment upon the demurrer ordered in favor of

THE PLAINTIFFS IN ERROR.

BAILEY v. RAILROAD COMPANY.

1. In December, 1868, a railroad company, which was in existence in 1862, and before, but which by its charter was limited to 10 per cent. dividends on its capital, now all taken, reciting that it had "hitherto expended of its earnings for the purpose of constructing and equipping its road, and in the purchase of real estate and other properties with a view to the increase of its traffic, moneys equal to 80 per cent. of its capital," and reciting further that the stockholders were "entitled to evidence of such expenditure and to reimbursement of the same at some convenient future period," resolved to give them and did give them in proportion to the amount of stock held by them respectively, certificates which it called "interest certificates;" which certified that A. B. "being the holder of —— shares of the capital stock of the company, was entitled to $——, payable ratably with the other like certificates, *at the pleasure* of the company out of its future earnings, with dividends thereon at the same rates and times as dividends should be paid upon the capital stock of the company." The "certificate" was declared to be transferable on the books of the company, and had a transfer in blank at the foot of it, in the form common at the foot of certificates of stock, with an appointment in blank of an attorney to transfer.

Held, that this was a "dividend in scrip," within the twenty-second section of the Internal Revenue Act of June 30th, 1864, as subsequently amended, which enacts that "any railroad company which may have declared any *dividend in scrip* or money due or payable to its stockholders as part of the earnings, profits, income, or gains of such company, carried to the account of any fund, or used for construction, shall be subject to and pay a tax of five per centum on the amount of such

dividends or profits, whenever and wherever the same shall be payable;" and which authorized the company making such dividend to withhold the five per cent. tax.

2. The said company having declared, in February and August, 1869, two dividends on these certificates, as well as on its stock, and having paid a tax of 5 per cent. on all the dividends, without any suggestion by the revenue officers that any further tax was due, became, in February, 1870, under legislative authority, consolidated with another company; the statute under which the consolidation was effected, enacting that it should be lawful for the old company "to merge and consolidate its capital stock, franchises, and property" with the other company which it was proposed to become united with; but enacting also "that the rights of all creditors of and all liens upon the property of either of said corporations shall be preserved unimpaired, and the respective corporations shall be deemed to continue in existence to preserve the same; and that all debts and liabilities incurred by either of said corporations (except mortgages) shall thenceforth attach to such new corporation and be enforced against it."

Held, that the new company was liable to the five per cent. tax on the dividend in scrip, which the old one was bound to pay. And the new company having paid it under protest, to save its property from being sold on a levy for it; *held* further, on *assumpsit* brought by the new company against the collector to recover back the money, that the dividend in scrip having been decided to be a proper subject for the five per cent. tax, and the company—notwithstanding a violation of its own duty in making, without demand, a return of the dividend—having had, in fact, a full hearing before the officers of internal revenue, and obtained thereby a large abatement from the tax as originally assessed, this court would not suffer a recovery by the railroad company against the collector, because, in compelling payment of the tax, he had not conformed with certain proceedings of form intended to secure a full hearing to taxpayers, which the act made it lawful and perhaps proper for the assessor to do before resorting to the ulterior measure of levy on the company's property.

3. On a question whether the so-called "interest certificates" were taxable as a dividend in scrip, evidence from the Reports, both of the old and of the new company, was allowable, to show that from the time the "interest certificates" were issued up to the time of the suit, dividends were declared and paid on them, just as on the company's capital stock.

ERROR to the Circuit Court for the Northern District of New York; the case being thus:

The 22d section of the Internal Revenue Act of June 30th, 1864,* enacts:

* 13 Stat. at Large, 284, as amended by the Internal Revenue Act of July 13th, 1866; 14 Id. 138.

Statement of the case.

"That any railroad company that may have declared *any dividend in scrip or money*, due or payable to its stockholders, as part of the *earnings, profits, income, or gains* of such company *carried to the account of any fund or used for construction*, shall be subject to and pay a tax of 5 per centum on the *amount of all such dividends* or profits, whenever and wherever the same shall be payable; and said companies are hereby authorized to deduct and withhold from all *payments* on account of any *dividends, due and payable*, as aforesaid, the tax of 5 per centum.

"And a list or return shall be made and rendered to the assessor, on or before the 10th of the month following that in which said dividends *became due and payable*, and as often as every six months; and said list or return shall contain a true and faithful account of the amount of tax, and there shall be annexed thereunto a declaration of the president or treasurer of the company, under oath or affirmation, that the same contains a true and faithful account of said tax.

"And for any default in making or rendering such list or return, or in the payment of the tax aforesaid, the company making such default shall forfeit as a penalty the sum of $1000."

The fourteenth section of the act thus enacts:*

"If any person shall not deliver a monthly or other list or return by the time required by law; or if any person shall deliver or disclose to any assessor or assistant assessor any list, statement, or return, which in the opinion of the assessor is false or fraudulent, or containing any understatement or undervaluation, it shall be *lawful* for the assessor to summon such person, his agent, or other person having possession, custody, or care of books of account containing entries relating to such person, to appear before such assessor, produce such books at any time or place therein named, to give testimony, to answer interrogations under oath or affirmation respecting any objects liable to tax as aforesaid on the lists, statements, or returns thereof on any trade, business, or profession liable to any tax as aforesaid; and the assessor may summon as aforesaid any person residing or found within the State in which his district is situated; and when the person intended to be summoned

* Section fourteen of the act of June 30th, 1864 (13 Stat. at Large, 226), as amended by the ninth section of the act of July 13th, 1866, 14 Id. 138.

does not reside, and cannot be found within the State, then the assessor may enter any collection district where such person may be found and there make the examination, hereinbefore authorized, and to this end he shall have and may exercise all the power and authority he has or may lawfully exercise in the district to which he is commissioned. . . . It shall be the duty of the assessor or assistant assessor of the district within which such person may have taxable property to enter into and upon the premises, *if it be necessary*, of such person so refusing or neglecting, or rendering a false or fraudulent return, and to make, according to the best information he can obtain, including that derived from the evidence elicited by the examination by the assessor, and on his own view and information, such list or return, according to the form prescribed, of the property, goods, merchandise, wares, and all articles or objects liable to tax, owned or possessed, or under the care or management of such person, and assess the tax thereon, including the amount, if any, due for special or income tax. . . . And the list or return *so made*, and subscribed by said assessor or assistant assessor, shall be taken and reputed as good and sufficient for all legal purposes."

Section nineteen of the same statute enacts:*

"That the assessor . . . shall give notice by advertisement, in one newspaper published in each county, and shall post notices, &c., stating the time and place where appeals shall be received and determined, relative to any erroneous or excessive valuation. . . . And such assessor is hereby authorized at any time to hear and determine in a summary way, according to law and right, upon any and all appeals by parties who shall appear voluntarily before him, &c. And shall have power to re-examine and determine upon the assessments and valuations, and rectify the same as shall appear just and equitable."

On the 19th of December, 1868—the above-quoted enactment being then in force—the New York Central Railroad—a company having its road between Albany and Buffalo, and which had been in existence since 1853—passed resolutions authorizing the issue of certain certificates to the stockholders of the company, to the amount of 80 per cent.

* 14 Stat. at Large, 102; amending section nineteen of the act of 1864.

of the amount of the capital stock of the company. The company by its charter was restricted to annual dividends of 10 per cent. The certificates were named "interest certificates," and the aggregate amount of them authorized by the said resolutions was $23,036,000. The amount of the capital stock of the company, at the time said resolutions were passed, was $28,795,000, and it was at this time all taken. The resolutions and certificate referred to each other, and all together made the form of the certificate. The following is a copy of the resolutions and certificate:

"THE NEW YORK CENTRAL RAILROAD COMPANY.

"*Whereas*, This company has hitherto expended of its earnings for the purpose of constructing and equipping its road, and in the purchase of real estate and other properties, with a view to the increase of its traffic, moneys equal in amount to 80 per cent. of the capital stock of the company; and whereas, the several stockholders of the company are *entitled to evidence of such expenditure*, and to reimbursement of the same at some *convenient future period*; now, therefore,

"*Resolved*, That a certificate, signed by the president and treasurer of this company, be issued to the stockholders severally, declaring that such stockholder is entitled to 80 per cent. of the amount of the capital stock held by him, payable ratably with the other certificates issued under this resolution, *at the option of the company, out of its future earnings, with dividends thereon, at the same rates and times as dividends shall be paid on shares of the capital stock of the company, and that such certificates may be, at the option of the company, convertible into stock of the company, whenever the company shall be authorized to increase its capital stock to an amount sufficient for such conversion.*"

The certificates were in this form:

THE NEW YORK CENTRAL RAILROAD COMPANY.

No. *Interest Certificate.*

Under a resolution of the board of directors of this company, passed December 19th, 1868, of which the above is a copy, the New York Central Railroad Company hereby certifies that A. B., being the holder of —— shares of the capital stock of said company, is entitled to —— dollars payable ratably with

the other certificates issued under said resolution *at the pleasure of the company out of its future earnings*, with dividends thereon, at the same rates and times as dividends shall be paid upon the shares of the capital stock of said company.

This certificate may be transferred on the books of the company on the surrender of this certificate.

In witness whereof, the said company has caused this certificate to be signed by its president and treasurer, this 19th day of December, 1868.

_____,
President.

_____,
Treasurer.

At the foot of each certificate there was a form of transfer in blank:

For a valuable consideration I, A. B., do hereby sell, assign, and transfer all interest in the above certificate to C. D., and do hereby irrevocably appoint E. F. attorney, to execute a transfer thereof on the books of the railroad company therein mentioned.

The company declared two dividends of $921,440 each upon these interest certificates, payable respectively, February 20th and August 20th, 1869, which were duly returned to the United States assessor, who assessed a tax of $46,072 upon each of them, which tax the company paid. The company also declared two dividends of $1,151,800 each, upon its capital stock, payable, respectively, February 20th and August 20th, 1869, which were also duly returned to the United States assessor, who assessed a tax of $57,590 upon each of them, which tax also the company paid. At the times these dividends upon the interest certificates and upon the stock were returned to the United States assessor, no allegation was made by the officers of the government, that the returns of the said dividends were false, or, that as to them there was "any understatement or undervaluation," or, that there had been any neglect on the part of the company to make a return as to the issue of said interest certificates; or that the said returns should have included the

interest certificates themselves as well as the dividends upon them.

At the time when these certificates were issued and taxes were paid, as for some years before, there existed in the State of New York a railroad company known as the Hudson River Railroad Company; a company having a road running from the city of New York to East Albany, and there connecting by ferry with the road of the New York Central Railroad Company, just above mentioned; the two making a line of transit from the city of New York to Buffalo.

On the 1st of November, 1869, somewhat less than a year after the 80 per cent. "dividend of scrip" above mentioned was made by the New York Central Company, the two roads were consolidated, under a general act of the legislature of New York, into a new company by the name of "The New York Central and Hudson River Railroad Company."

The act under which the consolidation was made, enacts that it shall be lawful for any railroad company "to *merge and consolidate* its capital stock, franchises, and property with the capital stock, franchises, and property of any other company."

The fifth section of the act provided that—

"The rights of all creditors of, and all liens upon, the property of either of said corporations, parties to said agreement and act, shall be preserved unimpaired, and the respective corporations shall be deemed to continue in existence to preserve the same, and all debts and liabilities incurred by either of said corporations, except mortgages, shall thenceforth attach to such new corporation, and be enforced against it and its property to the same extent as if said debts or liabilities had been incurred or contracted by it."

On the 26th of February, 1870, fourteen months after the certificates were authorized, and nearly four months after the consolidation of the New York Central Railroad Company with the Hudson River Railroad Company, the United States assessor sent a notice, directed to "Charles Wendell,

Esq., Acting Treasurer, New York Central Railroad Company," and dated—

ASSESSOR'S OFFICE, FOURTEENTH DISTRICT, N. Y.,
ALBANY, February 26th, 1870.

SIR: I am directed by the commissioner of internal revenue, &c., to cause an assessment of taxes against the *New York Central Railroad Company* upon the scrip dividend, issued by resolution of the board of directors of said company, December 19th, 1868.

I am also requested to furnish the supervisor the names of persons to whom such scrip was issued. Will you please furnish me with the amount of such dividend, and the names of the persons to whom the scrip was issued?

Respectfully,
R. P. LATHROP,
Assessor.

CHARLES WENDELL, ESQ.,
Acting Treasurer of the New York Central Railroad Company.

The assessor received no answer from Mr. Wendell, nor from the New York Central Railroad Company in reply to the foregoing notice.

On the 3d of March, 1870, more than four months after the consolidation, and more, considerably, than a year after the "dividend" above mentioned had been made, the assessor of internal revenue for the district of Albany, where the New York Central Railroad Company had had its principal office, made what he called, and asserted to be, an "assessment" against *that* company. The document ran thus:

UNITED STATES INTERNAL REVENUE.

Assessment against the New York Central Railroad Company.

The New York Central Railroad Company having failed to make return of the scrip dividend, or interest certificates, voted at a meeting of the directors of said company, held December 19th, 1868, as required to do by section 122, act June 30th, 1864, act July 13th, 1866, internal revenue laws.

Now, therefore, by the authority vested in me, and as required by the several sections of said internal revenue laws, I

do assess against the president, directors, and company of the *New York Central Railroad*, the following tax, to wit:

Capital stock, December 19th, 1868, . . .	$28,795,000 00
Scrip dividend, or interest certificates, being 80 per cent. of said capital, ...	23,036,000 00
Tax on same at 5 per cent., ...	$1,151,800 00
Penalty for failure, ...	1,000 00
Amount of tax, ...	$1,152,800 00

R. P. LATHROP,
Assessor, Fourteenth District, N. Y.

ALBANY, March 3d, 1870.

This assessment was made on the day it bore date by the assessor alone in his office. He made no examination of the books or officers of the company for the purpose of ascertaining whether the certificates were one of the objects liable to tax under the internal revenue law, nor gave notice when an appeal from the assessment could be heard, nor did any other of the things of form prescribed by the above-quoted fourteenth and nineteenth sections of the Revenue Act, as things lawful to be done, &c., in cases where the party liable to the tax had neglected or refused to make a return. He ascertained the amount of the scrip dividend from a document rendered by the company to the legislature of the State.

On an appeal made in February, 1872, from this assessment to the commissioner of internal revenue, that officer held that the company was liable to a tax of 5 per cent. without penalty, on $9,214,400, being six-fifteenths of the entire dividend, the proportionate amount chargeable to the period between September 30th, 1862, and September 30th, 1868. This reduced the assessment to $460,720. And he directed that on payment of that sum the remainder of the assessment, viz., $692,080, including the $1000 penalty, should be abated.

The assessment was accordingly reformed; but the New York Central and Hudson River Railroad Company still declined to pay it. The matter being referred by the reve-

nue bureau to its solicitor, this officer gave it as his opinion that the certificates were not taxable at all. It was afterwards submitted to Mr. Orton, former commissioner of internal revenue, Mr. Smyth, former supervisor of the same, and to the assessor who, under direction, had made the assessment; and these officers concurred in opinion with the solicitor. For the sake of having the matter judicially decided, the collector thereupon, under three different warrants, reciting that "The New York Central Railroad Company, OR the New York Central and Hudson River Railroad Company" had become liable to the tax, seized a large number of the last-named company's locomotives and cars, and was proceeding to sell them, when the amount claimed was paid under protest. The company now sued the collector in assumpsit to get back the money.

In the course of the trial the counsel of the collector offered to read from the reports of the New York Central Railroad Company for the year 1869, and from the reports from the New York Central and Hudson River Railroad for the years 1870, 1871, and 1872, for the purpose of showing that the interest certificates were merged in the capital stock of the defendant in error in 1872, and that dividends were declared and paid on such interest certificates in 1869, 1870, and 1871, the same as upon the capital stock.

The counsel for the latter company, the plaintiff, objected to the evidence as incompetent and irrelevant, upon the ground that it was immaterial what was done with the certificates after they were issued; that the question was whether they were taxable by their character and in the circumstances existing at the time they were issued.

The court sustained the objection; the counsel for the collector excepting.

The case being closed, the court charged:

"Dividends are included as a well-known indicia of the income of corporations, and constitute the profits divided by them after paying the expenses of their business and operations. They are usually declared in money, but as they are sometimes declared in stock, and known as scrip dividends, and as when

Statement of the case.—Charge of the court below.

so declared they represent income as profits which are apportioned to stockholders in stock instead of in money, Congress, intending to reach income in every form, subjected to tax 'dividends in scrip or money.' The inquiry then is, were the interest certificates, as issued by the company, a stock dividend? If they conferred on the respective stockholders any greater interest in the earnings or capital of the corporation than they had before receiving them, then they were a stock dividend though called 'interest certificates.' If they did not, they are not a stock dividend. Congress did not intend to tax dividends in stock which were not so in fact, and did not seek, while in search of income, to subject to tax that which is not income. In other words, they do not intend to tax, as stock dividends, those myths which, in the process known as watering stock, are sometimes assigned to shareholders of corporations as stock dividends. This intent is apparent from the limitation expressed. The tax is imposed on dividends declared in scrip or money, 'due as part of the earnings, profit, income, or gains of such company.' The certificates issued by the New York Central Railroad Company were issued as representing earnings and profits accruing from the operations of the company, and to that extent meet the requisites of a stock dividend. But did they vest in its stockholders any greater interest in its earnings or capital than they had prior thereto?

"In my judgment they did not. By the certificates and resolutions the stockholders are entitled severally to 80 per cent more of the stock than they had before, 'at the option of the company.' In other words, each stockholder shall have additional stock to that amount if the company shall, in its discretion and at its pleasure, see fit to assign it to him.

"The directors of the company reserve the right to decline, at their volition or caprice, to assign any additional stock. The stockholder receives nothing by the declaration of the resolutions and certificates, but the naked assurance of a possibility which, at some indefinite future period, may result to his advantage. It is in no sense a vested right, capable of enforcement, for he never could compel the company to transfer to him additional stock. It is true that the resolutions and certificates entitle the stockholder to a dividend to be paid on the 80 per cent. 'at the same time and ratably with dividends on the capital stock.' But I fail to see how this, in any manner, inures to his

advantage. The earnings of the company, instead of being applied to dividends on his capital stock, are applied on that and the certificates ratably, and to the extent that he receives a dividend on the certificates, his dividend on the capital stock is reduced. The stockholder derives and the company appropriates no income by the transaction which would not have been derived and appropriated if the certificates had never been issued. Another feature of the certificates is an important one, as marking a wide difference between their legal effects and that of a certificate of stock. The 80 per cent. is not to be paid out of the general assets and earnings of the corporation, neither are the dividends which are thereafter to be made. The dividends to be declared upon the certificates are only to be paid out of the future earnings of the company. Upon a dissolution of the corporation these certificate-holders would receive no part of the assets, except those accumulated from the earnings after the certificates were issued. An assignment of all dividends thereafter to arise upon stock may, in law, amount to a transfer of the stock, because it would entitle the assignee to receive all the original stockholder could have obtained of the assets of the corporation. But a holder of these certificates would have no such right, and would not stand at all in the position of a stockholder towards the corporation in case of a dissolution.

"It is not asserted that these certificates give to the holder the right to vote, and here again in an important feature, these certificates fail to vest the holder with the rights of a stockholder.

"Tested by all the rules by which we are to determine whether these certificates were certificates of stock, and as such entitle the holder to the rights of a stockholder in the corporation, the result is adverse to a conclusion in the affirmative. The tax was intended to be imposed upon gains and profits actually appropriated by the company and derived by the stockholders.

"The section which imposed it authorizes the company to deduct or withhold from all payments on account of any dividend due and payable as aforesaid, the tax of 5 per cent. from the stockholder to whom the same is payable. Can it be seriously asserted that if the New York Central Railroad Company had withheld 5 per cent. of the 80 per cent. from the amount of its dividend next declared after it issued these certificates, and deducted that sum from the dividends due to a stockholder, the

company would have been protected? The stockholder would have insisted that he had received no additional income by reason of the certificates, and it was not intended by the law to tax him through the corporation for that for which he could not be taxed personally.

"Or suppose, again, the assessor had attempted to compel the stockholder to pay a 5 per cent. tax on a sum equivalent to 80 per cent. of his stock in the company, on the ground that the company had not deducted the tax from his dividend, would it not be revolting to common sense to insist that he should pay these certificates as income actually received by him, when he had not only received no income in fact, but had not received that from which he could enforce or derive income in the future by any legal remedy?

"If the certificates did not represent income received by the stockholders, they were not of the character which the law intended to reach, because the dividends subjected to the tax were only those from which, by the act, the corporation could deduct the 5 per cent. imposed on the income of a stockholder, derived by him in the form of a dividend.

"My conclusion is that the tax was erroneously assessed, and the defendant must pay the amount realized by his proceedings.

"Had the tax been assessed upon the 'profits of such company, carried to the account of any fund, or used for construction,' it might have been enforced for the amount actually carried to the fund or used for construction since 1862, when the Internal Revenue Act was adopted."

The court thereupon directed the jury to render a verdict for the plaintiff for the sum of $594,002.89, which the jury did; and judgment being entered accordingly, the collector brought the case here; assigning for error:

1. The action of the court below, on the trial, excluding the report of the New York Central Railroad Company, and the reports of the plaintiff, offered by the defendant for the purpose of showing that the interest certificates were merged in the capital stock of such plaintiff in the year 1872, &c., &c.

2. The instruction of the court that the action of the New York Central Railroad Company, as evidenced by the reso-

lution and certificates issued December 19th, 1868, was not a declaration of a dividend in scrip within the meaning of the United States Internal Revenue Act then in force.

3. The direction given to the jury to render a verdict for the plaintiff for $594,002.89, and the judgment given therefor.

Mr. G. H. Williams, Attorney-General, and Mr. S. F. Phillips, for the plaintiff in error:

I. It will be admitted by opposing counsel that the resolution and certificate witness a dealing between the company and its stockholders, based upon earnings theretofore made, in the course of which a written instrument had been delivered by the company to each of its stockholders as evidence of such earnings, and of their having been expended in constructing and equipping the road and in the purchase of real estate and other properties; also that they were to be reimbursed at some convenient future period; two different methods of redeeming such instrument being left optional with the company, viz., its payment out of future earnings, or its conversion into stock, dividends thereon being in the meantime payable at the same rates and times as upon shares of the capital stock.

(1.) The paper, therefore, is upon its face evidence for each stockholder to persons with whom he may deal against the company—

(*a*) Of previous earnings;

(*b*) Of the expenditure (or investment) of such earnings to a specified large amount, in construction, equipment, and purchase of property; and

(*c*) That certain dividends will accrue, *pari passu*, &c., upon the amount specified therein.

(2.) It is also upon its face *notice* to such stockholder and his assignees that the company have a right to call it in whenever it may choose, and either pay it off or convert it into stock.

It is said by the court below that the holder of one or more of these certificates has no rights whatever except to

the dividends mentioned; that for the principal sum mentioned in the certificate he has no promise except the optional one specified therein, and that upon the whole the certificate effected nothing more than the substitution of two bits of paper for one, inasmuch as the stockholder who received it gained nothing by it which he had not before under his certificate of stock.

We submit that, on the contrary, this double option as to dealing with the subject-matter of the certificate does not exhaust the duty of the company to its holder; but that over and beyond such option it owes to such holder a duty arising out of the nature of the transaction, a duty which is, indeed, not technically a debt or an implied absolute assumpsit, but is of like sort with that implied in behalf of those who hold stock, viz., that at all events he shall have a *pro rata* share in the distribution of whatever assets may remain at the dissolution of the company.

It is said also that the transaction did not vest in its stockholders any greater interest in the earnings or capital of the company than they had before.

The same would have been true in the same sense had it been a dividend of stock based upon earnings. The stockholder who had a beneficial interest in a tenth part of the capital would, after receiving a dividend of stock, still have had no more than a tenth. After receiving a dividend of a tenth part of the stock, he would also still have had no greater interest in the road, rolling stock, or other capital of the company than he had before. This would all have remained the property of the *company*, and no part of it have become, because of such dividend, property of the *stockholder*.* We submit that the proposition that dividends transfer to stockholders property which previously belonged to the company is true only of ordinary money dividends, and never of dividends of stock. The subject-matter of a stock dividend is a thing created, *not transferred*, by the *declaration*. It is a *chose*, taking the place of an *aliquot share* in

* Van Allen *v.* The Assessors, 3 Wallace, 584.

capital.* That which a stockholder obtains is not a thing previously held by the company, but is only a definite and formal partition of some beneficial interest in the capital of the company, which previously he had held indefinitely and in common with other stockholders. Of this the certificate is *evidence*.

Indeed, even of dividends in money the stockholder acquires no new property by the dividend. Before being declared it was his; though not set apart from capital, nor passed into his specific control.

Again, it is said that dividends of stock do not *per se*, as intimated, entitle the holder to any additional vote in a company. Whether they do so in any particular case depends upon the charter. The question now before the court cannot turn upon matters merely incidental to stock, but depends upon the nature of stock *per se*. So far as a stockholder is a member of the company he has such right, but this right does not necessarily increase with an increase of stock or lessen with its diminution.†

Again, the test applied by the court below, *i. e.*, a deduction or withholding of the tax paid by the company from all payments to the stockholder on account of any dividend, &c., would have the same bearing upon a stock dividend as upon the transaction under consideration.

The only point in which, as occurs to us, it seems questionable whether what is objected by the court below to the present transaction as a subject of taxation, is not to be objected as well to a dividend of stock, is that of the rights of the holder of the certificate, as such, to a share in the assets after a dissolution of the company.

Even here it seems not difficult to maintain that the holder of such certificate is entitled, upon such dissolution, in case the assets remain as at the time of its issue, or be increased to the eighty dollars mentioned upon its face. Whether upon the diminution of such assets the certificate-holders would be *postponed* to the stockholders seems unnec-

* Frazer *v.* Seibern, 16 Ohio State, 620.

† Taylor *v.* Griswold, 2 Green (N. J.), 222.

essary to discuss. All that seems material is, to maintain that such certificate-holders had at their issue a trust which attached upon the assets and business of the company, as well for principal as for interest, just as if they had been holders of stock.

The "resolution" before the court speaks of the stockholders as being *entitled* to these certificates, as *evidence* that certain earnings of the road had been invested to a certain amount in that property which ordinarily constitutes railroad capital. We understand that this evidence was intended to be, like that above, evidence to parties outside; evidence upon which bargains might be made and trading done. This interpretation of the provision in the resolution is borne out by the insertion of a transfer clause in the certificate.

Our views are that the company, finding that by the application of previous earnings its capital had increased in substance by eighty per cent., not having that amount in hand in cash, and not being authorized to issue additional shares of stock, pressed also by some motive for enlarging the area of the dividend-yielding subject, devised this method of apportioning amongst its stockholders such additional capital; distributable in the end as its other capital, subject however to a condition, *in favor of the stock*, of being paid off before.

It is said by the court below that if the tax had been assessed upon the "profits of such company, carried to the account of any fund, or used for construction," it might have been enforced for the amount actually carried to the fund, or used for construction, since 1862, &c. Admitting, for the sake of argument, the truth of this proposition, we submit with confidence that where a fund composed of earnings expended (*i. e.*, invested) in construction, &c., or carried to any account whatever, is made the basis of scrip distributed amongst the several stockholders of a company, whatever other term in the revenue law may be applicable thereto, the transaction creates also a partition or distribution, *i. e.*, a dividend, a dividend in scrip.

Argument against the tax.—Assessment in violation of statute.

We find no case which bears much resemblance to the present. But three, to which we refer, seem to throw light upon one or other of the points under discussion.*

II. We dismiss the first assignment of error with the suggestion that the important point being the meaning of the transaction of December, 1868, any subsequent dealing of the parties thereto calculated to throw light thereupon is competent evidence of such meaning, and is one of the ordinary instruments of proof. If in 1872 the New York Central and Hudson River Railroad Company, as representative of the old New York Central Railroad Company, converted these certificates into stock, and thereby secured to some extent dividends thereon, such act is evidence that the parties to the transaction of 1868 regarded such certificates as conveying to their holders more than a mere estimate of the future business of the company and its probable future dividends.

Messrs. Roscoe Conkling and S. T. Fairchild, contra:

1st. *The issuing of the certificates by the New York Central Railroad Company, on the 19th of December, 1868, was not the declaration of a dividend in scrip, such as is made taxable by section 122 of the Internal Revenue law.*

To fall within the section, certificates must be—

1st. "A dividend."

2d. A dividend "due or payable"—due or payable at some time fixed or determinable.

3d. A dividend of part of the earnings, profits, income, or gains of the company.

4th. A dividend of earnings, profits, income, or gains, acquired within the year preceding the assessment, or at least a dividend falling within the year.

What is a dividend? Is it not something set apart to be divided, and divided at the time? Can it be a mere agreement to divide in future, contingently and conditionally, or

* Minot *v.* Paine, 99 Massachusetts, 101; Boston and Lowell Railroad Company *v.* Commonwealth, 100 Id. 399; Brown *v.* The Lehigh Company, 49 Pennsylvania State, 270.

even positively? To make a dividend, must not a corporation part with something it has, and must not the stockholder get something he had not before? Must not something before belonging to the corporation as a whole, pass over by distribution to the stockholders in severalty? Must not a debt be created as against the corporation by the declaration of a dividend?

There was in law and in fact, at the time that these certificates were issued, nothing to divide. There were no moneys belonging to the company on which they were based, or with which they could be paid. The earnings, as the certificates state, had been expended for the purpose of constructing and equipping the road, and in the purchase of real estate, &c.

There was no power to create or divide stock. All the stock had been divided before.

It cannot be argued that the corporation had at the time divisible property to answer the certificates.

No *debt* was created. There is no room to suppose that the idea or semblance of a debt entered into the transaction, because a debt or obligation might have robbed the shareholders, by absorbing the future moneys and earnings of the company, and by taking precedence of the stock. Such a debt would, indeed, have imperilled the stockholders' possession of the road itself.

That these certificates, or rather that certificates more efficacious than these, created no debt or obligation, was decided in the cases of *The Sun Insurance Company* v. *Mayor of New York*,* *Mutual Insurance Company of Buffalo* v. *Erie County*,† *People, ex rel., &c.* v. *County of New York*.‡

These interest certificates bear no resemblance to stock. Stock represents capital,—principal. Stock has absolute and ultimate force and value between the corporation and the holder. Each share of stock is the title to an aliquot part of the assets and property of the corporation. Whenever the corporation is wound up the assets belong abso-

* 4 Selden, 241. † 4 Comstock, 442. ‡ 16 New York, 424.

lutely and wholly to the stockholders; and while the corporation continues the stockholders govern and own it. Not so with the certificates and their holders. While the corporation lives the holders of certificates do not vote, or govern, or own it. They have no claim on it in any event, except for interest on their certificates, if interest is in future earned, and even that is contingent. And when the corporation dies, they have no claim on it for anything, and no ownership or interest in its assets at any time. If a stockholder owns also a certificate, he does not, at the dissolution, receive a cent more for his certificate than he would have done had the certificates never been issued. If one not a stockholder becomes owner of a certificate, he acquires no ownership in the capital or assets during the life or at the death of the corporation.

The company in issuing these certificates parted with no control over any property that it had. A stockholder acquired no interest whatever in anything that he did not have before, except in another piece of paper; another evidence of his joint ownership in property that he had a joint ownership in before, and to the same extent precisely. These certificates and the stock certificates represent the same property, real and personal, of every description, after the certificates were issued that the stock certificates represented before.

If these certificates had never been issued, the stockholders would have received precisely the same dividends upon their stock that they now receive upon their stock and interest certificates. It would have been a dividend of the net profits of the company distributed among the stock certificates instead of being distributed between the stock certificates and the interest certificates.

In short. Of principal, the certificates have none; of ownership in the corporation, there is none; of obligation binding the corporation, there is none. They are but the contingent promise of a shadowy by and by. Something radically different from all this is necessary to constitute a "dividend in scrip."

Argument against the tax.—Assessment in violation of statute.

2. *No assessment was made which the law would tolerate in any case, however clear the liability to tax, even if aimed at the right company and during its existence.*

The statute under consideration, all will admit, is one of the most arbitrary statutes ever enacted by Congress, even in the emergency of war. It is a rigorous, a summary, and a searching statute on the side of the United States. It requires discovery of books and papers, and compels full disclosure, punishing any shortcomings heavily. It denounces a penalty of $1000 for disobedience to the summons of the assessor, or for refusing to produce any books or papers in his judgment necessary. The history of the country has no parallel in legislation to it in some respects, in nearness of approach to the verge of constitutional power. To be defended, it must be preserved from perversion, and must not be stretched by lax construction. It is justifiable by reason of its safeguards and mitigations. Without these, it would be tyrannous, and destructive of the fundamental principles of the Constitution.

The fourteenth and nineteenth sections point out particularly in every case of default as to making returns, the function, power, and duty of the government assessor. These provisions are designed to preserve something, at least in form, of the right to due process of law. They were deemed, by those who enacted them, not only wise and suitable, but exacted by the principles of justice, and by the letter of the Constitution itself.

The assessor then could do only what the statute permitted and directed him to do; and at the time of the alleged assessment, March 3d, 1870, he could do nothing unless the New York Central Company was in default according to the statute. There must have been a time certain when the corporation was bound to make a list or return of a "scrip dividend" of $23,036,000, which return it neglected to make, or made falsely. The default was a fact requisite to give jurisdiction, and a condition precedent to any action whatever by the assessor. Assuming that default had been made, the action of the assessor was illegal and void, be-

cause in disregard of the provisions applicable to the case. In case of default, the act of Congress points out the way, and the only way, in which the assessor may proceed. The alleged delinquent must receive notice and be given a hearing with a view to "*the ascertainment* of liability *to tax.*" An inquiry must be made into the facts, and the assessor or his deputy must view, consider, and determine judicially. Time and opportunity must be given for appeal to the assessor. Every one of these provisions was disregarded, and by a mere *ipse dixit*, without the semblance of assessment or hearing, and without any notice known to the law, requisition was made for $1,151,800, and $1000 penalty for failure.

III. *The so-called assessment, even had it been otherwise good in point of form, was against a company which had no existence.*

The assessment, as will be seen by a reference to it,* is in its terms throughout an assessment against the New York Central Railroad Company; and was made on the 3d of March, 1870. But the New York Central Railroad Company ceased to exist on the previous 1st of November, 1869. At the time of the assessment it had become extinct, in law and in fact. An assessment against it, was an assessment against a dead person. No lien could come from such an assessment; nothing could come from it. It was absolutely void.

Nothing, however, was lost to the United States by the death of the New York Central Railroad Company. If, during its lifetime, it became liable to pay a tax, that "*liability*" lived after the debtor's death. The statute kept it alive and held the new corporation amenable to it. The statute of New York preserved such a debt if it existed, but ascribed it to the new corporation. It could not remain with the old. No *additional* corporation, it must be remembered, was created by the act of consolidation. The old New York Central Railroad Company was not left standing, but the old company was, by the terms of the consolidating statute, "merged and consolidated" in the new. The con-

* *Supra*, p. 611.

solidation obliterated and extinguished each of the old companies. There was no coeval existence of old and new for one moment. The birth of the new was the death of the old.

The effect of this statute and the consolidations under it have often been considered. The bar and the bench of New York have never supposed that the service of process on the New York Central Company after November 1st, 1869, was of any effect whatever. Process was so served for a time in ignorance or inadvertence, but no defence was made, no attention was paid to it, and no fruit ever came of it.

The Court of Appeals of New York construed the act of consolidation in this regard in *Prouty* v. *Railroad Company*.*

The syllabus of the case is as follows:

"Where two or more railroad companies are consolidated, as far as the creditors of one of the original companies are concerned, the consolidated company is the successor of the old company, but in respect to the properties of the other company it is a new and independent company, and such creditors have no claim against it upon their original contracts, but only by virtue of the assumption of the obligations of the old company.

"A subsequent order substituting the consolidated company and its officers as defendants was error, as it made them liable upon the original contracts, and subjected them, and all the funds and property of the consolidated company, to *the restraints adjudged against said old company*."

The opinion thus closes:

"But however clearly it may appear that the plaintiff and those in whose behalf the action purports to be brought are entitled to such a remedy, it can legally be obtained only in an action against the parties named, that is, the new company, founded upon their assumption of the liabilities of the other, and not by the summary process of a motion to insert their names as defendants, and then apply," &c.

Thus, bringing a suit against the old company after consolidation, and substituting a new one, was held to be wrong;

* 52 New York, 363.

yet that is the sort of operation which has been attempted here. The assessment is against the old company. The levy was, in fact, on the property of the new.

The principle of the decision above quoted, as well as its application to our case, is plain. When a corporation dies, it has no board of directors or agents. There is no authority to speak or act for it, or to employ an attorney to speak or act for it. All this is true if the corporation be simply extinguished; is it not more manifest when the law creates and names a corporation to take its place, and to be liable and responsible in every case in which the defunct corporation was liable in its lifetime?

The words of the consolidation act, "and the respective corporations shall be deemed to continue in existence to preserve the same," do not help the case of the other side. What is "preserved" by these words? "The rights of creditors," where they exist; and also "liens," where they exist. The words do not create a lien, and do not transfer or transplant a lien from the property of one to the property of another.

IV. *But if a dead corporation be suable, and assessable, still the distraint in this case was illegal. The seizure was of the property of the defendant in error, on an assessment against another person.*

By adverting to the notice of assessment* it will be seen, as we have just said, that it purports, in terms throughout, to be against the New York Central Railroad Company. The New York Central and Hudson River Railroad Company is not named in it. But the seizure was of the goods of the New York Central and Hudson River Railroad Company; a different company from the one which had been assessed. It is not pretended that the locomotives, cars, &c., of the New York Central and Hudson River Railroad seized in 1873 was the property of the New York Central Railroad in 1870. In point of fact we may state that the property seized had no existence in 1870.

* See it, *supra*, p. 611.—REP.

It was the seizure of the goods of one man on a judgment and execution against somebody else.

As respects the reception of the evidence objected to on the trial, we leave it on the ground then stated against its admissibility, to wit, that it was immaterial what was done with the certificates after they were issued; that the question was whether they were taxable by their character and in the circumstances existing when they were issued?

Reply: We have considered that the only important quesiton in this particular sort of case—a suit in assumpsit to recover back a tax because the object taxed was not taxable—was the one which we have argued, viz., whether the transaction of December 19th, 1868, made a "dividend in scrip;" since if it was, it was taxable. As the act of consolidation declared that as to the rights of all creditors the corporations should be continued in existence, the New York Central Railroad Company was the proper party to assess, even after the so-called "merger," for what it had owed and ought to have paid. For the rest, even admitting, *argumenti gratiâ*, the irregularity of the assessment, so far as mere form is concerned, yet if the New York Central and Hudson River Company is really bound for the tax, and on a more formal mode of assessment would have to pay it, the court would not affirm the judgment in the present sort of suit, only because a tax which could be properly collected by the observance of certain forms had been informally got. It would have to affirm the judgment on grounds not going to the merits, but going to form only, and therefore irrespective of merits.

Independently of which, the New York Central and Hudson River Railroad Company suffered nothing by disregard of form. It had an ample hearing, and on the hearing had an immense reduction of the tax as assessed.

Mr. Justice CLIFFORD, having stated the case, delivered the opinion of the court.

Authority to tax the plaintiffs in this case, if it existed at

all, was derived from that clause of the Internal Revenue Act which provides to the effect that dividends declared by a railroad company, in scrip or money, due and payable to their stockholders, as part of the earnings, profits, income, or gains of such company, and all profits of such company carried to the account of any fund or used for construction, are proper subjects of taxation, and that the company declaring such dividends in scrip or money shall pay a tax of 5 per centum on the amount of all such interest or coupons, dividends or profits, whenever and wherever and to whatsoever party or person the same may be payable.

Unless the authority to tax the plaintiffs was derived from that provision it is clear that it did not exist, and it is equally clear that it was not derived from that provision unless the certificates issued by the company to their stockholders are dividends of scrip within the meaning of the act levying the tax in controversy.

Viewed in that light, as the question should be, it is evident that the first instruction given by the court to the jury is the exact equivalent of the second, as it is clear that if the certificates issued by the company to their stockholders are not dividends in scrip within the true intent and meaning of that provision, the taxation of the company was unauthorized by law, and the plaintiffs were, in view of the evidence, entitled to a verdict. These instructions, therefore, may be considered together, and inasmuch as they involve the whole merits of the controversy they will be examined in advance of the exceptions to the ruling of the court.

Sufficient appeared to obviate the necessity for any extended reply to the suggestions that the certificates were not issued by the plaintiffs, or that the assessment was made to one of the old companies, which for many purposes went out of existence when the consolidated company was formed. All of these imaginary difficulties, which were the subject of repeated reference at the argument, are forever silenced by the legislative act of the State under which the plaintiffs came into existence.

By that act it is provided that the rights of all creditors

of, and of all liens upon, the property of the corporations, parties to the agreement and the act, shall be preserved unimpaired and the respective corporations shall be deemed to continue in existence to preserve the same, and all debts and liabilities incurred by either of the corporations, except mortgages, *shall thenceforth attach* to such new corporation and be enforced against it and its property to the same extent as if such debts or liabilities had been incurred or contracted by such new company.*

Apply that rule to the case and it follows that by virtue of that provision the new company formed by the act of consolidation assumed all the obligations of the old companies, except mortgages; or, in other words, that all debts and all liabilities, except mortgages, incurred by either of those companies attached to such new corporation and became enforceable against the same and their property to the same extent as if such debts or liabilities had been incurred or contracted by such new corporation.

Attempt is made in argument to question the soundness of that proposition as applied to the case before the court, and reference is made to the case of *Prouty* v. *Railroad Company*,† as promulgating a rule of decision inconsistent with the theory that the new corporation became liable for the internal revenue tax in question, or that the tax became enforceable against such corporation or their property, but the court here is of the opinion that the case cited supports the proposition that the payment of the tax in question is one of the obligations which the new company assumed when the consolidation became complete, as the liability to such taxation, on the part of the old company, existed before the consolidation was formed, and that the liability to pay the same attached to the new corporation and became enforceable against the same and their property to the same extent as if such liability had been incurred or contracted by such new corporation.

* 2 Sessions Acts of New York, 1869, chapter 917, page 2402.

† 52 New York, 366.

Opinion of the court.

Power was conferred by the legislative act to form the consolidation, subject to the condition that all debts and liabilities incurred by either company, except mortgages, should thenceforth attach to the new corporation and be enforceable against such new corporation and their property, and all the Court of Appeals decided in the case referred to, which is applicable to this case, is that the consolidated company in such a case becomes responsible for the debts and liabilities of the old companies only by virtue of the assumption of those obligations as part of the terms of the consolidation, which is sufficient to show that the theory of the plaintiffs cannot be sustained.

Scrip dividends as well as dividends in money, it must be admitted, are proper objects of taxation under that section of the Internal Revenue Act, and the same section provides that a list or return shall be made and rendered to the assessor or assistant assessor, on or before the tenth day of the month following that in which the interest, coupons, or dividends become due and payable, and as often as every six months, which shall contain a true and faithful account of the amount of the tax, verified under oath by the president or treasurer of the company.

Payment of the tax is required of the company, and for any default in making or rendering such list or return, or of the payment of the tax or any part thereof, the company making such default shall forfeit as a penalty the sum of one thousand dollars, and the assessment and collection of the tax and penalty, in case of such default, shall be made according to the provisions of law in other cases of neglect or refusal.

Except where the stockholder is exempt from such an exaction the tax may properly be assessed against the company required to render the return, and it is the company which is to make the payment and which becomes liable to the penalty in case of default.*

Liabilities of the kind do not attach to the company in

* Barnes *v.* The Railroads, 17 Wallace, 303.

cases where the stockholder is exempt by law from such an exaction, as the same section of the act provides that the company in such a case is authorized to deduct and withhold the amount of the tax from all payments on account of such interest or coupons and dividends, which cannot have any application in a case where the stockholder is by law exempt from any such exaction.*

Exemptions of the kind constitute an exception to the general rule, as the tax, in cases where no such exemption exists, may be assessed against the railroad company.†

None of these propositions are controverted by the plaintiffs, but they insist that the amount which they paid for the tax in this case should be refunded for the following reasons: (1.) Because, as they insist, the scrip in question is not a dividend in scrip within the meaning of the Internal Revenue Act. (2.) Because the assessment was illegal and void even if the scrip is a proper subject of taxation and the assessment is made against the proper party. (3.) Because the railroad company assessed ceased to exist, and became extinct before the assessment was made. (4.) Because the distraint was illegal, inasmuch as the goods of one party were seized to pay a tax assessed against another party.

1. For years the old company had earned moneys greatly in excess of their current expenses without any satisfactory scheme being suggested to render such accumulating surplus available to their stockholders, as they were not authorized to increase their capital stock and were forbidden by law to make dividends for the benefit of the stockholders beyond ten per cent. Difficulties of the kind existing, the excess of earnings beyond current expenses had been expended in constructing and equipping their railroad and in the purchase of real estate and other properties with a view to the increase of their traffic.

Accumulations of the kind had been appropriated in that

* United States *v* Railroad Company, 17 Wallace, 327.

† Stockdale *v.* Insurance Company, 20 Id. 323.

way until the same amounted in the aggregate to a sum equal to eighty per cent. of the capital stock of the company. Dissatisfaction arose among the stockholders, and all admitted that they were entitled to evidence that the excess of the earnings of the company beyond the current expenses had been appropriated in that way, and to reimbursement of the same at some convenient future period.

Motives, such as those recited, induced the company to grant the certificates, and they were accordingly issued to the stockholders, severally declaring on their face that such stockholder is entitled to eighty per cent. of the amount of the capital stock held by him, payable ratably with the other certificates issued under the same resolution, at the option of the company, out of their future earnings, with dividends thereon at the same rates and times as dividends shall be paid on the shares of the capital stock of the company; or they may be, at the option of the company, converted into stock whenever the company shall be authorized to increase their capital stock to an amount sufficient for such conversion.

Interest certificates of the kind were issued as evidence to the stockholders that an equal amount of the earnings of the company beyond current expenses had been expended for the objects stated in the preamble of the certificates, and to show that the respective stockholders were entitled to reimbursement of such expenditure at some convenient future period, and also to show that the stockholders were entitled to dividends on the same whenever dividends were paid on the shares of the *capital stock*, and that the certificates were to be paid out of the future earnings of the company, or to be converted, at the option of the company, into stock, if thereafter authorized to exercise that option.

Such a paper, therefore, by whatever name it may be called, is, upon its face, evidence for each stockholder, to persons with whom he may have dealings, of the amount of the previous net earnings of the company; that such net earnings, to the amount specified, have been expended in constructing and equipping the railroad and in the purchase

of real estate and other properties appertaining to the same, and that the holders of the certificates will be entitled to dividends whenever dividends are paid upon the capital stock.

By the terms of the paper it is stated that it may be transferred on the books of the company, and the form of the transfer is appended to the same, which also shows that the transferee, like the original holder, will be entitled to be reimbursed for the amount of the expenditure therein certified at some convenient future period, unless the company should elect to convert the same into the stock of the company instead of paying the same ratably out of their future earnings.

Stockholders to whom such certificates were issued, it is insisted by the plaintiffs, acquired no rights whatever by virtue of the instruments beyond what they had before, except the right to accruing dividends, but it is clear that the proposition is founded in mistake, as the certificates possessed every quality of stock except that they conferred no power to vote and may be redeemed by payment out of the future earnings of the company. Like stock certificates they are made conveniently transferable, as they may be transferred upon the books of the company, and possess an equal value with stock when used as collateral security or as the basis of credit in any moneyed transaction.

Money dividends could not lawfully be made to exceed ten per cent., and inasmuch as the law of the State forbade the company to increase their capital stock they devised the scheme of issuing these certificates to their stockholders as evidence that such expenditure of the net earnings of the company had been made, in the manner stated, and that the stockholders were entitled to reimbursement of the same at some convenient future period; and in order that the certificates might approximate as near as possible to stock, without exposing the company to the hazard of an actual addition to the same, in violation of law, they provided that the holders of the certificates should be entitled to dividends whenever dividends were paid by the company on the shares

of the capital stock, and that the certificates themselves should either be paid ratably out of the future earnings of the company, or be converted into stock at the option of the company.

Bonâ fide holders of the certificates might demand that the certificates should be paid out of the future earnings of the company, or that they should be converted into stock whenever the company should be authorized to increase their capital to an amount sufficient for the purpose, and that they should have a pro rata share in the distribution of whatever assets may remain at the dissolution of the company.

Stock dividends it is conceded are a proper object of taxation under the Internal Revenue Act, and if so, it is difficult to see why those certificates are not, as they differ from the former only in the fact that they do not confer the right to vote and that they may be cancelled by payment out of the future earnings of the company.

No attempt is made in argument to show that the fact that the company has reserved the right to pay the certificates out of their future earnings exempts them from liability to taxation under that act, and it is clear that the fact that they do not confer the right to vote cannot have any such effect, as dividends in stock do not necessarily entitle the holder to any additional vote. Whether they do so or not depends in any particular case upon the terms of the certificate and the charter of the company.*

Usually a stockholder is a member of the company and as such has a right to vote, but it does not necessarily follow that the right increases with the increase of stock, or that the right is lessened in case the number of shares owned by the stockholder should be diminished.

Net earnings of such a company may be expended or invested in constructing or equipping the railroad, or in the purchase of real estate or other properties, but the investment, whatever it may be, belongs to the stockholders, and

* Taylor *v.* Griswold, 2 Green (New Jersey), 226.

may be distributed, as they may direct, in dividends of stock or of scrip or of money, payable out of the future earnings of the company, or by a sale of property not necessary to effect the purposes for which the company was created.

Deductions such as are authorized by the second clause of the section imposing the tax in this case cannot be made in the case of a dividend of stock any more than in the case of a dividend in scrip, which of itself is a complete answer to the proposition that the certificates are not the proper objects of taxation because they cannot be subjected to such deduction, it being conceded that certificates of stock are the proper objects of such taxation.

Corporation bonds are the representatives of money, because they are issued for sale in negotiable form, but certificates of stock are not securities for money, nor are they negotiable instruments in the strict commercial sense. Like dividends in scrip they are simply muniments of and evidence of the holder's title to a described share or interest in the property and franchises of the corporation, and the dividend in scrip evidences the same extent of interest in such property and franchise as the dividend of stock, except that it is the right of the company to pay the same out of their future earnings, and that the dividend in scrip confers no right to vote.*

Much discussion to show that a dividend in scrip declared by a railroad as part of their earnings, profits, income, or gains is the proper subject of taxation by virtue of the Internal Revenue Act is scarcely necessary, as the express words of the act are that such a dividend "shall be subject to and pay a tax of five per centum whenever and wherever and to whatsoever party or person the same may be payable."†

Taken in a general sense the stock of an incorporated company may be defined to mean the capital of the company in the form of transferable shares of a specified amount, but the word is frequently employed in a much more re-

* Bank *v.* Railroad, 13 New York, 627; Bank *v.* Burr, 24 Maine, 264.

† State *v.* Bank, 11 Ohio, 95.

stricted sense. Stock, when it means anything else than the capital of a corporation, usually refers to the interests of the respective shareholders, and the aggregate of those interests may with propriety in many cases be denominated the stock of the corporation. *

Unless otherwise provided by the charter or by-laws of a corporation the profits and surplus funds of a corporation, whenever they have accrued, are, until separated from the capital by the declaring of a dividend, a part of the stock itself and will pass with the stock under this name in a transfer or bequest.†

Purchasers of stock have a right to claim and receive all dividends subsequently declared, no matter when the fund appropriated for the purpose was earned, whether before or after the transfer and delivery of the certificates constituting the evidence of ownership.‡

As a general rule stock dividends, even when they represent net earnings, become at once a part of the capital of the company, and, of course, entitle the holder to vote, unless it is otherwise provided in the charter or by-laws. Such a dividend, if earned and declared, necessarily increases the value of the old stock if new stock is not issued, and in that mode reaches substantially the same result.§

By the terms of the act a dividend in scrip declared by such a company as a part of its earnings, &c., is subject to the described tax whenever or wherever or to whatsoever party or person the same shall be payable. What is required to be due is the scrip and not the fund, money, or proceeds which it represents. Beyond doubt such scrip becomes operative and due within the meaning of the Revenue Act when it is unconditionally declared without containing any provision postponing its effect.

These certificates are not dividends in money, nor are they

* People *v.* Commissioners, 23 New York, 220.

† Iron Company *v.* Commonwealth, 55 Pennsylvania State, 451; Brundage *v.* Brundage, 1 Thompson & Cook, 90; Phelps *v.* Bank, 26 Connecticut, 269.

‡ March *v.* Railroad, 43 New Hampshire, 515.

§ Railroad *v.* Commonwealth, 100 Massachusetts, 404.

stock or certificates of stock in the strict sense, but they are exactly what they are described to be in the Revenue Act, to wit, dividends in scrip, which entitles the holder to just what he is promised in the instrument, or, in other words, his right must be determined by the contract under which alone he can claim, and that contract is found in the scrip issued by the company.*

Funds set apart as capital out of which debts are to be paid, it is held, amounts to a contract with those who become creditors on the faith of the transaction that the fund shall not be withdrawn and appropriated to the use of the owner or owners of the capital stock, and the court is of the opinion that the vote of the company issuing these certificates is a valid contract of the company with the holders of the certificates that the same shall be paid, at some convenient period, out of the future earnings of the company, unless the company, when thereto authorized, elect to convert the same into capital stock.†

Tested by these considerations it is quite clear that the first instruction given by the court to the jury is erroneous.

2. Suppose that is so, still it is insisted by the plaintiffs that the judgment should be affirmed even if the scrip is the proper subject of taxation, because the assessment, though made against the proper party, is in other respects illegal and void.

Mere irregularities may be passed over without remark, as the suit is an action of assumpsit brought by the plaintiffs to recover back money which they paid to the collector, and the burden is upon them to show that the defendant *ex equo et bono* is bound to refund the amount which they paid.‡ *Indebitatus assumpsit* is founded upon what the law terms an implied promise on the part of the defendant to pay what in good conscience he is bound to pay to the plaintiff.

* Brown *v.* Coal and Navigation Company, 49 Pennsylvania State, 273; People *v.* New York, 16 New York, 427.

† Insurance Company *v.* Mayor, 4 Selden, 250; Same *v.* Supervisors, 4 Comstock, 445.

‡ Swift *v.* Poughkeepsie, 37 New York, 512.

Where the case shows that it is the duty of the defendant to pay, the law imputes a promise to fulfil that obligation, but the law never implies a promise to pay unless some duty creates such an obligation, and more especially it never implies a promise to do an act contrary to duty or contrary to law.*

Throughout the argument for the plaintiffs it is admitted that they never complied with the requirement which made it their duty to make and render a list or return to the assessor or assistant assessor of the interest, coupons, or dividends described in the Internal Revenue Act as the proper objects of taxation.

Complaint is made that the assessor did not pursue the directions of the fourteenth section of the Internal Revenue Act before he made the assessment in this case, but the powers there given the assessor were conferred for the benefit of the United States. Taxpayers, if they make the required return, will have no cause to complain that the assessor did not issue a summons to them or those representing such taxpayer to appear and give evidence upon the subject, or that the assessor did not enter the place where the taxpayer resides and make the examination of his books and papers as authorized by that section of the act. Doubtless he may do so if he deems it necessary, but the tax is not rendered illegal if the assessor omits to procure the necessary information in that way. Steps of the kind may be taken by the assessor or they may be omitted, but he is required to give a written notice to the taxpayer requiring him to render the described list or return within a specified time, and the record shows that the assessor did substantially comply with that requirement.

Due notice of the assessment was also given, and the record shows that the plaintiffs appealed to the commissioner with a degree of success rarely ever surpassed, as it appears that they induced the commissioner to abate six

* Curtis *v.* Fiedler, 2 Black, 478; Cary *v.* Curtis, 3 Howard, 236; Philadelphia *v.* Collector, 5 Wallace, 732; Elliott *v.* Swartwout, 10 Peters, 150; Bend *v.* Hoyt, 13 Id. 267.

hundred and ninety-two thousand and eighty dollars of the tax, or nine-fifteenths of the same, with the whole penalty, though the plaintiffs now suggest in argument that they, if liable at all, are liable for the whole amount. Whether or not they are liable for the whole amount is not a question in this case, but the court is very clearly of opinion that the instruction given by the Circuit Court to the jury that they should render their verdict for the plaintiffs is erroneous, unless it shall appear that there is greater merit in the third and fourth objections to the assessment than is found in the first or the one under consideration.

Irregularity in giving the notice of the assessment is now certainly unimportant, as it is required chiefly to enable the party assessed to appeal and claim a review of the action of the commissioner. Such an appeal having been granted and all rights under it fully exercised and enjoyed, it is now too late to object that the notice of the assessment was irregular.*

3. Enough has already been remarked to show that there is no merit in the third objection to the assessment, as the act providing for the consolidation of the two companies enacts that the liabilities of the old company assessed in this case may be enforced against the new corporation and their property to the same extent as if such liabilities had been incurred or contracted by such new company.

4. Nor is there any merit in the fourth objection to the assessment, as the complaint is the same in principle as that contained in the third, and is decided to be unfounded for the same reason.

Most or all of these objections were sustained by the Circuit Court, and it was in view of their merit and influence that the presiding justice instructed the jury to render a verdict for the plaintiffs. Evidently that instruction is erroneous as well as the first instruction, and for these reasons the judgment must be reversed. Having come to that conclusion it is unnecessary to enter into any extended discus-

* State *v.* Dulle, 48 Missouri, 287.

sion of the exception to the ruling of the court in excluding certain evidence offered by the defendant. Suffice it to say that the court here is of the opinion that the ruling is erroneous; that the evidence was properly admissible as explanatory of the surrounding circumstances.

Judgment REVERSED with costs, and the cause remanded with directions to issue

A NEW VENIRE.

UNITED STATES *v.* O'GRADY.

When the government means to set up any counterclaim to the claim of a party suing in the Court of Claims, as *ex. gr.*, when on a suit under the Captured and Abandoned Property Act, to recover the proceeds of cotton sold under that act, it means to set up a tax, such as what is known as the "cotton tax," it must plead that tax by way of set-off or counterclaim to the suit, as is contemplated by the act of March 3d, 1863; or move for a new trial, under the provisions of the act of June 25th, 1868. It cannot, after judgment has been given for the amount claimed by the petitioner, irrespective of such counterclaim, and without any motion for a new trial having been made, set up and deduct at the treasury the counterclaim when the amount awarded by the decree of the court is asked for there.

APPEAL from the Court of Claims; the case being thus:

By the act organizing the Court of Claims, A.D. 1855, power was given to it to hear and determine all claims *against the United States* founded upon any law of Congress, or upon any regulation of an executive department, or upon any contract, express or implied, with the government of the United States.*

Doubts, however, were suggested immediately upon the act going into practical operation and on suits being brought against the United States, whether the act meant to allow the United States to file set-offs in such suits, and to give jurisdiction to the court to hear and determine them in the

* Act of February 24th, 1855 (10 Stat. at Large, 612).