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TRANSFERS OF CORPORATE STOCK BETWEEN HUSBAND AND WIFE IN KENTUCKY.

Section 2128 of the Kentucky Statutes reads, in part, as follows:

"A gift, transfer or assignment of *personal property* between husband and wife shall not be valid as to third persons unless the same be in writing, and acknowledged and recorded as chattel mortgages are required to be acknowledged and recorded, but the recording of any such writing shall not make valid any such gift or assignment which is fraudulent or voidable as to creditors or purchasers."

Assuming that a husband for a valuable consideration, and while he is solvent, sells his wife certain shares of stock in a Kentucky corporation, and indorses and delivers the certificate to her, and assuming that she delivers said certificate to the corporation and causes the corporation to issue new certificates to her for said stock, can creditors of the husband thereafter subject this stock to their claims against the husband, because the transfer was not acknowledged and recorded? The problem thus presented excludes all questions of fraud.

The statute by its terms applies to "personal property." Ordinarily corporate stock is described as personal property.¹ There is a very real difference, however, between tangible personal property on the one hand, and intangible personal property on the other, and this difference has often been the subject of judicial decision.² No general rule can be safely laid down to the effect that "personal property" as used in statutes means corporate stock, or other intangible property, or that such term does not mean corporate stock and other intangible property. The phrase "personal estate," as used in the statute governing the recording of mortgages, has no application to shares

¹ *Elkhorn Land Co. v. Childers*, 30 Ky. L. R. 1121, 100 S. W. 222.

² *Henderson v. Barrett's Exr.*, 152 Ky. 648, 153 S. W. 992

of stock or other intangible personal property.³ On the other hand, the term "personal estate," as used in the statutes with reference to descent and distribution does apply to corporate stock.⁴ Furthermore, the phrase "other personal property," as used in the exemption statutes, includes choses in action.⁵ It is clear, therefore, that no general rule as to the meaning of the phrase "personal property" can be laid down.

Did the legislature in enacting section 2128 of the Kentucky Statutes mean to require that in order for transfers of intangible personal property between husband and wife to be valid as to third persons such transfers must be evidenced by writing acknowledged and recorded? What was the purpose of this provision? What situation did it undertake to meet?

THE LEGISLATIVE INTENT

Assuming that this very statute has not been conclusively construed by the Court of Appeals, the problem is to determine that most elusive thing, the legislative intent. What did the legislature mean when it used the phrase "personal property" in enacting this very statute? In undertaking to ascertain this intent, we shall apply two tests to the statute: 1. At the time of the enactment of the statute, had the Court of Appeals construed the phrase "personal property" as used in any previous statute on the same subject, or in one so nearly analogous that the legislature is to be presumed to have used the phrase in the same sense in this statute? 2. Can we ascertain the object intended to be accomplished by the statute and conclude what construction will best advance that object?

Both of these tests are recognized as valuable aids in ascertaining the legislative intent. The first test is well recognized:

"Where a statute has been re-enacted in the same or substantially the same terms, the legislature is presumed to have been familiar with its construction and to have adopted it as part of the law, unless the statute expressly provides for a different construction. So where words and phrases employed in a new statute have been construed by the courts to have been used in a particular sense in a previous statute on the same subject, or on one analogous to it, they are presumed, in

³ *Spalding v. Paine's Admr.*, 5 Ky. L. R. 391, 81 Ky. 416; *Schuster v. Jones*, 22 Ky. L. R. 569; *U. S. Bank v. Huth*, 4 B. Mon. 423.

⁴ *Elkhorn Land Co v. Childers*, 100 S. W. 222, 30 Ky. L. R. 112L.

⁵ *Miller v. Mahoney*, 16 Ky. L. R. 799.

the absence of a clearly expressed intent to the contrary, to be used in the same sense in the new as in the previous statute."⁶

The second test has also received approval:

"Every statute must be construed with reference to the object intended to be accomplished by it. In order to ascertain this object it is proper to consider the occasion and necessity of its enactment, the defect or evils in the former law, and the remedy provided by the new one; and the statute should be given that construction which is best calculated to advance its object, by suppressing the mischief and securing the benefits intended."⁷

It is obvious that the two questions must be considered together. Prior constructions of other statutes are of no avail here unless those statutes are analogous, because we have seen that there are prior constructions both ways. The only way to ascertain whether the statutes construed in decisions rendered prior to the passage of this statute are analogous is to compare the object sought to be served by the statutes thus construed with the object sought to be served by the statute in question.

The statutes provide that a mortgage on "personal estate," if recorded, is constructive notice to those dealing with the mortgagor, in reliance upon his apparent ownership of the mortgaged property. Prior to the passage of section 2128, it was well settled in Kentucky that these mortgage recording statutes had no application to mortgages on intangible personal property.⁸

The reasons why such mortgages cannot be recorded are stated by the court:

"Again, the policy which dictated the statutes is not *applicable to a chose in action or claim for a debt, as there is no such visible possession of such claims or separation of the right in them from the apparent ownership, which is calculated to deceive creditors and purchasers; and, indeed, for many years after the enactment of the early statutes, choses in action were not subject to the payment of debts, nor could be reached coercively and so applied by a creditor. It is true that the creditor has the possession of the evidence of the debt, if the promise or undertaking be reduced to writing, if not, he has no visible possession of even that. But he has no visible possession of property or money which may be seen and looked to by the creditor for the payment of his debt, but of the right only to demand money, valuable or worthless, according to the condition of the debtor. He may assign such evidence of debt, absolutely, conditionally, in trust or in mortgage, by an indorsement on the same, and such indorsements have*

⁶ 36 Cyc. 1153.

⁷ 36 Cyc. 1110.

⁸ *U. S. Bank, et al. v. Huth*, 4 B. Mon. 423.

never been deemed necessary to be recorded. To require them to be recorded, if they assumed the character of an assignment in trust or mortgage, would embarrass commerce by checking the negotiability and circulation of such paper."

It is also held that a mortgage upon shares of stock does not come within the provisions of the recording statutes which refer to personal estate.⁹ In *Spalding v. Paine's Administrator* the court takes the position that because of the very nature of intangible property a mortgage, though recorded, cannot, as a practical matter, furnish the protection which the recording statutes were meant to furnish.

"These certificates of stock are in the pockets of the owner, and go with him where he may happen to locate as choses in action, or evidence of his right without any means on the part of those with whom he proposes to deal on the faith of such a security of ascertaining whether or not this stock is in pledge or mortgaged to others. He finds the name of the owner on the books of the company as a subscriber of paid-up stock amounting to 180 shares, with the certificates in his possession; pays for these certificates their full value, and has the transfer to him made on the books of the company, thereby obtaining a perfect title. What other inquiry is he to make so as to make his investment certain and secure? Where is he to look in order to ascertain whether or not this stock has been mortgaged? The chief office of the company may be at one place today and at another tomorrow. The owner may have no fixed or permanent abode, and with his notes in one pocket and certificates of stock in another, and the one evidencing the extent of his interest in the stock of the corporation, the other his right to money owing him by his debtor, we are asked to say that the mortgage is effectual as to the one and inoperative as to the other."

Furthermore, the court holds that if the recording statutes should be construed to cover intangible property, such construction would unreasonably interfere with commercial transactions based upon the ready transfer of such intangibles.

"We find no precedent in this State sustaining the views presented by the appellant, and, as suggested by the counsel for the appellee, much of the business of the country is conducted on the faith of the pledge of such stock as collaterals, and to adjudge that the holder of the stock by transfer on the books of the corporation or by endorsement and delivery by the owner is subordinate in his claim to the mortgage, upon the doctrine of constructive notice, would paralyze trade and open a wide field for the fraudulent disposition of such valuable interests at the expense of honest and confiding purchasers."

It is clear that the purpose of the mortgage recording statutes construed in these cases was to protect those dealing with owners of the property in reliance on their ownership.

⁹ 5 Ky. L. R. 391, 81 Ky. 416.

The Court of Appeals of Kentucky has a number of times construed section 2128, and an examination of those decisions will indicate whether that section had an object similar to that of the mortgage recording statutes just referred to. In *Morehead's Administrator v. Mayfield*,¹⁰ the plaintiff's intestate had a policy of insurance on his own life, payable to his estate, and by an unrecorded instrument, transferred it to his wife. After his death the transfer was attacked by his creditors. The wife's rights to the proceeds of the policy were sustained because the transfer did not deplete the estate of the transferor. The court said:

"Counsel for appellee suggests that this policy of life insurance, or, indeed, any chose in action is not intended to be included in section 2128, *supra*, as personal property, and cites authority holding that a mortgage of choses in action are not recordable instruments. While there is force in this position, we do not think it necessary to a decision of this case to determine the question as to what particular kinds of property are embraced in the term "personal property," as used in the statute. We think the statute meant to *include property of a tangible, substantial nature or right*, having at the time an ascertainable value, and thus an applicable part of the husband's estate. We do not think the statute includes any mere possibility, expectancy or contingency, but its aim and purpose is to cover some kind of property that, at least, a creditor might subject by attachment to his debt, or that would pass by a deed of general assignment for the benefit of creditors."

In *McWethy v. McCright*,¹¹ a husband gave his wife certain bonds. After his death his heirs sought to require the wife to account for the bonds because the transfer to her was not in writing or recorded. The court held that the transfer was valid as between the parties thereto.

"It will be found from a careful examination of the opinions in these cases that they recognize the validity, as between husband and wife, of a gift of personal property from one to the other by word of mouth and manual delivery, notwithstanding the provision of the statute which requires that in order to make such a gift valid as to third persons it must be in writing, duly acknowledged and recorded."

And it further held that it was only invalid as to purchasers or creditors, and that the heirs could not upset it.

"In our opinion the appellee is not, in the meaning of the statute, a third person having the right to complain of the gift of the bonds to appellant by decedent. . . . If the gift to appellant of the bonds in question had been by a writing from the donor, duly signed, ac-

¹⁰ 109 Ky. 51.

¹¹ 141 Ky. 816.

knowledge and recorded, appellee would not have been in any way affected thereby. Notice to her of the gift was unnecessary; having no interest as heir at law of the donor in the bonds given appellant and no right to complain of the gift, she was not a third person to whom the statute required that the notice, furnished by the recorded transfer of the bonds, be given; nor could she as heir at law of the donor have brought suit to cancel the writing or annul the gift."

In *Jones v. Louisville Tobacco Warehouse Company*,¹² a wife rented her farm to her husband. He raised a crop of tobacco thereon and she had a lien on said crop to secure the payment of her rental both by virtue of her rental contract and by virtue of the statutes. The husband transferred the tobacco to his wife, and she shipped it to the warehouse company which sold it. The warehouse company held the proceeds in payment of pre-existing indebtedness from the husband to the company. The wife sued the warehouse company for the proceeds of the tobacco, and it contended that the transfer of the tobacco from the husband to the wife was invalid because not recorded. The court denied this contention, and in so doing said:

"While as between husband and wife, such contracts must be in writing to affect third persons, by the expression it is meant that others may deal with the former owner on the faith of his ostensible ownership unaffected by secret transfers. The provision as to recordation of the contract is to give a notice of the changed title. Obviously, if the party dealing with it knows equally well from other sources that the title is in the wife, but he buys from the husband, knowing that the wife is ignorant of the transaction, he is not the kind of 'third person' intended to be protected by the statute. The statute aims at promoting honesty, not trickery, and is meant to enlarge, not to restrict, married women's property and contractual rights. In ought to be given a liberal construction to effectuate the legislative purpose. The transaction between husband and wife was not meretricious. The transaction itself was valid; the only thing lacking was the publicity necessary to protect third persons who might deal with it. *The possession by the wife was of itself notice* that she had some sort of claim upon the property. If her possession was obtained in fact by reason of the transfer of the tobacco in satisfaction of her lien, it preserved her lien, independent of the statute, as against all the husband's creditors who had notice of the facts; and *her possession was of itself notice of the facts.*"

In *Fogarty v. Neal*,¹³ a resident of Kentucky executed a note to a resident of Oklahoma, which note was secured by a lien on Kentucky real estate. The payee endorsed and delivered the note to his wife, but without notifying the maker, the payee collected the note from the maker. The wife then sued

¹² 135 Ky. 324.

¹³ 201 Ky. 85.

the maker, and he defended on the ground that he had paid the note to the husband, and that the transfer of the note from the husband to the wife was invalid because it was not acknowledged and recorded. The court sustained the transfer, on the ground that the transfer had taken place in Oklahoma, and the statute in question had no extra-territorial effect. It declined to pass on the question whether the statute had any application to the transfer of a note. It referred to the statute in question as one "*dealing solely with the fraudulent transfer of property between husband and wife.*" The unhappy maker who had to pay the note twice was in a position to call for the court's sympathetic consideration. By failing to demand the surrender of the note when he paid the husband he created a situation which resulted in his having to pay it again. Not even his unfortunate plight was sufficient to induce the court to apply the statute to the transfer of a note.

From these decisions it seems clear that the statute in question was really meant to protect persons dealing with ostensible owners of property against fraudulent transfers of that property to the transferor's husband or wife. If A owns a horse, that fact is generally known to those in the vicinity, and credit is extended to him in reliance thereon. After obtaining the credit, he can very easily claim that he has sold the horse to his wife. There is no visible change of possession, and it is very difficult for a third person to prove fraud, or lack of consideration. This was the situation the statute was designed to meet. This is shown in the case of *Eberhardt v. Wahl*,¹⁴ *infra*, where the court said:

"It was recognized that their relation was one affording amplest opportunities for the practicing of fraud against creditors of either, unless their dealings with respect to their property were made the subject of public record. As they generally live together and use each other's property in common, there will be no visible change of possession to indicate a change of ownership. Persons crediting the former real owner might then be misled into believing that no change in the title had occurred, and upon the face of such apparent condition give credit where there was not property to support it."

It was only intended to upset transfers which were prejudicial to those dealing with the transferor, in reliance on his apparent ownership. The mortgage recording statutes provide

¹⁴124 Ky. 223.

that a mortgage shall not be valid as to purchasers or creditors unless acknowledged and recorded. They are designed for a very similar purpose, that is, to protect those dealing with the apparent owners of property against secret claims by third persons. Also, of course, they were to protect the rights of *bona fide* mortgagees. If the purpose of the statutes is similar then two conclusions follow: 1. When the legislature passed section 2128, it is presumed to have been familiar with the established rule that the phrase "personal estate" or "personal property" in recording statutes does not include intangibles;¹⁵ and 2. If the purpose of the statutes is similar, the authorities construing the phrase "personal estate" in the recording statutes are persuasive of the meaning of the phrase "personal property" in section 2128.

The court says in the cases of *U. S. Bank v. Huth*, and *Spalding v. Paine's Admr.*, that the phrase "personal estate" does not mean intangible personal estate, because to construe the statute to apply to intangibles would not meet the evil at which the statute was directed, but would unreasonably hamper commerce. The same may be said as to section 2128.

It is said, however, that the case of *Eberhardt v. Wahl's Admr.*,¹⁶ is a direct decision that section 2128 does apply to the transfer of corporate stock. A husband executed two notes to a bank. On one of these notes he pledged his own stock, on another he pledged his wife's stock. His wife undertook to pay the note upon which her stock was pledged. By error of the bank, the note secured by the husband's stock was marked paid. The error being discovered, the husband pledged his stock, which had thus been released, with his wife, to secure her against loss by reason of her paying off this note. A creditor of the husband sought to subject this stock which had thus been released from the bank's lien to his claim. The court said that the arrangement by which the husband pledged his stock to his wife was in violation of the statute, but it held that the bank had a valid lien on the husband's stock to secure its debt; the wife, by reason of paying that debt, was subrogated to the bank's lien on the stock without regard to any agreement which she may have had with her husband, and her claim to a lien on the stock released

¹⁵ 36 Cyc. 1153.

¹⁶ 124 Ky. 223.

by her payment of her husband's debt was superior to that of the attaching creditor. So far it will be seen that the case is not a decision on the question at all. However, after the transactions above mentioned, the note secured by the wife's stock was still in the bank. She claimed that her husband had agreed that she might hold the stock released by the bank, not only to secure the repayment of the money she had paid the bank, but also to secure her against loss by reason of the pledging of her own stock on the other note. The court held this much of the agreement invalid, and to this extent the case is authority for the proposition that section 2128 applies to the transfer of corporate stock.

The case does not indicate that the court considered the analogy of *Spalding v. Paine's Admr.*, and the *U. S. Bank v. Huith*. That the Court of Appeals does not regard the case as settled is shown by its opinion in *Fogarty v. Neal*,¹⁷ where it specifically declined to pass on the applicability of section 2128 to the transfer of a promissory note, as it had theretofore declined in the case of the transfer of the insurance policy in *Morehead v. Mayfield*.¹⁸

CONTEMPORANEOUS CONSTRUCTION

No test of statutory construction is more often employed than that of contemporaneous construction. This statute has been in effect for more than thirty years and it is confidently asserted by lawyers of large practice, extending over this entire period of thirty years, that probably no transfer of corporate stock between husband and wife has ever been recorded in the state of Kentucky in compliance with this statute. Numberless transfers have no doubt been made, and the fact that the bar of the State has not regarded a compliance with this statute as necessary is entitled to weight when considering that question.

APPLICATION OF SECTION 545, KENTUCKY STATUTES

Section 545 provides for the transfer of shares of stock upon the corporate books. It has been suggested that a compliance with this statute in a measure serves the purpose sought

¹⁷ 201 Ky. 85.

¹⁸ 109 Ky. 51.

to be served by section 2128. This is not the case, because no one is entitled to rely upon the corporate books except the corporation itself. A transfer made without registration upon the corporate books is valid against all the world, except the corporation, including attaching creditors of the transferor. In *Thurber v. Crump*,¹⁹ the court said:

"Transfers of stock in corporations organized under chapter 56 of the General Statutes, are valid, not only between the parties but as against creditors, although not entered upon the books of the company. The provision of the statute requiring such transfers to be made upon the books of the company is for the protection of the corporation and purchasers and *not for the protection of creditors of the stockholders, the books of the company not being open to the inspection of the public.*"

To the same effect are *Husband v. Linehan*,²⁰ and *Stowe v. Harvey*,²¹

The title to stock is in no way affected by the transfer or failure to transfer same upon the corporate books.

THE DUTY OF A CORPORATION

If it be true that section 2128 requires that transfers of corporate stock between husband and wife be acknowledged and recorded, is it the duty of the corporation, when requested to transfer stock, to inquire whether it is being transferred from husband to wife, and to exercise care that no such transfers be registered on the corporate books unless it has been recorded in the county clerk's office? This inquiry is not fanciful. If a corporation transfers stock without right, it may in some instances be required to answer to the transferee and also to recognize the original owner as a stockholder.

In *St. Romes v. Cotton Press Co.*,²² an agent of the widow who owned stock in the defendant corporation, presented the certificates and induced the corporation to transfer the stock. It was thereafter transferred from time to time to innocent purchasers. The court held that the agent exceeded his powers in causing this transfer, and that the corporation was absolutely liable to recognize the widow as the owner of the number

¹⁹ 86 Ky. 408.

²⁰ 168 Ky. 304.

²¹ 241 U. S. 199, 60 L. Ed. 952.

²² 127 U. S. 614.

of shares of stock thus wrongfully transferred, and inferentially held that the corporation was also bound to recognize the rights of the innocent transferees of this stock. The same thing was held in *Telegraph Co. v. Davenport*,²³ where the transfer was made through means of forgery by an agent of the real owner of the stock.

The husband or wife transferee would acquire a good title subject only to attack by the transferor's creditors.²⁴ The transferee could no doubt give a good title to an innocent purchaser by endorsing and delivering the certificate to such purchaser. No doubt the corporation would be compelled to recognize the innocent purchaser and it might conceivably be held to answer to the wronged creditor of the transferor. On the other hand, the corporation could answer that the unrecorded transfer was merely voidable, not void, and that no liability attaches to a corporation for registering a voidable transfer, and that a corporation has no right to inquire into the validity of the transfer between parties. If the owner has endorsed and delivered the certificates to the transferee, the corporation must register the transfer and is not liable therefor though the transfer is illegal as between the parties thereto.²⁵

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Louisville, Ky.

²³ 97 U. S. 369.

²⁴ *McWethy v. McCright*, 141 Ky. 816.

²⁵ *Fletcher, Cyc. Corp.*, vol 6, p. 6412; *Machen on Corporations*, sec. 934.