Marquette Law Review

Volume 22
Issue 2 *February 1938*

Article 7

1938

# Corporations: Participating Operation Certificates: Who are Creditors and Who are Co-Adventuers?

Edward J. Kulig

liability is extremely difficult. It is suggested that for purposes of administrative convenience responsibility should be imposed upon the person holding the stock at the time of the bank's insolvency. "Statutes and constitutional provisions which seem to point toward a different solution should be construed so as to make them harmonize with this result." ZOLLMANN, 3 BANKS AND BANKING § 1614 . In Wisconsin, it is not the shareholders at the time the debt accrued, but the shareholders at the time an action is commenced thereon who are individually responsible for such debt to the amount of their respective shares. *Cleveland* v. *Burnham,* 55 Wis. 598, 13 N.W. 677 (1882). The liability of a stockholder becomes fixed at the date of the judgment by which it is ascertained that the assets of the bank have been exhausted and that the deficiency exceeds the amount of his stock, and from that date he is liable. *Cleveland* v. *Burnham,* 64 Wis. 347, 25 N.W. 407 (1885).

Section 221.42 of the Wisconsin Statutes (1937) limits the liability of a state bank stockholder's liability to one year after written notice is given to the banking commissioner of any transfer of stock, and liability attaches only to the affairs of the bank at the time and prior to the date of the transfer. This statutory liability terminates at the end of one year after written notice of the stock transfer is given to the banking commissioner, even in cases where the transferor knew of the insolvency of the bank and of the transferee's financial irresponsibility and where the transferor intended to avoid statutory liability. *Cleary* v. *Bertrand,* 217 Wis. 622, 258 N.W. 799 (1935). To terminate such liability there must be compliance with the statute. The legal owner remains liable as long as his name remains on the books of the bank, and fraudulent transfer of stock to an agent or one who is financially irresponsible will not terminate the legal stock owner's liability. *Lochner* v. *State,* 214 Wis. 109, 252 N.W. 695 (1934). Voluntary assessments paid by shareholders of a bank under Sections 220.07 (20) and 221.42 (1933) are independent from statutory liability and do not give immunity to statutory liability, nor can such voluntary assessments be applied to the statutory liability. In re *Security Savings Bank,* 217 Wis. 507, 259 N.W. 426 (1935). This is because the voluntary assessments are for the benefit of the bank and the statutory liability is for the benefit of creditors. In re *Plain Bank,* 217 Wis. 257, 258 N.W. 783 (1935). Stockholders can not claim as a set off against their statutory liability the deposits in an insolvent bank. *Banking Commission, Receiver* v. *Bitker,* 216 Wis. 497, 257 N.W. 616 (1934). Whether satisfaction can be obtained against two stockholders, on the same share of stock, has never been decided in Wisconsin. But the majority of states having statutes like our own seem to hold that although two persons may be liable, it "does not mean that the receiver can enforce full payment of the liability against both." ZOLLMANN, 1 BANKS AND BANKING § 494.

ROY C. PACKLER.

---

CORPORATIONS—PARTICIPATING OPERATION CERTIFICATES—WHO ARE CREDITORS AND WHO ARE CO-ADVENTURERS?—The Sterling Oil Company, a Wisconsin corporation, proposed to erect a filling station. For the purpose of financing the cost of erecting the station, the corporation, by authority of its stockholders and its board of directors, issued "participation operation certificates." To secure the repayment of the indebtedness, the corporation executed and delivered to the plaintiff, as trustee, a deed of trust on all buildings, land, and equipment, such conveyance being made "for the equal pro rata benefit and security of every holder of any of the certificates." The purchasers paid $150 for each "partici-

pation operation certificate" and $150 for one and one-half shares of Class B non-par stock. The certificates and stock were sold in units for $300. The "participation operation certificates" provided that the holder was to receive one cent for every gallon of gasoline and one cent for every gallon of kerosene sold by the corporation, and 5 per cent of the gross sales in all other goods, "the fund so created to be divided equally at the end of each month among the certificate holders of such station and such distribution shall continue until such certificate holders shall have received $300 for each certificate, which sum the Company guarantees shall be paid on or before ten years. This sum shall be in full of all profit and interest of every kind and nature and upon completion of payment thereof, all the right, title, and interest of the holder shall cease." The trust deed was recorded. Subsequently, the defendant Sterling Oil Company was adjudicated a bankrupt. Defendant has paid $169 from the fund created on each certificate. The trustee in bankruptcy conveyed the premises to appellant Cosden Oil Company, the deed reciting that it was "subject to all legal liens and incumbrances." The purchaser, the Cosden Oil Company, leased the premises to the Pure Oil Company. In the action to foreclose the trust deed, the trial court found that the rights of the Cosden Oil Company and the Pure Oil Company are subsequent and subordinate to the plaintiff's claim. On appeal, *held,* judgment affirmed; the holders of the certificates are creditors and not stockholders of the corporation within the meaning and wording of the "participation operation certificates." *Kettenhofen* v. *Sterling Oil Company,* (Wis. 1938) 275 N.W. 425.

The law is well settled that a certificate of stock does not make the holder a creditor as well as a stockholder; he cannot be both creditor and debtor by virtue of his ownership of the same certificate. *Cring* v. *Sheller Wood Rim Manufacturing Co.,* 98 Ind. App. 310, 183 N.E. 674 (1932). If a man is a stockholder, he takes a risk in the concerns of the company, not only as to dividends and a proportion of the assets on the dissolution of the company, but also as to any statutory liability for debts in case the corporation becomes insolvent. *Miller* v. *M. E. Smith Bldg. Co.,* 118 Neb. 5, 223 N.W. 277 (1929). If a man is a creditor of a corporation, he takes no interest in the corporation's affairs, is not concerned in its property or profits as such, but his whole right is to receive agreed compensation for the use of money he furnishes, and the return of the principal when due. Whether he falls into one category or another depends on a proper construction of the contract he holds with the company. *Spencer* v. *Smith,* 201 Fed. 647 (C.C.A. 8th, 1912). Furthermore, some legislative scheme may expressly authorize the issue of stock which will give the holders the rights of creditors, and a lien on the property of the corporation which will have priority over the claims of subsequent creditors, and at the same time give them all the incidents, rights, and privileges and immunities and subject them to all liabilities to which the ordinary stock of the corporation or holders thereof are entitled or subject to. *Heller* v. *National Marine Bank,* 89 Md. 602, 43 Atl. 800 (1899); *Kingston Cotton Mills* v. *Wachovi Bank and Trust Co.,* 185 N.C. 7, 115 S.E. 883, 29 A.L.R. 251 (1923). Whether or not the holders of certificates like those in the instant case are to be regarded as stockholders or creditors, it is said, is a matter for interpretation. *Hazel Atlas Glass Co.* v. *Van Dyk & Reeves Inc.,* 8 F. (2d) 716 (C.C.A. 2d, 1925). The nature of the transaction is to be determined by the substance and effect of the contract which is being foreclosed, rather than by the name given to the security or the obligation. To call a thing by its wrong name does not change its nature. *Koeppler* v. *Crocker Chair Co.,* 200 Wis. 476, 228 N.W. 130 (1929). The important inquiries that must be made are whether

a date is fixed within which the company is bound to pay up the "shares," and whether it appears that the parties intended that the interests of the "shareholders" be subordinated to the interest of the creditors at large in case the company should become insolvent. *Kidd* v. *Puritan Cereal Food Co.,* 145 Mo. App. 502, 122 S.W. 784 (1909). Where no time is fixed when the principal shall become due and payable, the certificate itself cannot create a debt. *Jefferson Banking Co.* v. *Trustees of Martin Institute,* 146 Ga. 389, 91 S.E. 463 (1917). It has been held that the fact that certificates provide that they "shall be a preferred lien on the assets of the Company" does not make the holder a creditor, when it is manifest from the certificate construed as a whole that the corporation never intended to make him one, but merely to give him a lien on the assets of the corporation when in liquidation, over the common stockholders. *Weaver Power Co.* v. *Elk Mountain Mill Co.,* 154 N.C. 76, 69 S.E. 747 (1910).

In the instant case there was a definite promise to pay a fixed sum within a fixed period. The separate instruments apparently contained all the essential elements of promissory notes. In a case where the promotion scheme was comparable to the one carried out in the instant case and where the participating "operation certificates" were secured by a trust deed on all the premises, the court held that the holders were profit-sharers and co-adventurers. *United States and Mexican Oil Co.* v. *Keystone Auto Gas and Oil Service Co.,* 19 F. (2d) 624 (W.D. Pa. 1924). It is important to notice that in the latter case no fixed date for payment was prescribed in the certificates. And in the latter case the controversy developed between holders of the certificates and a receiver representing general creditors over the fund which had been built up from percentage contributions out of gross sales. In the instant case the controversy was not one between the certificate holders and general creditors. The corporation had been adjudged a bankrupt. The properties had been sold by the trustee in bankruptcy. At the time no issue between certificate holders and general creditors with respect to recourse against the company's assets or the proceeds from the sale had been raised. The purchaser from the trustee took with notice of the asserted encumbrance. It does not appear how much the purchaser paid. It is submitted that the equities are with the certificate holders as against a purchaser like the one in the instant case who probably paid little more than enough to carry the costs of the bankruptcy administration. But the court's apparent willingness to decide this case according to its "interpretation" of the instruments may be hard to explain if the court ever has to decide a case just like the *Keystone Gas Co.* case.

EDWARD J. KULIG.

---

CORPORATIONS—SERVICE OF PROCESS—FOREIGN CORPORATIONS DOING BUSINESS WITHOUT A LICENSE.—The defendant, an automobile manufacturer, pleaded in abatement to the jurisdiction of the court on the ground that no valid service was made as it was not present or found in the state. Prior to November, 1935, the defendant had a Boston distributor who contacted all the dealers. The sales were understood to be made at Detroit and the distributor was not an agent. The distributor went out of business in November and a district manager took over the duties so the local dealers could get automobiles. His office was in a building which was owned by a corporation and the stock of such corporation was owned entirely by the defendant. The defendant sent him its own stationery to use. He sent all the dealers' orders on to Detroit. He arranged for the show-