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Erwin Esser Nemmers

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# EMPLOYEE STOCK REPURCHASE AGREEMENTS\*

ERWIN ESSER NEMMERS†

ONE of the aspects of treasury stock<sup>1</sup> and the power of a corporation to buy its own stock which has come to the fore during the last decades has been the employee stock ownership plan.<sup>2</sup> In general, there are at least two advantages in employee stock ownership.<sup>3</sup> The first is economy in raising capital and the second is increase in employee loyalty. The first advantage is real and not inconsiderable. In selling to employees, the marketing costs of the investment banker (which may run around 10%) are saved. Secondly, and more important, the corporation has thereby increased its borrowing capacity or if it has no desire to increase its borrowing capacity, has placed itself in a position to secure lower interest rates on its bonds, all because it has increased the stock cushion between the bondholder and insolvency.<sup>4</sup>

The other and more dubious reason why employee stock ownership is desirable is that employee loyalty and efficiency will increase.<sup>5</sup> The trouble with this argument is that employee ownership is a double-

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† Member of the Wisconsin bar; Austin, Lehman and University fellow, Harvard University.

<sup>1</sup> On the general subject of treasury stock, see Nemmers, *Power of a Corporation to Purchase Its Own Stock*, 1942 WIS. L. REV. 161.

<sup>2</sup> In general see: Laura A. Thompson, *A Selected Bibliography: Employee Stock Ownership in the United States*, MONTHLY LABOR REVIEW OF BUREAU OF LABOR STATISTICS (June, 1927); NATIONAL INDUSTRIAL CONFERENCE BOARD, *EMPLOYEE STOCK-PURCHASE PLANS IN THE UNITED STATES* (1928) and *EMPLOYEE STOCK PURCHASE PLANS AND THE STOCK MARKET CRISIS OF 1929 (1930)*; Hearings before Sub-committee of Senate Committee on Banking and Currency, 72d Cong., 2d Sess., 1933, pt. II at 1919, pt. VI at 1872 *et seq.* and 1944 *et seq.*; FOERSTER and DIETEL, *EMPLOYEE STOCK OWNERSHIP IN THE UNITED STATES* (1926). Distinguish agreements to repurchase stock sold by a corporation from subscriptions made with a secret agreement to return and get money back. The former involves property belonging to the corporation and it is free to make contracts to repurchase. The latter involves the rights of subscribers as a whole and is unenforceable as a fraud on fellow stockholders. *Burke v. Smith*, 16 Wall. 390 (1872). Cases collected in Note, 101 A.L.R. 154 (1936).

<sup>3</sup> Cf. generally, DEWING, *FINANCIAL POLICY OF CORPORATIONS* (3rd ed., 1934) 1078-1079.

<sup>4</sup> This same advantage accrues from customer ownership of stock, cf. Dewing, *supra*, n. 3, 1068-1078.

<sup>5</sup> Employee stock ownership plans of the type here under discussion should be distinguished from the various plans designed to gear executive compensation on an equity basis to corporate profits by granting a flat salary plus a percentage of the net profits and/or stock shares in ratio to net profits as an added stimulus. Indirectly, the present plan is related to the executive profit-sharing scheme in that presumably the increased effort of employees will be reflected in increased earnings which will be distributed to stockholders.

edged sword. If the business does not prosper, no dividends result and the employee may have this as an added complaint where wages are being lowered.<sup>6</sup> In addition, in times of depression, the employee may desire to liquidate some of his savings because of decreased earnings in some other source of income. To do so, he may desire to call upon the corporation to repurchase and under the rule that a corporation cannot be forced to repurchase stock when it is insolvent or will be made so by the repurchase, the employee's futile efforts may well create ill-will.

Not all employee stock ownership plans call for repurchase clauses, and these clauses may be of widely different kinds. Certainly the repurchase clause is an added selling point. It may provide for repurchase on demand, after a stated period or on cessation of employment. It may provide that the employee only is to have the right to demand repurchase, or that both employee and employer can demand repurchase. It may be an option to repurchase or an obligation to do so, or both. The variations are obviously numerous and may be dictated by selfish or sincere motives.

The "loyalty and efficiency" reason for employee stock ownership has been variously analyzed into further components, such as: stimulating saving by employees, sharing the profits with the workers, giving employees a voice in management, increasing efficiency and minimizing labor turnover.<sup>7</sup>

A special twist is given the subject because stock purchase plans have been used by corporations in need of new management by offering new managers stock at depressed prices so that if they are successful they will share as stockholders in the new earnings. Or a highly profitable corporation may be endeavoring to keep its successful management by such terms.<sup>8</sup>

The cases dealing with repurchase of a corporation's own stock from an employee are but one class of the larger group dealing with general repurchase agreements. There is another frequent and important group: agreements by corporations (usually utilities) to repurchase from customers who have bought stock in the corporation.

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<sup>6</sup> If employee stock ownership is a palliative for underpayment in the first place, it is hardly likely to succeed.

<sup>7</sup> Cf. Fordham, *Some Legal Aspects of Employee Stock-Purchase Plans* (1930) 8 N. CAR. L. REV. 161; Blackstock, *A Corporation's Power to Purchase Its Own Stock and Some Related Problems* (1935) 13 TEX. L. REV. 442. See note, 48 A.L.R. 622 (1926). On the tax aspect see: Bastedo, *Taxing Employees on Stock Purchases* (1941) 41 COL. L. REV. 239. This article avoids duplication of certain aspects dealt with in the articles just mentioned.

<sup>8</sup> On this aspect see a series of works by J. C. BAKER, *EXECUTIVE SALARIES AND BONUS PLANS* (1938); *Executive Compensation Policies of Small Industrial Companies* (1938) 16 HARV. BUS. REV. 446; *Stock Options for Executives* (1940) 18 HARV. BUS. REV. 106; and *Executive Compensation Practices in Retail Companies, 1928-1939*. Harv. Bus. School Division of Research, Business Research Studies, No. 23, July, 1939; S.E.C., *Official Summary of Security Transactions and Holdings* (March, 1935).

Perhaps the first case dealing with the validity of employee repurchase agreements of a corporation was *Fleitmann v. Stone Cotton Mills*.<sup>9</sup> In that case the corporation agreed to give its selling agency to plaintiffs who bought \$15,000 of defendant's stock, the corporation agreeing to repurchase the stock if it terminated the plaintiff's agency. In a summary opinion on this point, the court granted specific performance to the agents when the corporation terminated the agency but refused to repurchase the stock.

A few months later, in *Strodl v. The Farish-Stafford Co.*<sup>10</sup> a North Carolina corporation was sued in New York as successor to a Connecticut corporation by a former employee who claimed the corporation had entered into a contract to repurchase his shares if he left the employ of the company. The law of a foreign jurisdiction not having been pleaded, the court found the common law did not hold such a contract void as against public policy. The contract in this case involved a promise by the employee to sell upon cessation of employment, a feature which was not present in the *Fleitman* case. There is a *dictum* in the case where it is said there must be a surplus to carry out the repurchase, but the burden of showing that no surplus exists is on the corporation.<sup>11</sup>

Then followed what have become two leading cases on the subject, *Richards v. Weiner Co.*,<sup>12</sup> and *Re Tichenor-Grand Co.*<sup>13</sup> In the former case, the plaintiff purchased stock on the corporation's promise to

<sup>9</sup> 186 Fed. 466, 108 C.C.A. 444 (C.C.A. 5, 1911), *cert. den.* 223 U.S. 723, 56 L.Ed. 631, 32 Sup. Ct. 524 (1911). There were earlier cases dealing with employee repurchase agreements but not by a corporation. In *Guernsey v. Cook*, 120 Mass. 501 (1876) two majority shareholders agreed to repurchase. In *Noyes v. March*, 123 Mass. 286 (1877) it does not appear what position the contemplated repurchasers occupied with reference to the corporation. In *Wilbur v. Stoepel*, 82 Mich. 344, 46 N.W. 724, 21 Am. St. Rep. 568 (1890) the contract was between two of the three stockholders in a corporation and the employee. In *McIntyre v. E. Bement's Sons*, 146 Mich. 74, 109 N.W. 45 (1906) there was a repurchase agreement by the corporation but with a shareholder not an employee. In *Meurer v. American Moving Picture Mch. Co.*, 61 Misc. 281, 113 N.Y. Supp. 719 (1908) an employee repurchase agreement was involved but the case was decided on insufficient notice within the time available for demanding performance. The principal case was followed in *Re Fechheimer Fishel Co.*, 212 Fed. 357 (C.C.A. 2d, 1914) where the court said: "A corporation's contract to purchase its own stock, though valid in its inception cannot be enforced unless a surplus exists when payment is due." It is true that in *Mulford v. Torrey Exploration Co.*, *infra*, n. 48, the court had held an employee repurchase contract a conditional sale at an earlier date.

<sup>10</sup> 145 App. Div. 406, 130 N.Y. Supp. 359 (1911), *reversing* 67 Misc. 402, 122 N.Y. Supp. 609 (1910). Perhaps the best way to deal with employee repurchase contracts would be to trace the history of this type of contract in a single jurisdiction. New York has been chosen for this purpose because its cases include most of the leading cases on the subject.

<sup>11</sup> Followed in *Richards v. Weiner Co.*, *infra*, n. 12. The Federal rule may be contra: *Hamor v. Taylor-Rice Engineering Co.*, 84 Fed. 392 (Del. C.C.D., 1897). And see *Reith v. University Housing Corp.*, 247 Mich. 104, 225 N.W. 528 (1929).

<sup>12</sup> 207 N.Y. 59, 100 N.E. 592 (1912).

<sup>13</sup> 203 Fed. 720 (S.D. N.Y. 1913).

employ him. The corporation was to have the right to discontinue employment and thereupon bound itself to repurchase the employee's stock if he so desired. The court followed the *dictum* in the *Strödl* case and held that the burden was on the corporation to show insolvency as a defense to the contract. In the *Tichenor-Grand Co.* case the referee in bankruptcy disallowed the claim of a employee under a repurchase agreement. The contract called for repurchase at the end of three years upon sixty days' notice. A few months before the end of the three years the corporation became insolvent. In the argument one aspect of the employee situation seems to have been suggested for the first time. It was argued that because of the employee's relation to the corporation, his contract of repurchase should be governed by a special rule entitling him to claim from the corporate treasury. This argument was quickly brushed aside by Judge Learned Hand, who said:<sup>14</sup>

"If he is entered upon the books as a stockholder, and if his shares figure as a part of the share capital actually issued, certainly all the evils which the statute<sup>15</sup> means to forbid will arise from allowing him thereafter secretly to deplete the treasury of the company, as would arise if he reserved no right to do so. Creditors have no means of knowing what part of the shareholders have reserved this right, and how many may dip into the corporate treasury, or, as in this case, come in to share with them in insolvency. From the reason of the thing, therefore, the fact [of employment] should make no difference."

There is one "out" for the employee which was suggested in the *Richards* case.<sup>16</sup> In that case the employee agreed to purchase the stock for \$10,000 but had paid only \$3,000 and no shares had actually been issued to him. Such an arrangement might be treated as an option or contract to purchase rather than a purchase.

The next leading case in New York was *Topken, Loring & Schwartz, Inc. v. Schwartz*.<sup>17</sup> In that case the corporation sold shares to the defendant, who agreed to sell, and the corporation agreed to buy at the book value when the term of employment ceased. When his employment was terminated, the defendant refused to sell the shares

<sup>14</sup> *Ibid.*, at 721.

<sup>15</sup> N.Y. Consol. L. (1909) c. 40, now Gilbert's Ann. Penal Code (1940) § 664, forbidding purchases except out of surplus and making it a misdemeanor for officers of a corporation to do otherwise. Section 14 of N. Y. Stk. Corp. L. (1940) requires stockholder consent to such issue of stock to employees. Any dissenting shareholder having preemptive rights is entitled to appraisal. This provision was enforced in *Matter of Stockwell*, 210 App. Div. 753, 206 N.Y. Supp. 834 (1924).

<sup>16</sup> *Supra*, n. 11.

<sup>17</sup> 249 N.Y. 206, 163 N.E. 735 (1928) noted in (1929) 29 Col. L. Rev. 356, (1929) 15 Corn. L. Q. 108, (1929) 42 Harv. L. Rev. 830, (1930) 43 Harv. L. Rev. 831, (1930) 3 St. John's L. Rev. 115, (1937) 12 St. John's L. Rev. 276, (1929) 6 N. Y. U. L. Q. 321, (1929) 39 Yale L. J. 902.

he held to corporation which had only four shareholders. Upon suit by the corporation for specific performance, the court denied relief, treating the contract as one involving merely executory promises (and thereby excluding employment as a consideration) and held that since the defendant could only have enforced the contract against the corporation if there were surplus profits, there was not the "binding" obligation on the corporation essential to a contract. In calling the contract illusory because one party—the corporation—was not bound, the court is assuming that the existence or non-existence of profits was so far within the control of the corporation as to equate the matter to the situation where the corporation withdraws at will.<sup>18</sup> But is this a case of withdrawal at will, and is the existence of profits a contingency arbitrarily controllable by the corporation?<sup>19</sup> Failure to use an easy interpretation making employment the consideration on the part of the corporation<sup>20</sup> threatened to jeopardize a valuable and desirable type of contract. Later cases were left a ground of distinction because in this case the corporation was closed and therefore control of surplus might be very easy.<sup>21</sup>

There followed shortly *Cross v. Bequelin*<sup>22</sup> where a corporation which had sufficient surplus agreed to purchase the shares of plaintiff stockholder. Before payment was fully made, the corporation became insolvent and a creditors' committee took over the assets and paid all existing debts. The plaintiff stockholder's claim for the balance due was held payable out of the funds held by the creditors' committee *pro rata* with the salary claims. Those having salary claims were directors who knew of the contract to purchase plaintiff's shares.

Why does not the logic of the *Topken* case apply equally here so that there is no contract, there being no consideration? In the present case a closed corporation also is involved. The court did not mention the *Topeka* case in this connection. It has been suggested that the *Topeka* case has "now been pared down to hold that equity will not grant to a corporation specific performance against a stockholder who has received nothing but a promise which he may not be able to en-

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<sup>18</sup> Admittedly if one party can withdraw at will there is no contract. WILLISTON, *CONTRACTS* (rev. ed., 1936) § 43.

<sup>19</sup> If the existence of surplus is a contingency, then the contract is not illusory but bilateral and binding. Many cases uphold contracts where the performance on one side is entirely conditional on the happening of a future event. *Green v. Hollingshead*, 172 Ark. 575, 290 S.W. 51 (1927); *Beaumont Traction Co. v. Texarkana & Ft. S. Ry.*, 103 Tex. 49, 123 S.W. 124 (1909). And see WILLISTON, *CONTRACTS* (rev. ed., 1936) § 104, *Restatement of Contracts* (1932) § 2 (b).

<sup>20</sup> As had been expressly done by the corporation in the *Richards* case *supra*, n. 12.

<sup>21</sup> But still there would be technical consideration.

<sup>22</sup> 252 N.Y. 262, 169 N.E. 378 (1929). Noted in (1930) 43 Harv. L. Rev. 830, (1930) 39 Yale L. J. 902, (1929) 29 Col. L. Rev. 1152.

force"<sup>23</sup> but the stockholder could get relief because his objection of unfairness would not be available to the corporation.

The *Topken* case overlooked a similar case<sup>24</sup> in Pennsylvania under a similar statute<sup>25</sup> in which the opposite result was reached and the contract was not held illusory. In that case the corporation entered into an agreement with an employee for the sale of shares. It was mutually agreed that on cessation of employment or within thirty days thereafter the corporation would repurchase and the employee would sell. The case involved a dispute as to income but the court assumed the contract was valid.

The *Topken* case also overlooked the first New York case of *Strodl v. The Parish-Stafford Co.*,<sup>26</sup> holding such a contract binding, and succeeding cases.<sup>27</sup>

The suggestion of some courts that the arrangement be viewed as an option in the corporation to repurchase as distinguished from an agreement to repurchase or an option in the employee to resell has been discarded by others who hold the arrangement void if unreasonable as a restraint on alienation, but valid if there is a statutory<sup>28</sup> charter<sup>29</sup> or by-law<sup>30</sup> provision permitting such restraint or if the restraint is "reasonable."<sup>31</sup>

<sup>23</sup> (1930) 43 Harv. L. Rev. 830 at 831.

<sup>24</sup> *Revloc Supply Co. v. Troxell*, 281 Pa. 424, 126 Atl. 774 (1924).

<sup>25</sup> Penn. Bus. Corp. Law (1924) art. 3, § 320(7) provides that a corporation may "purchase, take, receive or otherwise acquire, its own stock—except that no such purchase or acquisition shall be made at a time when the net assets of the corporation are less than its stated capital, or which would reduce its net assets below its stated capital."

<sup>26</sup> *Cf. supra*, n. 10 and as to its being the "first" New York case, *supra*, n. 9. However, the court in *Topka* case does cite the *Strodl* case in another connection. It might be justified in treating the *Strodl* case in silence because that was a lower court (appellate division) decision.

<sup>27</sup> *E.g.*, *Richards v. Ernest Wiener Co.*, *supra*, n. 12, which the court in the *Topka* case considered *dictum*, arguing that there was an *option* in the *Richards* case. This is a questionable interpretation of the opinion in the *Richards* case which in turn seemed willing to raise a questionable doubt about such clear language as "we shall purchase these 30 shares of stock from you" under certain conditions. *Richard v. Wiener*, 207 N.Y. 59 at 63, 100 N.E. 592 (1912).

<sup>28</sup> *Kretzer v. Cole Bros. Co.*, 193 Mo. App. 99, 181 S.W. 1066 (1916).

<sup>29</sup> *Lawson v. Household Finance Corp.*, 17 Del. Ch. 1, 147 Atl. 312 (1929); *Tauchet, Inc. v. Tauchet*, 264 Mass. 499, 163 N.E. 184 (1928); *Bloomingtondale v. Bloomingtondale*, 107 Misc. 646, 177 N.Y. Supp. 873 (1919).

<sup>30</sup> *Sterling Loan & Investment Co. v. Litel*, 75 Colo. 34, 223 Pac. 753 (1924). But see: *Ireland v. Globe Milling Co.*, 19 R.I. 180, 32 Atl. 921 (1895).

<sup>31</sup> *People ex rel. Rudaitis v. Galskis*, 233 Ill. App. 414 (1924) where the restraint was held reasonable where the corporation was allowed to substitute a purchaser that it thought more suitable, at the prevailing market price. But see: *People ex rel. Malcolm v. Lake Sand Corp.*, 251 Ill. App. 499 (1929) where it was held unreasonable to require the consent of the majority of the stockholders. Charter provisions also must be reasonable. Holding individual agreements valid where reasonable is: *Model Clothing House v. Dickinson*, 146 Minn. 367, 178 N.W. 957 (1920).

It would thus seem best in order to avoid the want of consideration argument of the *Topken* case<sup>32</sup> and in order to avoid any difficulty as to restraint on alienation to either

- 1) specify employment as the consideration<sup>33</sup> or
- 2) to insert an option to buy at market price or if there is no market, at a figure to be determined by appraisers and to insert the provision in the stock certificate.<sup>34</sup>

Repurchase contracts are subject to the defense of insolvency by the corporation, leaving the shareholder remediless as is the general rule as to contracts to purchase one's own stock<sup>35</sup> as regards any action against the corporation.

The minority jurisdictions refusing to recognize *repurchase* agreements as *intra vires* constitute a smaller group than the minority holding that general agreements to purchase its own stock are *ultra vires*.

The leading case on another distinction is *Ophir Consolidate Mines Co. v. Brynteson*.<sup>36</sup> That case did not involve an employee repurchase agreement but a general repurchase agreement. Another point was involved in the case but on the repurchase agreement, the contract simply provided<sup>37</sup> that the corporation agreed "to return to said John Brynteson [the purchaser] said Fifteen Thousand (15,000) Dollars, with interest on the same at the rate of six per cent per annum, eighteen months after the date hereof if said John Brynteson be not satisfied with aforesaid investment."

In this case the corporation was chartered in Colorado. The statute in that state<sup>38</sup> forbade the use of corporate funds "for the purchase of stock in their own company or corporation except such as may be forfeited for the nonpayment of assessments thereon." Referring to this statute the court said:

"This agreement is in no sense within the meaning or object of the provision referred to. The stock was held in the treasury<sup>39</sup> of the company to raise funds for improvements, upon such terms of sale as were adopted by the president. The right to so hold and own stock remains in the corporation until an absolute

<sup>32</sup> Cf. *supra*, n. 20. Other devices, of course, can be used to avoid want of consideration.

<sup>33</sup> As in the Richards case, *supra* n. 11.

<sup>34</sup> The first to avoid any "unreasonableness" and the last to comply with § 15 of the Uniform Stock Transfer Act which provides that no restriction of a by-law is valid unless stated on the stock certificate.

<sup>35</sup> Cf. Nemmers, *Power of a Corporation to Purchase Its Own Stock*, 1942 Wis. L. Rev., 161 at 171, section on insolvency. But if the corporation has no creditor and no injury will be done to a fellow shareholder, a corporation may purchase its own shares even though insolvent. *Davies v. Montana Auto Finance Corp.*, 86 Mont. 500, 284 Pac. 267 (1930).

<sup>36</sup> 143 Fed. 829 (C.C.A. 7, 1906).

<sup>37</sup> *Ibid.*, at 830.

<sup>38</sup> Mills, Ann. Stat. Colo. (1891) § 485.

<sup>39</sup> This stock is not properly referred to as treasury stock; it is authorized but unissued stock.

sale is made. No such sale arose under the agreement in suit. It was of the well-recognized class, known as a contract of "sale or return," [citing case] where the title passes for the time being, but subject to the option of the purchaser to rescind and return the property within the time stipulated. With the exercise of the option the contract of sale terminates and the right and title of the corporation is restored to the original status. No sale has been accomplished, and no purchase or repurchase arises upon the part of the corporation through this return of its unsold stock."

For its position the court cited *Sturm v. Baker*<sup>40</sup> which was a case involving a consignment of arms on sale or return, and *Vent v. Duluth Coffee & Spice Co.*,<sup>41</sup> which was a case involving an option in a purchaser of shares to demand the purchase price back but not involving a statute, holding it a conditional sale<sup>42</sup> and citing as authority *Browne v. St. Paul Plow Works*,<sup>43</sup> which was a similar case and which in turn cited three early Massachusetts cases<sup>44</sup> involving conditional sales of stock *between individuals*. The inch by inch progress of these cases needs no commentary. It is interesting to note that none of the cases mentioned cites any of the early purchase (as distinguished from repurchase) cases. It seems that the purchase and repurchase cases had a disassociated development at least until 1915.

The *Ophir* case and its conditional sale rule have been followed<sup>45</sup> in a few states only.

Besides the conditional sale theory, there are other schemes for allowing a corporation to repurchase. One is to view the purchase and repurchase elements as constituting one entire contract.<sup>46</sup> In the leading case of *Porter v. Plymouth Gold Mining Co.*,<sup>47</sup> the court said: "There was but one contract, viz., for the sale and repurchase of the stock,

<sup>40</sup> 150 U.S. 312, 14 Sup. Ct. 99, 37 L.ed. 1093 (1893).

<sup>41</sup> 64 Minn. 307, 67 N.W. 70 (1896).

<sup>42</sup> No distinction for the present purposes appears to be recognized between sale and return and conditional sale in the matter of title as between buyer and seller.

<sup>43</sup> 62 Minn. 90, 64 N.W. 66 (1895).

<sup>44</sup> *Thompson v. Alger*, 12 Metc. 428 (Mass. 1847); *Thorndike v. Locke*, 98 Mass. 340 (1867); *Pearson v. Neason*, 120 Mass. 53 (1876).

<sup>45</sup> *Schulter v. Boulevard Gardens Land Co.*, 164 Cal. 464, 129 Pac. 582 (1913); *Mulford v. Torrey Exploration Co.*, 45 Colo. 81, 100 Pac. 596 (1909); *Williams v. Maryland Glass Corp.*, 134 Md. 320, 106 Atl. 755 (1919); *Lyons v. Sinder*, 136 Minn. 252, 161 N.W. 532 (1917); *Ephraim Downs v. N. J. Central Power & Light Co.*, 115 N.J. Eq. 348, 170 Atl. 835 (1934). But in many states this "sale or return" idea has been rejected inferentially or *sub silentio*, e.g., in Delaware, *In re International Radiator Co.*, 10 Del. Ch. 358, 92 Atl. 255 (1914); *Pasotti v. U. S. Guardian Corp.*, 18 Del. Ch. 1, 156 Atl. 255 (1931) (not an employee situation); *Hegarty v. American Com. Power Corp.*, 20 Del. Ch. 231, 174 Atl. 273 (1934) (employee situation).

<sup>46</sup> *Porter v. Plymouth Gold Mining Co.*, 29 Mont. 347, 74 Pac. 938 (1904); *Latulippo v. New England Inv. Co.*, 77 N.H. 31, 86 Atl. 361 (1913); *Griffin v. Bankers' Realty Inv. Co.*, 105 Nebr. 419, 181 N.W. 169 (1920).

<sup>47</sup> *Supra*, n. 46.

each object being a consideration for the other. This contract was entire and indivisible. The contract could not be sustained unless the contract of repurchase could be enforced. Therefore, if a portion of the contract is ultra vires, the whole contract must fall." Another theory is that even though statutes prohibit corporations from purchasing their own stocks, this prohibition is to be construed as not applying to treasury stock as opposed to stock of the original issue.<sup>48</sup>

In only a few jurisdictions have such repurchase agreements been held unenforceable.<sup>49</sup>

In view of the different treatment accorded repurchase agreements and the evident effort (even in jurisdictions which are in the minority on the general power to purchase one's own stock) to find them valid, the question may well be raised whether repurchase agreements are covered by the recent statutory enactments on the general subject of the power of a corporation to purchase its own stock. Few cases have yet arisen under the new statutes. No express provision for employee repurchase agreements is made in the recent statutes of Illinois, Maryland and Michigan although the language in some of the statutes<sup>50</sup> seems broad enough to remove reasonable doubts. Kansas,<sup>51</sup> a very recent state to revamp its corporation laws, expressly provides for the problem of allowing purchases "from one who, as an employee other than as an officer or director, has purchased such shares from the corporation under an agreement reserving the corporation [*sic*] the option to repurchase or obligating it to repurchase." California<sup>52</sup> has the same

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<sup>48</sup> *Mulford v. Torry Exploration Co.*, 45 Colo. 81, 100 Pac. 596 (1909); *Wilson v. Torchon Lace & Mercantile Co.*, 167 Mo. App. 305, 149 S.W. 1156 (1912); *Korn v. Cody Detective Agency*, 76 Wash. 540, 136 Pac. 1155, 50 L.R.A. (N.S.) 1073 (1913). This distinction is criticized in (1927) 36 Mich. L. Rev. 790 at 794. It has not been followed by the S.E.C. See, F. T. C., Release No. 131 (Mar. 13, 1934). (The Federal Trade Commission was the forerunner of the Securities and Exchange Commission.)

<sup>49</sup> *Pothier v. Ried Air Spring Co.*, 103 Conn. 380, 130 Atl. 383 (1925); *Civil Service Inv. Ass'n. v. Thomas*, 138 Tenn. 77, 195 S.W. 775 (1917).

<sup>50</sup> E.g. Illinois Smith-Hurd Ann. Stat. (1935) ch. 32, § 157.6 says: "A corporation shall have power to purchase, take, receive, or otherwise acquire, hold, own, pledge, transfer or otherwise dispose of its shares."

<sup>51</sup> Gen. Stat. Kans. (1939) 17-3004 (3).

<sup>52</sup> Cal. Civ. Code (1941) § 342 (3). It is interesting to note that the California statute gives preferential treatment to employee repurchase agreements, permitting the execution of such agreements from any surplus thereby placing such agreements in the class of compromising claims, buying out dissenters, eliminating fractional shares, and redemption agreements) whereas usual purchase or repurchase agreements are limited to earned surplus. Employee stock purchase plans are authorized by Cal. Civ. Code § 297a, but that section contains no limitation as to officers and directors. Directors and officers may secure repurchase, however, if there is *earned* surplus. Cal. Civ. Code (1941) § 342 (3). These two parts of the California statute must be construed together or there is a conflict.

provision. This section, except for the proviso as to officers and directors, is taken from the Louisiana statute<sup>53</sup> and the Ohio statute.<sup>54</sup>

There is at least one Maryland case indicating that employee repurchase agreements are not receiving treatment different from general purchase agreements. That is *Reed and Fibre Products Corp. v. Rosenthal*<sup>55</sup> in which the corporation employed Rosenthal for two years paying him partly in stock which the corporation agreed to repurchase if no extension of employment was worked out. The president also agreed individually to repurchase. The suit was against the corporation to force it to issue shares and against the president to repurchase them.<sup>56</sup> The case came up on demurrer and in a *dictum* the court said "there is nothing in the record to indicate that either of these conditions had or had not been complied with; but there being what on its face is a valid contract of the corporation to purchase [*i.e.*, repurchase], upon certain contingencies, shares of its own stock, we must, without any showing to the contrary, presume that the necessary condition had been complied with."<sup>57</sup>

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<sup>53</sup> Dart's Gen. Stat. (1939) § 1103 (I) (d) first enacted in 1928, Acts, No. 250 § 23.

<sup>54</sup> Throckmorton's Ohio Code (1940) § 8623-41(4).

<sup>55</sup> 153 Md. 501, 138 Atl. 665 (1927).

<sup>56</sup> *Ibid.*, at 516.

<sup>57</sup> *Ibid.*, at 514.