

Voting Trusts

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therefore promptly released the levy and demanded possession of the property under the chattel mortgage, and upon refusal commenced an action to recover possession. In behalf of the creditors the trustee in bankruptcy contested his right and claimed that the proceedings on the debt followed by judgment, execution and levy constituted a waiver of his rights under the chattel mortgage. The Supreme Court held there was no waiver and that the rule of election of remedies did not apply; as the two proceedings were not inconsistent and as long as the levy was released before sale, the rights under the chattel mortgage were not lost.

This case very well illustrates the fact that while one remedy may be a quicker and easier way of securing the relief desired, the rights given under the security agreement, whether it be chattel mortgage, pledge or conditional contract of sale, must in some cases be relied upon to obtain a complete satisfaction of one's claim.

The foregoing examples are demonstrative of the fact, that before the commencement of any proceeding, careful consideration should be given: as to whether the choice of one remedy will constitute an election of remedies and bar the right to pursue the other; and, secondly, which course of procedure will give ample relief in the speediest, easiest and safest way.

VOTING TRUSTS

BY MAX W. HECK, OF THE RACINE BAR.

The discussion of this subject is not intended to be a brief on the subject, but rather a discussion of a subject, which must, in the near future, be disposed of with the development of corporations and corporate interests, so that stockholders in such corporations may know their respective rights and responsibilities. A close examination of this subject, as passed upon by the various courts in this country, is apt to mislead attorneys as well as investors in stock, as to the real trend of discussion on the subject in America.

"Voting trusts are defined to be a term applied to the accumulation in a single hand or in the hands of a few, known as trustees, of the shares of corporate stock belonging to several owners, in order to control the business of the corporation." It may be

added, that this accumulation means the accumulation of a majority of such stock. American-English Encyclopedia of Law, volume 29, page 1077.

It is not hoped here because of necessary brevity of space, to give a complete review, but rather to make a few suggestions, which may lead to a further examination of the subject, in the hope of clearing up some of the misunderstandings now existing in regard to voting trusts.

Mr. Cushing writes on voting trusts as follows:

“The history of American corporations may be roughly divided into an early period, in which corporate organizations appeared chiefly in the development of banks and insurance companies, the later period of railroad expansion, and the modern period of the general application of corporate forms to mercantile enterprises. If a bank ceased to be solvent, holding only the assets usually acquired by such concerns and with no plant or real estate investment to be gradually developed, the natural result is the prompt winding up of the business, without any attempt at reorganization. When, on the other hand, the rapid expansion of railroads under ill-considered financial policies led to or threatened disaster, there existed the road itself which could not be abandoned, and the saving of which required the concerted action of either the former owners or new investors or of both. Likewise, with many of the large mercantile corporations more recently established, financial embarrassment could not properly be met, by those interested, merely by writing off an investment, for the same reason that there usually existed a property or business of some intrinsic value which ought not to be sacrificed, and which might under proper conditions be managed with some probability of ultimate success. Naturally, thus the history of corporate development in the last forty years has been marked by the introduction and refinement of the reorganization agreement or readjustment agreement. Usually as an incident or as a result of these, and after experience showing the ineffectiveness of pooling agreements and deposit agreements in meeting the needs of the case, there gradually came into use the voting trust agreement.

“In its early form the typical voting trust agreement evidenced little more than the stockholders’ transfer of their certificates, absolutely, to trustees, or in some instances to a trust company, and the undertaking on the part of the trustees to deliver stock

certificates on the expiration of the trust and in the meantime to distribute to the holders of trust certificates the amount of any dividends paid upon the stock * * *."

Like every other detail or process in corporate affairs, the voting trust may have been subject to such misuse as is inevitable when dependence is placed on the personal equation, but, on the other hand, while the object of some adverse comment, it has been much less harmful and much more productive of desirable results than most features of modern corporate development.

"When properly used, the voting trust," says the New York Law Journal, January 19, 1914, "has come to be recognized both by conservative bankers and by investors as a desirable and effective adjunct of modern finance, whose invention and whose application to difficult situations, have been amply justified."

Many instances have been published where voting trusts have not been merely successfully operated, but have saved many financial investments from becoming total losses, and have placed such institutions back upon a profitable interest-bearing basis.

Even in the early seventies this method of temporary control was not infrequent, and some cases have been made public where wonderful benefits have been derived therefrom. A number of states have passed Statutes limiting the time for which proxies can be given, some of them being limited to one year, thereby practically prohibiting the creation of a voting trust. There are many things to be said in the ordinary affairs of a corporation against the creating of a voting trust. We must not lose sight of the fact that when an individual buys stock in a corporation, he assumes certain responsibilities and liabilities as well as the receiving of certain benefits.

In *Bird Coal & Co. vs. Humes*, 157 Pa. St. 278, 27 Atl. 750, 37th Am. St. Rep. 727, the court says: "A stockholder, being the owner of his shares absolutely, he had a right to manage his own property as suited his own notion," which is one of the purposes of corporate organization of capital to facilitate independent acknowledgment and uses by each member of his fractional interest in the whole.

Too often a stockholder does not appreciate the necessity of his personal responsibility to the other stockholders and neglects to attend a stockholders' meeting, which the other stockholders have a right to expect, with reason. The giving of a proxy was intended, originally, to provide a means of representation for

non-present stockholders, who, because of sickness or other inability, were unable to attend a meeting. Many times people are induced to buy stock in a corporation, because they are led to understand that certain other persons, in whom they have an unusual degree of confidence, are not only stockholders, but are giving the corporation the benefit of their counsel and advise, so that we must not lose sight of the fact that the stockholder is presumed to give to the company, within reason, the benefit of his assistance, which is sometimes lost, by putting into the hands of others, through a voting trust, the right to vote his stock for a long period.

Mr. Cushing in his work on Voting Trusts, page 100, says:

“The law relating to voting trusts was earlier somewhat uncertain, due in part to a lack of thoroughness and of exact analysis in many of the decisions on the subject, and due also in part to the fact that in a considerable proportion of the cases, no appeal having been taken, the state of the law rested on the opinion of a court first instance. Suits involving the validity or effect of voting trusts have usually been commenced shortly before corporate elections and coupled with an application for an injunction, the decision on which has substantially determined the case so far as the pending election might be concerned, after which, unless substantial interests were at stake, the question at issue in the particular case has been permitted to become largely academic * * *.”

The commonest and also the most indefinite test applied to the validity of a voting trust has been its relation to public policy. The application of this rule has been as elastic as were the earlier standards of equitable relief, while the restrictive force attributed to public policy has varied greatly. On the one hand is the liberal doctrine which has been expressed by Justice Holmes, then Chief Justice, in *re Brightman vs. Bates*, 175 Mass. 105: “We know nothing in the policy of our law to prevent a majority of stockholders from transferring their stock to a trustee with unrestricted power to vote upon it.” In *Bowditch vs. Jackson Co.*, 76 N. H. 351, the court says: “Judged by the strictest rule of a stockholder’s right to the free and honest judgment of his co-stockholders, the agreement here made by more than three-fourths of the stockholders is a legitimate arrangement for carrying out their purpose.” “Even the cases holding the particular agreements then under consideration to be invalid, usually recognize the

proposition that there may be a valid voting trust." Early recognizing the proposition that there may be a valid voting trust, the Vermont court took a similar view in re: *Thompson-Starrett Co. vs. Ellis Granite Co.*, 86 Vt. 282.

The New Jersey Equity Court took a similar view in *Chapman vs. Bates*, 61 N. J. Eq. 658, and in *Warren vs. Pimm*, 66 N. J. Eq. 353; the court in a minority opinion, being divided seven to six, said: "It is now settled by a decision of this court that pooling or combining of stock, where the object is to carry out a particular policy with a view to promote the best interest of all the stockholders, is not necessarily forbidden." In the dissenting opinion in *Bridgers vs. First National Bank*, 152 N. C. 293, the judge says: "I am of opinion that such agreements among stockholders of a private corporation are not per se void or against public policy, but that their validity should be determined by the propriety and justness of the ultimate purpose which is sought to be accomplished. This is now the generally accepted view * * *. There is no more objection to assigning certificates of stock in a private corporation in trust for a lawful purpose than any other property." In re *Boyer vs. Nesbit*, 227 Pa. 398, the court held that it was not against public policy because the agreement contained "all the essential elements of an active trust."

In re *Harvey vs. Linville Improvement Co.*, 118 N. C. 693, the court took the opposite view and says bluntly: "In short, all agreements and devices by which stockholders surrender their voting powers are invalid." Following the opinion in the decision of *Cone vs. Russell*, 48 N. J. Eq. 208, which case involved a clear illegality of purpose.

The Harvey decision was followed in *Sheppard vs. Rockingham Power Co.*, 150 N. C. 776. The court there held the agreement to be against public policy and illegal. This case was followed by *Worth vs. Knickerbocker Trust Co.*, 152 N. C. 242. The court there assumed the law to be settled and spoke of "a voting trust, forbidden by the law." In *Griffith vs. Jewett*, 15 Weekly Law Bull. 419, the court is quoted as saying: "It is said to be the 'universal policy' of the law 'that the control of the stock shall be and remain with the owners of the stock.' The right to vote is an incident of the ownership of the stock and cannot exist apart from it."

In re *Warren vs. Pimm*, 66 N. J. Eq. 353, the proposition was expressed in the prevailing opinion of the court as follows: "Any

arrangement that permanently separates the voting power from stock ownership nullifies, to the extent of the stock involved, the annual submission of the question of the management of the company to the stockholders. Where, as here, the arrangement includes a majority of the stock, and extends for a period of fifty years, it renders all annual elections in the meantime a hollow form."

The voting trust for a period of fifteen years in *Bridgers vs. First National Bank*, 152 N. C. 293, was overthrown on the bald ground of public policy, although the court admitted that in exceptional cases some good might be accomplished by such agreements. "Yet, in our opinion, the general effect is vicious and in contravention of a sound public policy." A great many of the courts in this country, however, refused to take this view.

The specific ground most frequently taken by the courts which hold voting trust agreements to be repugnant to public policy is that they are illegal because the voting power in stock is separated from the legal ownership.

As to the separation of the voting power from the legal ownership, a significant case is that of *Elger vs. Boyle*, 126 N. Y. Supp. 946, in which a testator directed that certain stock held by his testamentary trustees should be voted by them as directed by six persons named in the will. On the pertinent branch of the case Justice Bischoff's opinion is as follows: "I find no force in the contention that the trustees, as holders of the stock, cannot be controlled in their manner of voting. The power to vote stock incidental to ownership of the stock itself may not be taken from the holder in invitum; but he may certainly qualify his ownership by his own consent that another may vote for him, as in the familiar instance of a vote by proxy, or may accept the ownership with a condition which involves this consent, as here. These trustees became possessed of the stock, not as their own asset, but solely by virtue of the will and of the conditions which the will imposed. One condition involved their consent to a restriction of their voting power, and no rule of law or of public policy is offended by giving effect to that consent."

On the other hand, in *re Tunis vs. Hestonville, etc., R. R. Co.*, 149 Pa. 70, the court says (this being also a case of a will), "the right of voting trust is inseparable from the right of ownership. The one follows as a sequence from the other, and the right to vote cannot be separated from the ownership, without the consent of the legal owner."

There seems to be no doubt that when the agreement is made in bad faith for the purposes of controlling the board and raising salaries, or any other bad faith, that the agreement will be set aside. *Fennessy vs. Ross*, 5 App. Div. N. Y. 342; *Guernsey vs. Cook*, 120 Mass. 501; *Snow vs. Church*, 13 App. Div. N. Y. 108. These agreements have been also set aside because of their being in restraint of trade and because of not being based upon a real consideration. The restraint of trade usually arises when one corporation tries to control another. *Hafer vs. New York L. E. & W.*, 14 Weekly Law Bull. 68.

One of the most important points upon which courts disagree is whether or not such a voting trust agreement is revocable or not. In *Vanderbilt vs. Bennett*, 2 Rlwy. & Corp. L. J. 409, the court held it to be revocable.

Restraint on competition is also so held as a reason for setting aside voting trusts re *Clarke vs. Central R. R. & B. Co.*, 50 Fed. 338. In re *Shepaug Voting Trust Case*, 60 Conn. 553, the court advanced as one of the reasons for not upholding a voting trust, an agreement for secret profits.

One of the most interesting cases upon voting trusts is that of the *Carnegie Trust Co. vs. Security Life Ins. Co.*, 111 Va. 1; 68 S. E. 412; 31 L. R. A. (N. S.), page 1186. In this case the voting trust agreement was founded upon mutual agreement only, as a consideration, and the court held that the consideration was sufficient. This agreement ruled for a period of more than 25 years, and it was sustained as not against public policy, and the court also held in this case that it was an active and not a passive trust. They also held that it did not separate the ownership of the stock and the beneficial interest, so as to render the transaction void. This case is especially referred to because in the notes to the case the whole subject is very extensively treated.

The contrary view is held in *Bridgers vs. First National Bank*, 152 N. C. 293, previously cited, also reported in 67 S. E. 770.

In the case of *Smith vs. San Francisco, N. P. Ry. Co.*, 115 Cal. 584, 47th Pac. 582 and 35 L. R. A. 309, the court sustained the legality of a voting trust, as also in *Clark vs. Central Ry. & Banking Co.*, 50th Fed. While in re *Harvey vs. Linville Improvement Co.*, 118 N. C. 693; 26 S. E. 489; 32 L. R. A. 265, hold the opposite view.

The case of *Shepaug Voting Trust Case*, 60 Conn. 553; 24 Atl., page 32, is one of the leading cases against voting trusts. The court goes very far in this case in holding such a contract

as illegal and contrary to public policy. In many respects this case is the leading case on the subject. In reviewing this case and the notes thereon, many cases will be found approving of this rule. One of the principal doctrines in this line of cases, which tends to be opposed to the creation of voting trusts, is the proposition that the trust is revocable. Of course, it can be readily seen that if the trust is revocable there can be very little purpose in the creation of such a voting trust.

One of the late cases on the subject is that of *Luthy et al, vs. Ream et al*, reported in the 270 Ill. 170; 110 N. E. 373. This case was decided in October, 1915. In this case the court reviews the whole subject of voting trusts from all of its angles, and reviews many of the decisions herein referred to, and it seems to agree that the better doctrine is that of the line of cases which hold voting trusts generally as contrary to public policy and illegal. It cites approvingly the *Shepaug Voting Trust Case, supra*; *Kreisel vs. Distilling Co.*, 61 N. J. Eq., 5, and many other cases herein referred to, and in approving of them the court uses this language:

“The principle to be deduced from these cases is that the holders of the majority of the shares of stock in a corporation may control its management, and every person who becomes an owner of stock has a right to believe that the corporation will, and to insist that it shall, be managed by the majority; that the power to vote is inherently attached to and inseparable from the real ownership of each share, and can only be delegated by proxy, with power of revocation; that each stockholder must be free to cast his vote, whether by himself or by proxy, for the best interest of the corporation; and that each stockholder has the right to demand that every other stockholder, if he desires to do so, shall have the right to exercise at each annual meeting his own judgment as to the best interest of all the stockholders, untrammelled by dictation, and unfettered by the obligation of any contract.”

Thereafter reviewing the cases decided by the court, contrary to this view, and expressly referred to *Smith vs. San Francisco & North Pac. Ry. Co.*, 115 Cal. 584, 47 Pac. 582, 35 L. R. A. 309, 56 Am. St. Rep. 119; and in *Carnegie Trust Co. vs. Security Life Ins. Co.*, 111 Va. 1, 68 S. E. 412, 31 L. R. A. (N. S.) 1186, 21 Ann. Cas. 1287, the court says: “These cases are inconsistent with the views which we have expressed and the cases cited in support of them, but in our judgment the latter cases stated the true rule.”

The court also quotes approvingly the following language in the *Shepaug Voting Trust Case*, 60 Conn. 579 and 24 Atl. 41, previously cited:

"It is the policy of our law that an untrammelled power to vote shall be incident to the ownership of the stock, and a contract by which the real owner's power is hampered by a provision therein that he shall vote just as somebody else dictates is objectionable. I think it against the policy of our law for a stockholder to contract that his stock shall be voted just as someone who has no beneficial interest or title in or to the stock directs, saving to himself simply the title, the right to dividends and perhaps the right to cast the vote directed, willing or unwilling, whether it be for his interest, for the interest of the stockholders, or for the interest of the corporation, or otherwise. This I conceive to be against the policy of the law, whether the power so to vote be for five years or for all time. It is the policy of our law that ownership of stock shall control the property and the management of the corporation; and this cannot be accomplished, and this good policy is defeated, if stockholders are permitted to surrender all their discretion and will, in the important matter of voting, and suffer themselves to be mere passive instruments in the hands of some agent, who has no interest in the general prosperity of the corporation. And this is not entirely for the protection of the stockholder himself, but to compel a compliance with the duty which each stockholder owes his fellow stockholder to so use such power and means as the law and his ownership of stock give him that the general interest of stockholders shall be protected, and the general welfare of the corporation sustained, and its business conducted by its agents, managers and officers, so far as may be, upon prudent and honest business principles, and with just as little temptation to and opportunity for fraud, and the seeking of individual gains at the sacrifice of the general welfare, as is possible. This, I take it, is the duty that one stockholder in a corporation owes to his fellow stockholders; and he cannot be allowed to disburden himself of it in this way. He may shirk it, perhaps, by refusing to attend stockholders' meetings, or by declining to vote when called upon; but the law will not allow him to strip himself of the power to perform his duty. To this extent, at least, a stockholder stands in a fiduciary relation to his fellow stockholders."

In view of the decision of the Illinois Court just referred to the decision of the New Hampshire Court, *Chas. P. Bowditch et*

al. vs. Jackson Co., et al., 76 N. H. 351; 82 Atl. 1014; L. R. A. 1917 A, page 1174, is interesting. The court says in regard to voting trusts in that case on page 1180 L. R. A.: "The legality of the votes passed at the meeting of the Jackson Company stockholders is questioned on account of the nature of the trust agreement under which the majority of the stock was then held, and because the trustees voted more than one-eighth ($\frac{1}{8}$) of the entire stock. While the decisions upon the first question are not entirely in accord, yet substantially all of them recognize that an agreement to vote stock in a certain way may be valid. The rule is well stated in the case, largely relied upon by the plaintiff.

"If the transfer of the legal title to the stock is made and accepted under an agreement of the stockholder, it deprives him of all power to direct the trustee, and all opportunity to exercise his own judgment in respect to the management of the affairs of the corporation, then, whether the transaction is open to the objection of other stockholders as depriving them of the right they have to the aid of their co-stockholders, must be dependent upon the purposes for which the trust was created, and the powers that were conveyed.

"If stockholders, upon consideration determine and adjudge that a certain protection for conducting and managing the affairs of the corporation is advisable, I have no doubt that they may, by power of attorney or the creating of a trust, or the conveyance to a trustee of their stock, so combine or pool their stock, as to provide for the carrying out of the conditions so determined upon. But if stockholders combined by their mode to protect and convey to others the formulation and execution of a plan for the management of the affairs of a corporation, and exclude themselves by acts made and attempted to be made irrevocable for a fixed period, through the exercise and determination thereof, or if they reserve to themselves any benefits to be derived therefrom, to the exclusion of other stockholders who did not come into the combination, then in my judgment such combining and the acts to effectuate it are contrary to public policy, and our stockholders have a right to its not being put into operation," citing *Kreissel vs. Distilling Co.*, 61 N. J. Eq. 5, 47 Atl. 471.

The court further said: "An examination of the cases chiefly will disclose that in nearly all of them where the agreement was held invalid, there were stipulations or covenants which infringed this rule. The proposition that it is as legitimate for a majority of stockholders to combine, as for other people, and that com-

bining is illegal, if the gain was to be at the expense of the corporation, or in some way to work a wrong to the other stockholders, are generally recognized as sound law." Further quoting: "Even the cases holding the particular agreement then under consideration to be invalid, usually are recognized with the proposition that there might be a valid voting trust." Citing: *Shepaug Voting Trust Case*, heretofore cited.

A review of these cases must leave a practitioner in this state all at sea as to what he might expect from the Supreme Court of Wisconsin. The only expression I see by the Wisconsin Supreme Court is in *Goetzinger vs. Donahue*, 138 Wis. 103, and which is obiter-dicta. Until either the Supreme Court of the United States, or the Supreme Court of the State of Wisconsin passes upon this subject in a positive and definite manner, the bar of this state must of necessity speculate as to what view our courts will take. In view of the fact that such a case can only be considered in an equitable proceeding, the writer cannot refrain from expressing the judgment that a voting trust can be created when the consideration therefor, and the motives therefor, are to the advantage and best interests of all the stockholders, otherwise it would be practically impossible for a corporation to secure financial assistance when it was most needed, because in large financial loans, the loaning party would insist on stable management, which can only be secured by the knowledge that a majority of the stockholders will continue a management approved of by those who have financial interests at stake.

The writer is also of the opinion that where a stockholder had been secured because of his influence either financially, or because of his technical ability, and as a condition required that the management be planned in such a way that he would know that his policy would be continued, so that he might be entitled to protection in the investment of his money, such stockholders are entitled to such protection by means of a stable policy, which can only be secured to him by the means which will provide for the control for a definite fixed period.

There are many other things that the writer could think of which ought to give sufficient weight and force to the support of such a voting trust agreement, but the writer can readily understand that a court has reason to look upon these agreements with extreme caution, and is of the opinion that the burden should be upon those attempting to carry out such an agreement to show not only that it is made in good faith, and for a valuable con-

sideration, but that the best interests of all of the stockholders are promoted by it.

I cannot refrain from expressing the opinion, however, that it is more a question for the legislature to use judgment in protecting stockholders by surrounding these agreements with proper limitations, rather than for courts to set them aside as against public policy.

IMPUTED NEGLIGENCE AS APPLIED AGAINST A GUEST IN A PRIVATE CONVEYANCE

(A CRITICISM OF THE WISCONSIN RULE.)

BY WALTER D. CORRIGAN, OF THE MILWAUKEE BAR.

The Wisconsin cases hold that the negligence of a driver of a private conveyance is imputable to the occupant.

The rule is founded on an implied relation of Principal and Agent.

This doctrine, now generally repudiated or greatly qualified, first found expression in Wisconsin in *Prideaux vs. Mineral Point*, 43 Wis. 513-526-531, where it was held that:

“The driver of a private conveyance is the agent of the person in such conveyance, so that his negligence contributing to the injury complained of by such person will defeat the action.”

While such had substantially been assumed to be the law in *Houfe vs. Fulton*, 29 Wis. 296, the principle had not received deliberate sanction. *Prideaux Case, Supra*, 530.

The court apparently hesitated to take this position and was in large part led so to do by the English case of *Thorogood vs. Bryan*, 8 C. B. 115, and the case of *L. S. and M. S. Ry. Co. vs. Miller*, 25 Mich. 274, and the New York case of *Beck vs. Ferry Company*, 6 Roberts 82. This becomes important because of the later decisions of those courts hereinafter considered.

In the *Prideaux* case, Mrs. P., with another lady, was in the back seat of a carriage, and through the negligence of the driver the carriage went over an embankment.

In *Otis vs. Janesville*, 47 Wis. 442, plaintiff and several other persons were riding along a highway in a private conveyance,