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Horace LaFayette Wilgus

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PURCHASE OF SHARES OF CORPORATION BY A DIRECTOR FROM A SHAREHOLDER.

IT is generally laid down in the encyclopedias and text books, and affirmed in many court opinions that "the doctrine that officers and directors [of corporations] are trustees of the stockholders, applies only in respect to their acts relating to the property or business of the corporation. It does not extend to their private dealings with stockholders or others, though in such dealings they take advantage of knowledge gained through their official position."¹ Much of this doctrine is based upon the language of Chief Justice SHAW in *Smith v. Hurd*² decided in 1847. He said: "There is no legal privity, relation, or immediate connection between the holders of shares in a bank, in their individual capacity on the one side, and the directors of the bank on the other. The directors are not the bailees, factors, agents, or *trustees of such individual stockholders.*" This case was an action on the case at common law, by an individual share holder against the directors for damages due to various acts of negligence and malfeasance in office through a series of years, in consequence of which the whole bank capital was wasted and lost, and the plaintiff's shares, along with the others, became of no value. In sustaining a demurrer, the court gave the following reasons for the rule above: (1) The corporation is a distinct person in the law, in whom the whole stock and property are vested. (2) The individual members have no right to intermeddle with the property, simply because they are not the legal

¹ 21 Am. & Eng. Enc. of Law, 2d Ed. 898; 10 Cyc. 796; 1 Morawetz, Priv. Corp. p. 537 n. 1, § 565; Taylor, Priv. Corp. 5th Ed. § 698; Cook, Priv. Corp. 6th Ed. § 320; Elliott, Priv. Corp. 3d Ed. § 502; 3 Clark & Marshall, Priv. Corp. § 616, (b), (c); Marshall, Priv. Corp. § 378; Purdy's Beach, Priv. Corp. §§ 356, 743; 3 Thompson, Priv. Corp. 1st Ed. § 4034; Machen, Modern Law of Priv. Corp. § 1637.

² 12 Met. (Mass.) 371, 46 Am. Dec. 690.

owners of it. (3) Injury done to the capital stock by impairing its value is not in the first instance a damage to the stockholder.

(4) Shares do not constitute a legal estate and property, but a qualified, equitable interest, and an injury done to the stock is not an injury to such separate interest but to the whole body of stockholders in common.

The Supreme Court of the United States has recently been called upon to deal with that phase of the relation between the corporate officers and the individual shareholder arising out of the purchase of the shares of the latter by one of the former, in the case of *Strong v. Repide*,³ in which it overruled the decision of the Supreme Court of the Philippine Islands.⁴ The case grew out of the sale of the friar lands, about one-half of which were owned by the Philippine Sugar Estates Development Company, Limited.⁵ Repide was the owner of 30,400 of the 42,030 shares of this company, was one of its five directors, and had been elected by the board as the agent and administrator general of the company, and as such, without formal authority but after informal discussion at the directors' meeting, represented the company in the negotiations of the sale of its lands to the United States. The plaintiff, Mrs. Strong, was the owner of 800 shares of the stock in this company, which were in the possession of her agent, Jones, with power to sell, and who sold them on October 10, 1903, for \$16,000 Mexican currency. July 5, 1903, the United States offered to purchase all the friar lands at a price which would make plaintiff's 800 shares worth \$129,664 Mexican currency; this offer was rejected by Repide in his capacity as majority shareholder without consulting other shareholders. In the latter part of October, 1903, the government increased its offer to a price that made plaintiff's shares worth \$181,504 Mexican currency. All the owners of the friar lands, except the defendant, wished to accept this offer, but the defendant would not until the others offered to pay his company \$335,000 and the government offered to exclude 1000 hectares of the company's land. With these concessions, on December 21, 1903, defendant as attorney in fact for his company accepted the government's offer of purchase. In September, 1903, the defendant, while still holding out for a higher price for the company's lands, took steps to purchase plaintiff's stock which he knew was in the possession of

³ *Strong v. Repide* (1909), 213 U. S. 419, 53 L. Ed. 853, 29 S. C. 521.

⁴ *Strong v. Repide* (1907), 5 Off. Gaz. P. I. p. 72, reviewed 5 Mich. L. R. (April, 1907), p. 454.

⁵ The facts are partly taken from the report of the opinion of the Philippine Supreme Court.

Jones, who had an office next door to him. Instead of seeing Jones, he employed K (a relative of his by marriage), who in turn employed S, a broker, who had an office some distance away, to purchase the stock for him. K told S the stock was to be purchased for a member of his wife's family; beyond this, S did not know who wanted to buy; and Jones did not know, but if he had known defendant was purchasing, he would not have sold at the price he did. The articles of incorporation required a resolution of the stockholders in general meeting for the purpose of selling more than one hacienda of the company's land. No such meeting had been called when the stock was bought by the defendant, and in all the negotiations for the purchase of the stock not one word of the facts affecting the value of the stocks was made known to plaintiff's agent by the defendant or his agent,—the real state of the negotiations for the sale of the land was not mentioned, nor that it rested chiefly with the defendant to make the sale. During this time however the subject of the sale of the friar lands was frequently discussed in the public press, and the plaintiff and her agent knew the negotiations were going on and that defendant represented the company in the matter, but the state of the negotiations, or probabilities of sale, or the influential position of the defendant in the matter were not accurately known to, nor inquired into by, plaintiff's agent prior to the sale. The Civil Code provides that "Consent given by deceit shall be void,"—§ 1265; and "there is deceit when by words or insidious machinations on the part of one of the contracting parties the other is induced to execute a contract which without them he would not have made." The trial court found that the defendant concealed from plaintiff's agent "facts affecting the value of the stock which he in good faith was bound to reveal," and directed the defendant to return the 800 shares on repayment of the price, or pay plaintiff \$165,504 Mexican currency. The Philippine Supreme Court reversed this decision, on the ground that the code required "some positive act of fraud," "which includes false promises, the abuse of confidence," and of which there is no evidence; "it is absolutely erroneous to consider as consent obtained by deceit consent given upon insufficient information"; this was a "sale in which consent was freely given, without any deceit, without any information,—good, bad, or indifferent on the part of the purchaser," and "it was not preceded by insidious words or machinations of any kind whatever." Judge JOHNSON dissented, holding that the corporate directors occupy a fiduciary relation to the shareholders individually and collectively, and cannot be allowed to deal with the corporate property so as to reap individual benefit at the expense

of individual shareholders. The Supreme Court of the United States reverses the decision of the Philippine Supreme Court, but does not go so far as to affirm the view taken by Judge JOHNSON in his dissenting opinion.

The late Mr. Justice PECKHAM rendered the opinion. He defines "insidious machinations" as "a deceitful scheme or plot with an evil design, or in other words, with a fraudulent purpose," which "need not be by misrepresentations in words," but may be "by means of concealing or omitting to state material facts with intent to deceive." "This is the rule of the common law also; but in both cases it is based upon the proposition that under all the circumstances of the case, it was the duty of the party who obtained the consent, acting in good faith, to have disclosed the facts which he concealed. In such cases concealment is equivalent to misrepresentation."

"If it were conceded," says the court, "that the ordinary relations between directors and shareholders are not of such a fiduciary nature as to make it the duty of the director to disclose to the shareholder general knowledge which he possesses regarding the value of shares before he purchases, yet there are cases where *by reason of the special facts such duty does exist.*" The judge then states these special facts: (1) defendant was a director; (2) owned three-fourths of the stock; (3) was administrator general with large powers; (4) was engaged in negotiations which finally led to the sale of the land at a price which very greatly enhanced the value of the stock; (5) was the chief negotiator; (6) was acting substantially as the agent of the shareholders by reason of his ownership of shares and by acquiescence of other shareholders; (7) the negotiations were for the sale of the whole of the property; and (8) the lands were the only valuable asset owned by the company. The existence of these make "such a combination as rendered it the plain duty of the defendant to speak." Under these circumstances concealing his own identity, the state of the negotiations, and their probable result, and giving the check of a third person, were part of the deceitful machinations, and "the law would indeed be impotent if the sale could not be set aside or the defendant cast in damages for his fraud." The court does not review or discuss the authorities upon any of the propositions involved, but cites two cases, *Stewart v. Harris*,⁶ and *Oliver v. Oliver*,⁷ as illustrations of "*where by reason of special facts,*" a duty to give information ex-

⁶ *Stewart v. Harris* (1904), 69 Kans. 498, 66 L. R. A. 261, 105 Am. St. R. 178, 77 Pac. 277, 2 A. & E. Ann. Cas. 873.

⁷ *Oliver v. Oliver* (1903), 118 Ga. 362, 45 S. E. 232.

ists, and one case, *Tippicanoe County v. Reynolds*,⁸ illustrating the general rule that there is no such duty. These cases are referred to hereafter.

A review of the pertinent authorities, in chronological order, and their grouping together afterward, may be helpful in weighing the result and reasons arrived at in *Strong v. Repide*. The first case to be considered is *Walsham v. Stainton*,⁹ decided in 1863, by the English High Court of Chancery before Lords Justices KNIGHT BRUCE and TURNER overruling Vice Chancellor Sir W. PAGE WOOD.¹⁰ In this case H. S. and J. S. were brothers and the London agent and manager respectively of a corporation incorporated in 1773. Through a series of years these parties defrauded the company by selling large quantities of its goods at high prices, but entering the sale upon the records much below the sum received, and keeping the difference themselves. In 1816 this amounted to £120,000. These parties also placed their nephews in the accounting offices of the company, and required them to prepare fictitious balance sheets to be placed before the directors which would not show the true state of the company, in order that the stock might be purchased by them at less than its real value. In 1813 G sold shares to J. S., and in 1817 to H. S. at what was then supposed to be the value of the shares, based upon the reports of the company, but much below the real value, if the true condition had been known. There was no concealment of the identity of the purchasers, or of their official relation to the company. In the purchase there were no false statements then made inducing the sale, though the price was undoubtedly based upon the supposed condition due to the former false reports. This was not discovered until 1860, after all the parties were dead,—38 years after the transactions. The executor of G sued the executor of J. S. to hold him liable to account for the loss by the sale to H. S. Lord Justice TURNER stated the case thus: "two confidential agents of the partnership, Joseph Stainton and Henry Stainton, conspired together to obtain for themselves the shares of the parties in the concern, at an undervalue, by keeping the accounts of the partnership fraudulently, so as to conceal from the partners the true value of the shares and it was by means of this fraudulent conspiracy, these 40 shares were obtained by Henry Stainton at a price far below their real value." In holding that J. S. and H. S. were jointly and severally liable, he said further, "A more gross breach of duty on the part of an agent

⁸ *Tippicanoe County v. Reynolds* (1873), 44 Ind. 509, 15 Am. Rep. 245.

⁹ 1 De Gex, J. & S. 678 (66 Eng. Ch. R. 527).

¹⁰ *Walsham v. Stainton* (1863), 1 Hem. & M. 322.

towards his principal than is disclosed by this bill cannot well be conceived, and it is not denied that there would be a remedy at law against Joseph Stainton and his estate in respect to this breach of duty," and "though J. S. got no benefit of the sale to H. S., yet he stood in a fiduciary position toward the shareholder and was a party to the fraud, and he as well as H.S. was liable to W. for the real value of the shares." Here the defendants (1) defrauded the company, (2) conceal this, (3) made false reports to directors, and (4) this depressed the value of the shares to the damage of all the shareholders. There had been a partial recovery (£220,000) by the company from H. S. The whole case was treated as if there was a direct relation of agency and trust existing between the directors and individual shareholders, analogous to partnerships. The case seems to be one of actual fraud, without reference to any fiduciary relation.

Next is *Carpenter v. Danforth*,¹¹ in the Supreme Court of New York in 1868, SUTHERLAND, J. Here plaintiff was the administrator of the estate of G., who with the defendant had been an active trustee in the management of the company, ¹² which had declared no dividends, but applied all its profits to the enlargement of its business. When G. died he was the owner of 136 shares of the par value of \$50 each; the corporate property was subject to liens very nearly equal to the par value of the shares. There were no market quotations of the stock, and the plaintiff was wholly ignorant of the company's affairs. The shares were sold to one W. but for the use of the defendant then a director, in December, 1862, at \$60 per share. In May, 1863, extraordinary dividends (310 per cent) were declared and paid from extraordinary profits made from the extraordinary amount of work done—engraving the postage currency and the extraordinary price charged and in the end allowed by the United States government. The company had made an offer to plaintiff for his shares. The defendant told plaintiff he would do better by him than the company, and that he was buying the stock to get control of the company; and he spoke of what the company was doing for the government and of the report of the Secretary of the Treasury as bearing on the continuance of the work. These statements were true, but the postal currency engraving was not specifically mentioned. When the sale of the shares was made all the officers thought the continuance of the work on the postage currency was precarious and might be terminated at any time, and

¹¹ *Carpenter v. Danforth*, 52 Barb. (N. Y.) 581.

¹² The facts are partly taken from 19 Abb. Pr. 225.

no bill was rendered to the government therefor before February 1863, and was not allowed and paid till May, 1863. Until then there was no reasonable certainty as to what the company would be paid for the work.

On behalf of the plaintiff it was contended that "from the relation of a director and a shareholder, undue influence on one side and a corresponding trust and confidence on the other is to be presumed," and that the sale must be declared void unless the defendant paid full price and disclosed every fact known to him, or which with reasonable diligence he might have known, and unknown to the plaintiff. The court says to this: There is a trust relation between directors and shareholders, but it extends only to the management of the general affairs of the corporation. The title to the property is in the corporation. The directors are not trustees for *the sale of the stock* of the corporation. They have no power as directors to sell stock, except their own. Plaintiff's stock is not the subject of trust between plaintiff and directors, and the trust relation had no connection with plaintiff's stock except so far as good or bad management affects the value.

As to the duty to disclose material facts, the Court says: "It will not do to make the principle generally applicable. As to stocks having a regularly quoted price or market value, parties generally buy and sell with reference to *this* price rather than to the real value founded on knowledge of the corporation. As to such would it do to make the purchase of it by a director an exception, and say the parties dealt with reference to the supposed real condition of the corporation? Plainly not. But the duty from the mere trust relation must be the same where it exists, and my conclusion then is there is here no trust relation and no constructive fraud."

Further the court says if there is liability it must be because there is actual fraud,—either by false representation of a material fact, or fraudulent concealment of a material fact; and upon a review of the facts as above stated, held there was neither false representations, nor fraudulent concealment; but as to the latter adds: "I think then the question is, 'Did the defendant say or do anything to divert or prevent plaintiff, and which did divert or prevent him, from looking into or making inquiry into the condition of the company and its prospects for dividends especially as to the work for the government on the postal currency?' I think the sale should be set aside if this question be answered in the affirmative. I think not." While the opinion in this case is to the effect that a director is not a trustee for the individual shareholder so as to make it constructively fraudulent for him to purchase shares from the share-

holder, yet it seems that even if the director had been held to be such a trustee, the facts were such as to support the purchase anyhow, under the rule stated by PERRY that a "trustee may buy from the *cestui que trust* provided there is a distinct and clear contract, ascertained after a jealous and scrupulous examination of all the circumstances and proof that the beneficiary intended the trustee to buy, and there is a fair consideration, no fraud, no concealment, and no advantage taken by the trustee of information acquired by him in his character as such."¹³

The next case is *Board of Commissioners of Tiptecanoe County v. Reynolds*,¹⁴ decided by the Supreme Court of Indiana in 1873, WORDEN, J. The declaration alleged plaintiff was the owner of 570 shares of \$50 each in a railroad company of which the defendant was president and principal manager, and was, at the time of the purchase of the stock for \$25,650, or \$45 per share, negotiating a sale of the road, which was afterward consummated for a price which made plaintiff's shares worth \$342,000; and further that the condition of the company had been concealed by failing to declare dividends and by representations by the defendant that the stock was not worth its face, and that depreciation of the stock had been caused by losses, when he knew the accumulations of the company were sufficient to pay all debts and losses and leave the stock 1,100 per cent above par. Upon a *general denial* by the defendants the trial court found for him, and on a review of the evidence the majority opinion of the Supreme Court says: "We are satisfied that no actual fraud was established. The defendant doubtless knew much more about the condition of the affairs of the company and the value of the stock both present and prospective than the plaintiff. He purchased the stock greatly below its real value, as subsequent events established, but he paid the market value at the time, as far as it seems to have had a market value. It is not shown that there was any special trust or confidence reposed in the defendant by the plaintiff, which was violated by the former, or of which he took advantage. * * * Was the defendant in consequence of being a director and the president of the company, a trustee of the plaintiff as a stockholder, whereby it became his duty as a purchaser of the stock, to pay a fair and adequate price for it, to take no advantage of the relation which he bore to the company or the knowledge acquired thereby, and to disclose to the plaintiff all the material facts within his knowledge, not known to

¹³ Reeder v. Meredith (1906), 78 Ark. 111, 115 Am. St. R. 22; Perry, Trusts, § 195; Bispham, Equity, § 237.

¹⁴ Board &c. Tiptecanoe Co. v. Reynolds (1873), 44 Ind. 509, 15 Am. Rep. 245.

the plaintiff affecting the value of the stock?" After reviewing several cases including *Smith v. Hurd*, *Carpenter v. Danforth*, *Walsham v. Stainton*, and many others, not directly in point, the court says: "Stock in a corporation held by an individual is his own private property which he may sell or dispose of as he sees proper and over which neither the corporation nor its officers have any control. It is the subject of daily commerce, and is bought and sold in the market like any other marketable commodity. The directors have no control or dominion over it whatever, or duty to discharge in reference to its sale and transfer, unless it be, to see that proper facilities are furnished for that purpose. As the property of the individual holder, he holds it as free from the dominion and control of the directors as he does his lands or other property. * * * Such being the nature of the interest of the stockholder in his stock, and the directors having no control, power or dominion over it, or duty to discharge in reference to it, beyond the duty devolving upon them prudently to manage the affairs and property of the corporation itself, it seems to us to be very clear that in the purchase of stock by a director from the holder the relation of trustee and *cestui que trust* does not exist between them." DOWNNEY, C. J., rendered a vigorous dissenting opinion to the effect that the defendant was guilty of actual fraud, and if not, he occupied such a relation of trust and confidence toward the plaintiff as under the circumstances made him guilty of constructive fraud. Mr. TAYLOR says of this case: "The transaction which in this case was allowed to stand seems to the writer to have been eminently unfair, and indeed a rule—for which this decision is certainly authority—that directors in their dealings with shareholders are entitled to take advantage of their knowledge of facts not known to the latter, but which the directors are acquainted with by reason of their official position, seems of questionable propriety,"¹⁵ Judge THOMPSON also says of this case, "This holding is believed to be unsound, and the dissenting opinion of Chief Justice DOWNNEY is to be preferred."¹⁶

Fisher v. Budlong,¹⁷ decided by the Supreme Court of Rhode Island in 1873, is a case in which there was a special agency between the seller and purchaser of the shares. The plaintiff had upon the recommendation of the secretary of the company bought shares in an insurance company at \$54 per share. A few days later when the plaintiff told the defendant (who was president of

¹⁵ Private Corporations, 5th Ed. § 698, note 1.

¹⁶ Thompson, Private Corporations, 1st Ed. Vol. 3, § 4034.

¹⁷ *Fisher v. Budlong*, 10 R. I. 525.

the company) of the purchase the defendant said they were worth only about \$35, as the company had had many losses, and advised plaintiff to sell, and said he might hear of a buyer. A short time afterward the defendant told plaintiff he had a buyer at \$48 per share, and advised him to sell. Plaintiff said he confided in the defendant and would do so on his representations; they immediately had the shares transferred to a third party, but payment was made by the check of the defendant to whom plaintiff paid a commission for selling the shares. The shares were soon afterward transferred to the defendant. When the company was wound up within two years afterward, the shares were found to be worth about \$90 each. It was not fully shown that the defendant had misrepresented the condition of the company. The court however held the defendant liable because the defendant professed to be aiding the plaintiff in selling his stock and getting a good price for it, and was really acting as his agent in making a sale of plaintiff's shares.

In *Deaderick v. Wilson*,¹⁸ the Supreme Court of Tennessee, in 1874, by FREEMAN, J., upon demurrer to a declaration by shareholders in a railroad company against the directors charging them both officially and individually with conceiving and executing a scheme of speculating in the stock to the damage of the owners of it, and to the profit of themselves, that they availed themselves of their superior knowledge, influence and power, and other advantages incident to their positions as such officers and procured the stockholders to transfer to them their shares of stock at prices far below the prices that their superior information enabled them to foresee said shares would command; said: The legal proposition underlying the charge made is "that the officers are trustees for the individual owners of stock and as such cannot be allowed to make a profit out of their trust. * * * It is not in the line of their duty to sell the shares owned by the shareholders. Nor can it be said that such officers may not as individuals purchase and hold stock in the corporation of which they are members. * * * After all, the simple question involved is whether the officers and directors are free to purchase stock from a shareholder in the corporation on the same terms as others. To this there can be but one answer, that is, they may, unless prohibited by legislative restriction." The court relies on *Smith v. Hurd* and *Tippecanoe Co. v. Reynolds*, *supra*, and sustains the demurrer.

In *Grant v. Attrill*¹⁹ (1882), WHEELER, D. J., ruled on a demurrer

¹⁸ *Deaderick v. Wilson* (1874), 67 Tenn. (8 Baxt.) 108.

¹⁹ *Grant v. Attrill*, 11 Fed. 469.

to a declaration alleging: that the defendants, who held a majority of the stock on which only 50 cents per share of \$100 had been paid, elected defendant and others who acted with him as directors, and who made an assessment on the stock and threatened to make others rapidly for the purposes of the company, which were not in fact necessary, and which they did not intend to enforce if they could purchase the rest of the stock; that the plaintiff believing the threatened assessments would be made and enforced, and the money misapplied, sold his shares to defendants at \$2.50 per share; that the assessments were not made nor enforced; and that the stock turned out to be of great value,—did not state a cause of action. The court says defendant does not appear to have misrepresented or concealed any material fact, relative to the corporate franchises or property. What was represented or withheld related to the policy of management and plaintiff seems to have preferred to sell rather than risk this.

In *Gillette v. Bowen*²⁰ (1885), Judge BREWER said "that trust relations to the corporation do not, as to the stockholders, create trust relations *inter sese*." Here plaintiff was one of four directors who had transferred to T. one of the directors, \$500,000 of the mining corporation stock, upon his promise to procure a stamp mill for the company. T. failed to do this, but Bowen, another director, did procure a stamp mill, and the \$500,000 issued to T. was used to pay for it; later the vendor of the mill sold back part of this stock to Bowen and the other defendant directors, at a profit to themselves, for which plaintiff claimed they were liable to him. Judge BREWER says: "There being no confidential relations between Bowen and the complainant it devolves upon complainant to prove that Bowen's conduct was wrongful, and not upon Bowen to prove that it was rightful. * * * The wrong charged upon defendant Bowen is not proved and judgment should be rendered for him."

In *Perry v. Pearson*²¹ (1890), Perry was the owner of a large part of the stock in a lumber company of which he and Pearson were both directors. The company was not prosperous, and in 1884, Perry sold all his stock to Pearson for \$375,000. Two years later, the price of lumber had greatly increased, and the company sold out all its stock to third parties, at a profit of \$135,000. Perry then sued Pearson for his share of these profits,—on the ground that a confidential relation existed between him and Pearson as directors. The court said "He made the sale with his eyes open. * * * No misrepresentations

²⁰ *Gillette v. Bowen*, 23 Fed. 625.

²¹ *Perry v. Pearson*, 135 Ill. 218.

were made to him. He was as well acquainted with the value of what he was selling as were those who purchased from him. * * * If it be admitted that there were confidential relations between the parties we see nothing in the evidence to convince us there was any abuse of such relations."

*Crowell v. Jackson*²² in the Court of Errors and Appeals of New Jersey in 1891 ruled, by Chancellor MCGILL, that "In purchase or sale if there be no designed misrepresentation by words or deeds and no active intentional concealment, and no intentional silence where there is a duty to speak, an action for deceit will not lie. A director or treasurer of a corporation is not because of his office, in duty bound to disclose to an individual stockholder before purchasing his stock, that which he may know as to the real condition of the corporation affecting the value of that stock. He is to some extent trustee for the stockholders as a body, but does not sustain that relation to individual stockholders with respect to their several holdings over which he has no control." This case was an action for deceit by plaintiff against the defendant who was a director and treasurer of a printing company which *had made* a favorable sale of all its property of which the defendant knew and plaintiff did not know, and knew no facts to put him on inquiry. Knowing this the defendant bought the shares at a price for which the plaintiff in his ignorance was willing to sell but which was much below their real value.

In 1892 Mr. Justice STERRETT, of the Supreme Court of Pennsylvania, in *Krumbhaar v. Griffiths*,²³ held there was no liability on the part of the defendant to the plaintiff on these facts: the plaintiff was the owner, February 1, 1890, of twenty-five shares in a warehousing company. The market value of the shares was then \$42.50 per share; an offer had then been made by the company to lease its piers to the Reading railroad company, which had declined to accept the offer. Later the railroad offered to lease one pier at \$10,000 per year with an option to rent all the piers at \$6,000 per year for each pier; this was accepted and a lease executed, and confirmed by the shareholders February 3. Early in this month plaintiff received a note from a broker offering to sell his stock for him; he called at the office of the company February 8, and had an interview with the defendant who had been elected secretary February 3, and who showed plaintiff the annual report made February 3; on February 11, the defendant wrote plaintiff telling him he could find a pur-

²² *Crowell v. Jackson*, 53 N. J. L. (24 Vroom) 656.

²³ *Krumbhaar v. Griffiths*, 151 Pa. St. 223.

chaser for him. Plaintiff called the next day, and defendant offered him \$50 per share; plaintiff asked \$60 per share, but finally gave defendant an option at \$55 per share, which defendant exercised later in the day, and the sale was completed the next day, February 13. February 17, the railroad company exercised its option to lease all the piers, and when this became known in March, the stock rose to \$125 per share. Before February 17, it was not supposed the railroad would exercise its option, and the lease was not considered favorable. The plaintiff claimed that he asked the defendant if he knew of anything pending likely to increase the value of the shares, and the defendant answered he did not, and the court found this was true. The court said: "It seems there is no special confidential or fiduciary relation between an officer of a corporation and a person from whom such officer purchases the stock of the corporation."

In *Haarstick v. Fox*,²⁴ (1893), plaintiff was the president of a St. Louis transportation company in which M. (living in New York) was the owner of 1414 shares, which had belonged to her husband who died in 1888. In December 1889 she wrote plaintiff asking him what the market value of the shares was; he answered he thought he could sell them at \$65 or \$70, but it probably would take 30 or 60 days to place so large a block of stock. January 27, M wrote "Think stock is worth more; what is the very best you can do?" Plaintiff answered "We are having all rail competition, and I think the figure mentioned is about as much as you can realize." February 10, M wrote saying she had concluded to sell for \$100,000; plaintiff answered February 19, telling of losses amounting to \$75,000, and said "If you will sell the 1414 shares for \$92,500, I will undertake to dispose of them in 60 days"; February 25 M. wrote accepting the offer, but said she would not give possession for 40 days. Plaintiff answered that this was satisfactory, mailing the letter on March 1, but which did not reach M. until March 4, at Salt Lake City, where she had gone, was ill and died March 5, after being unconscious for 24 hours, and never knew the letter had been received. M.'s administrator refused to deliver the stock to plaintiff, it having a value April 10, of \$104,000. Plaintiff sued; the defense was that a confidential relation existed between plaintiff and M. which raised a presumption of fraud which can be rebutted only by proof that plaintiff had fully disclosed to M. all his information concerning the company prior to making the contract. The court held not so, and gave judgment for plaintiff, saying "So long as he

²⁴ *Haarstick v. Fox*, 9 Utah 110.

remains silent and *does not actively* mislead the person with whom he deals the transaction cannot be set aside for fraud."

In *Ritchie v. McMullen*²⁵ (1897), Judge TART held: "If a stockholder pledge his stock as collateral, with directors of the corporation, and the latter enter into a conspiracy to depreciate the price of the stock by using their power as directors, for the purpose of buying it in for less than its value, this is a wrong not against the corporation only, but against the pledgor for which there is a direct liability to him. * * * If such pledgee use his position as director and his vote as stockholder intentionally to depreciate the stock with the dishonest purpose of acquiring ownership at forced sale, this is a direct injury to his pledgor, and he cannot avoid direct liability to his pledgor for it, by pleading that the means by which he accomplished this wrong, and violated his duty as pledgee involved an injury to the corporation for which it may also recover damages." The judge relies on *Walsham v. Stainton*, above.

In *Brown v. DeYoung*,²⁶ decided by the Illinois Supreme Court in 1897, H. and M. owned 4,100 of 5,000 shares in a corporation of which M. was president. H. not agreeing with M. in the policy of management transferred his shares to the defendant who was to induce M. to adopt a policy of management suitable to H. and for which defendant was to receive \$1,000 per year, and on demand retransfer the shares to H. The defendant became secretary and as such was entitled to \$500 salary. Soon afterward defendant in collusion with M. and with the knowledge of H., but without the knowledge of other shareholders increased their salaries from \$500 each to \$1,500, then to \$2,500, and then to \$3,500. After this H. demanded the return of his stock, and defendant returned it. H. then sued defendant and M. for the amounts they wrongfully paid themselves, making the corporation a party, and allowing the innocent shareholders to join as parties plaintiff. The corporation disclaimed any interest in the sum, and it was held H. could not recover because he knew of the transaction, but that the innocent shareholders should recover individually as if the fund to be recovered should be declared as a dividend upon the stock in proportion to their holdings and the defendant be allowed to keep the balance.

In *Mulvane v. O'Brien*,²⁷ in the Supreme Court of Kansas, in 1897, DOSTER, C. J., held Mulvane was liable to O'Brien upon these facts: Mulvane was president and O'Brien secretary of a corporation, with equal opportunities to know the conditions of the corporation.

²⁵ *Ritchie v. McMullen*, 79 Fed. 522, 25 C. C. A. 50.

²⁶ *Brown v. De Young*, 167 Ill. 549.

²⁷ *Mulvane v. O'Brien*, 58 Kans. 463, 49 Pac. 607.

While O'Brien was ill and at Hot Springs, Arkansas, Mulvane wrote O'Brien proposing to effect a sale of all the corporate stock at par, and asked O'Brien to transfer his shares in blank to him, to be delivered in case the sale went through. O'Brien did this. Mulvane was at the time negotiating for a sale at much above par, and effected a sale for \$150,000 more than par. He *concealed* this from O'Brien and settled with him at par. *Held* that Mulvane was liable, on the ground that he was a special agent of O'Brien to effect the sale of the stock, and must account to him for all the received.

In *Rafferty v. Donnelly*,²⁸ (1900) in the supreme court of Pennsylvania, the plaintiff charged the defendant directors with fraudulently voting themselves \$50,000 back salaries as officers of a corporation, fraudulently concealing this fact, and through an agent acting for defendants, inducing plaintiff to sell his stock to them for a price based upon the existing assets, debts, and liabilities, and without the plaintiff's knowledge that they had wrongfully paid themselves such back salaries. The court by Mr. Justice BROWN said: "If they did directly wrong him in his estate by fraudulently impairing its value, and by their concealment of their misconduct, he parted with his property for less than it was really worth, he would upon proper averments and proofs be entitled to relief." The master however found that plaintiff failed to prove his averments. The court further said that "if he sold with knowledge, his bill was properly dismissed. At no time did the money belong to plaintiff, and if defendants improperly took it, plaintiff though a stockholder could not have sued to recover his share, but only by a proper suit to compel its return to the treasury, where it would have become assets, and preserved the real value of his stock."

In *Hume v. Steele*,²⁹ (1900) the defendant, who was engaged in the management of the corporation, in which plaintiff owned shares, made false accounts against the company and other false statements of its financial condition to the plaintiff, whereby he, believing them to be true, was induced to sell his shares to him at much less than their real value, was held liable on the ground of actual fraud.

In the English case of *Percival v. Wright*,³⁰ (1902), in the Chancery Division, the plaintiff sued to set aside a sale of his shares to the defendants who were directors of a coal company, with

²⁸ *Rafferty v. Donnelly*, 197 Pa. St. 423.

²⁹ *Hume v. Steele* (Tex. Cir. App.), 59 S. W. 812.

³⁰ *Percival v. Wright*, [1902], L. R. 2 Ch. 421.

power to manage, but not to sell all the property without a special resolution of the company. October 8, 1900, the plaintiff wrote the secretary asking if he knew of any one disposed to purchase shares; the secretary answered, asking price; plaintiff replied £12 5s per share; this was based upon a valuation made by independent valuers, and obtained by P. One of the defendants replied saying the letter to the secretary had been handed to him, and he would take the shares at the price named £12 5s. In the meantime plaintiff's solicitors had taken a new valuation, and plaintiff wrote he would take £12 10s. October 22, defendant wrote accepting this and directing that 85 shares be transferred to him, and 84 shares to each of the other directors. This was done. The shares had no market price, and were not quoted on the stock exchange. Later, plaintiff learned that at the time of these transactions, the directors were negotiating for the sale of all the corporate property at a price that would make the shares worth much more than £12 10s. The directors did not inform plaintiff of these facts. The sale of the property however did not go through, yet plaintiff sued to set aside the sale, and his attorney argued that as soon as a proposition for *sale of all the property was taken up*, the directors were trustees for the shareholders, but admitted they would not be concerning matters arising in the management such as a large profit, discovery of a new mine, or prospect of an extra dividend, etc. He also argued "that a share was like a share in a partnership, and in equity the property belongs to the shareholders, and directors as trustees cannot purchase the interest of the beneficiary without giving him full information. Incorporation cannot affect this broad equitable principle that the shareholders *inter se* are in the same position as partners." Mr. Justice SWINFEN EADY, however held otherwise,—“directors are trustees of the company's property, as an entity distinct from shareholders,” and said “I do not adopt the view that the position of the shareholders *inter se* was the same as that of partners or shareholders in an unincorporated company.” *Walsham v. Stainton*, above, was not referred to either in the argument or in the opinion.

In *Walsh v. Goulden*,³¹ (1902), the facts were: The defendants, directors of a gas company secured options from all the shareholders to purchase their stock at double the par value, having at the time an option with another company to sell the entire stock and property for the same price, and of which plaintiff was aware when he gave his option. Later, the directors perfected the sale

³¹ *Walsh v. Goulden*, 130 Mich. 531.

for this price and an additional sum to pay the debts of the company. Still later, but before the sale was completed, the purchasing company agreed to give each of the defendants \$5,000 in bonds and \$1,200 in stock of the purchasing company, if they would become directors thereof, and to which they consented. Judge GRANT of the Supreme Court of Michigan held that the defendants, not having made false representations or secret agreements by which they were to profit at the expense of the shareholders, were not liable to the plaintiff for any stock or bonds so received. Directors stand in a fiduciary relation to the corporation itself, but not to the stockholders individually when dealing with them for the purchase or sale of stock; and some actual misrepresentation is necessary to constitute fraud.

In 1903, the Supreme Court of Washington, in the case of *O'Neile v. Ternes*,³² held there was no liability on the following facts: Plaintiff was the owner of 100 shares of stock in a transfer company, by a specific legacy under a will of which the defendant was executor, and at the same time president and general manager of the company; the shares,—par value \$20,—were appraised at \$4.75 per share. Plaintiff wrote defendant that she had been offered \$1,000 for the shares, and if he wanted them at that price he could have them. Defendant immediately accepted the offer, paid the price and had the shares transferred to his wife. There was no evidence that the shares were worth more at the time of purchase. Plaintiff testified that she did not rely on the defendant's statements, that she did not believe what he had told her, that she knew that the stock was worth more, and she sold it because she wanted to get something out of it. Afterward, plaintiff was offered \$1,500 for the stock, and she then made an effort to repudiate the sale, tendering back the \$1,000 and interest, and demanding a retransfer, charging "betrayal of confidence and violation of trust obligations." The court by ANDERS, J., held that no trust relation arising out of his office existed between defendant and plaintiff.

In *Oliver v. Oliver*,³³ (1903), the Supreme Court of Georgia easily found a liability on the part of the defendant, who, while president of a cottonseed oil company sought and obtained options from the shareholders at \$110 per share, saying there was no longer profit in the business, more mills were being built, and he wanted to be in a position to sell out, if opportunity offered, to the benefit

³² *O'Neile v. Ternes*, 32 Wash. 528.

³³ *Oliver v. Oliver*, 118 Ga. 362.

of all. At the end of the year the defendant reported the company had lost money and omitted certain assets from the statement of the company, and no dividend was declared; under these circumstances the plaintiffs, believing the options were to sell for not less than \$110 per share, and more for the benefit of all if more could be obtained, allowed the options to continue, and the defendant was thus constituted agent for this purpose; he then had entered into negotiations for the sale of the shares, completed in August, at the price of \$185 per share; he borrowed money, paid the shareholders \$110 per share, and took a transfer to himself, keeping the extra \$75 per share after the sale was completed, and repaying the money borrowed. The court, by LAMAR, J., in holding the defendant liable, after saying that all authorities agreed that he was a trustee for the *company* adds: "But the fact that he is a trustee for all is not to be perverted into holding he is under no obligations to each. * * * That he is primarily trustee for the corporation is not intended to make the artificial entity a fetich to be worshipped in the sacrifice of those who in the last analysis, are the real parties in interest. No process of reasoning and no amount of argument can destròy the fact that the director is in a most important and legitimate sense, trustee for the stockholder." If the market or contract price differs from the book value there is no duty to point that out, for in theory this information is equally accessible to both. If the officer has information his duty to the company requires him to keep secret, this overrides his duty to disclose to the shareholder,—but this does not permit him to use it to his own advantage and to the disadvantage of the shareholder, it only prevents him from then dealing with the shareholder. If he has information which affects the selling price, and which can be disclosed to the shareholder without detriment to the company "the director before he buys is bound to make a full disclosure. In a certain sense the information is a *quasi-asset* of the company, and the shareholder is as much entitled to the advantage of that sort of an asset as to any other regularly entered on the list of the company's holdings. If the officer should purposely conceal from a stockholder information as to the existence of valuable property belonging to the company, and take advantage of this concealment the sale would necessarily be set aside. The same result would logically follow where the fact giving value to the stock was of a character which could not formally be entered on the records. When the director obtains the information giving added value to the stock by virtue of his official position, he holds the information in trust for the benefit of those who placed him where this knowledge was obtained, in

the well founded expectation that the same should be used, first for the company, and ultimately for those who were the real owners of the company. The director cannot deal on this information to the prejudice of the artificial being called the corporation, nor on any sound principle can he be permitted to act differently towards those who are not artificially but actually interested * * * The shares are but the paper evidence of the interest which the stockholder has in the *property* under the control of the director. In their sale the stockholder disposes not only of the lithographed or engraved scrip but of his holdings in property. And when the director deals with a stockholder for the purchase of shares he is not buying paper but in effect buying an undivided and substantial interest in property which has been committed to the director's care, custody and control. * * To say that a director who has been placed where he may himself raise or depress the value of the stock or in a position where he first knows of facts which may produce that result, may take advantage thereof, and buy from or sell to one whom he is directly representing, without full disclosure and putting the stockholder on an equality of knowledge of these facts, would offer a premium for faithless silence, and give a reward for the suppression of truth. It would sanction concealment by one who is bound to speak and permit him to take advantage of his own wrong,—a thing abhorrent to a court of conscience."

So, too, in *Morrison v. Snow*³⁴ (1903), a liability was easily found by the Supreme Court of Utah. Here plaintiff agreed to deed to a mining company, formed by the defendant, mining claims for 300,000 shares, half to be issued to plaintiff and half to the defendant. This was done. A mining engineer reported favorably upon the claims, saying some of the ore was worth \$296 per ton. The defendant requested that this report be not communicated to plaintiff, and after he had sold some of his shares at two cents a share, told plaintiff that he could not give the stock away, that the ore would not pay to ship, that he had advanced \$2,000 for running expenses, and that an assessment on the stock would be necessary, and offered plaintiff \$500 for 145,000 shares, saying he wished some one would make him such an offer. The statements of the defendant were false and known to him to be so. Plaintiff accepted the offer, and afterward learned of the falsity of the statements, and sued to rescind. *Held*, he was entitled to such relief. Here there was positive and intentional misrepresentation of material facts, and the case comes within the ordinary rule of actual

³⁴ *Morrison v. Snow*, 26 Utah 247.

fraud, and does not depend upon any special confidential relation.

In *Stewart v. Harris*³⁵ (1904), the defendant took hold of the affairs of a bank in 1893, when it was in a deplorable condition, having many notes due that had been charged off as worthless, and much land that was considered worthless, was carried on the books at a nominal valuation only. Under defendant's management the bank became prosperous; the supposed worthless notes were paid, and the lands became valuable, but these facts were kept so as not to appear in the statement of assets, and were not referred to in the published reports of the bank. Plaintiff owned shares, and inquired of defendant if dividends would be paid; the defendant said no, that the bank was in good condition, and the policy was to strengthen it; he also told the plaintiff of the bad condition when he took hold of it, and of the large amount of property then charged off, but said nothing about the property having since become valuable; he offered plaintiff \$1,000 for his shares, later \$1,400, and later purchased them for \$2,000, when they were then worth \$4,200, and still later a dividend of 120 per cent was paid. The defendant was held liable, and the Supreme Court, by ATKINSON, J., approved a charge by the lower court that directors stand in the relation of trustees to all stockholders not engaged in the management, and must give any shareholder from whom he purchases shares all pertinent information possessed by him affecting their value, before purchasing.

In *Hooker v. Midland Steel Co.*,³⁶ (1905), the defendant, president of a prosperous corporation, wrote the plaintiff in California stating the majority of the share holders had closed a deal for turning over all the property and shares of the corporation to New York parties, and asking plaintiff to forward his 72 shares with a sight draft for \$14,400; instead of doing this however, plaintiff sent his agent to make an investigation; this agent found the net profits had averaged 30 per cent for several years, that the surplus was \$200,000, and that the New York offer was over \$230 per share; defendant refused to give definite information, falsely denied the existence of a book (which however was not shown to contain pertinent information), but did not refuse or prevent an inspection of the books. Upon this report of the agent, and the repeated declaration by the defendant that the majority had determined to sell, plaintiff sold his shares to defendant at \$18,000, when

³⁵ *Stewart v. Harris*, 69 Kans. 498, 77 Pac. 277, 105 Am. St. R. 178, 66 L. R. A. 261. See the later case of *Stewart v. Smith* (1905), 72 Kans. 77, involving the same facts, where the method of valuing the shares and of measuring the damage is considered.

they were really worth \$32,000. The court held that the director is not a trustee for the shareholder, and besides in this case the plaintiff relied upon the independent investigation of his own agent, instead of the statements of the defendant.

In *Boulden v. Stilwell*,³⁷ (1905), where the president (S) and general manager (L) conspired to secure control of the corporation by inducing the plaintiff (B), the secretary and treasurer of the company, to sell his shares to (L), by S telling B he *was going* to sell his stock to L, that the company *was going* to fall down, and later that *he had* conditionally sold to L; and S and L had several times pretended to quarrel in the presence of B; and L told B he *had agreed* to buy S's stock, and would then control the company, and B *would be* deprived of his salary. Relying on these, B sold his shares to L, and a few days later S and L sold out to a third party for a sum much greater than the price paid to B, who sued for deceit. The court held the statements that the company *was going* to fail, that he *was going* to sell, and plaintiff *would be* discharged were not statements as to existing facts but declarations as to future contingent events, and that the other statements were not such as a prudent person would rely on, and further "where both parties have equal means of knowing the value of the thing sold a false statement by one relating to its value is not actionable fraud." The trust relation is not discussed.

In *Baird v. Grannis*,³⁸ (1907), Baird had in 1901 put his shares in a Louisiana land company in the hands of brokers in St. Louis to sell at \$125 per share. The company then had a contract with a coal company to sell its lumber at \$1.50 per 1,000 feet, with a provision that the price should be fixed every two years. Baird wrote the defendant, then president of the company, insisting that the price should be increased. January 20, 1902, the defendant wrote he was making such an effort with fair prospects of success, and that land in the vicinity was worth from \$12 to \$15 per acre. January 29, and 30, defendant wrote again giving details of negotiations, and that an increase would be obtained upon the return of an officer of the coal company. April 8, Baird's broker wrote him they had a purchaser at \$115; he answered he would sell for \$125; on April 16, they wrote they would take it at that price; and April 19, Baird telegraphed his acceptance, and the sale was completed April 21, the defendant being the purchaser. On April 22, the coal company unexpectedly offered to buy the land at \$15 per acre;

³⁶ *Hooker v. Midland Steel Co.*, 215 Ill. 444.

³⁷ *Boulden v. Stilwell*, 100 Md. 543.

³⁸ *Baird v. Grannis*, 208 Mo. 426.

this made the shares worth \$187, and the offer was accepted May 5. Upon learning this, Baird sued the defendant on the ground that as president and general manager it was his duty to disclose his identity as a purchaser of shares and disclose all information as to pending negotiations likely to result in an advantageous sale of the corporate property, and that the defendant stood in a trust relation to the plaintiff. The court, by VALLIANT, P. J., said we do not feel justified in deciding this point, because if the allegations are sufficient so to charge the defendant, the proof does not sustain the allegations, and does not show that the defendant misrepresented any fact or withheld any material information.

In *Wann v. Scullin*,³⁹ (1908), Mrs. Wann was the owner of 50 shares of stock in a ferry company, and was also a member of a voting trust including a majority of the stock. Scullin was president of the company and one of the three voting trustees, of whom Wade was another and also president of the Mercantile Trust Company in which Scullin was a large shareholder. Scullin and Francis also were joint owners of a railroad, which the Rock Island Railroad Company wished to buy, and did buy of Scullin and Francis April 21, 1902, paying them in cash and 5,000 shares each of Rock Island stock. Later, but the same day this deal was completed, the Rock Island company offered to buy the ferry stock, and to give \$500 per share for it, if a majority of it could be obtained. Scullin and Wade both thought a majority could be obtained at this price, and each offered to take that price for their own shares and to recommend to the other shareholders to sell at the same price, but insisted that the same offer should be made to all shareholders alike. An agreement was then made with Wade that the Mercantile Trust Company should handle the matter for a commission of 2½ per cent, and Wade insisted that this should be stated to shareholders. These transactions occurred in New York. Scullin and Wade returned to St. Louis, and immediately sent letters and telegrams to all ferry shareholders making them this offer, saying they proposed to sell their shares at this price, and advising them to sell. Up to that time the ferry stock had never brought over \$250 per share. Plaintiff immediately accepted the offer by telegram, and sent her stock to Scullin, who in the forenoon April 26, turned the stock over to the Mercantile Trust Company. Near evening of the same day, the Mississippi Valley Trust Company made an effort to secure ferry stock for another party, and by telegrams offered \$600 per share, and within the next few days, in the contest

³⁹ *Wann v. Scullin*, — Mo. —, 109 S. W. 688.

between the two trust companies, the price of the stock went as high as \$1,525 per share. As soon as Mrs. Wann learned of the contest she telegraphed Scullin and Wade to protect her interest. They did not answer, but the Mercantile Trust Company sent her a check for the whole amount at \$500 per share, claiming to have purchased it at that price on April 26th. Sometime later this check was cashed, and plaintiff sued Scullin for violation of his trust relation as an officer of the ferry company toward herself as a shareholder, on the ground that he had an interest in the trust company and in the railroad company that made the purchase of the ferry stock, which he did not disclose. It was held however, that this was not a fraud in law, and the failure to disclose was not shown to be a material inducement to the plaintiff to make the sale; and that the defendants could not have acted more fairly, and could not anticipate the war between the trust companies to secure the stock. The court reviews several cases upon the liability of a special agent for nondisclosure to his principal.

In *Von Au v. Magenheimer*,⁴⁰ (1908), MILLER, J., in holding defendants, liable used language very appropriate to cases of this kind. Here the plaintiff owned 483 of the 1,500 shares of a confectionery company; each defendant owned a like number of shares, and were respectively president and treasurer of the company. The plaintiff averred that defendants conspired to obtain her stock for less than its worth, and in order to depress its value, make her believe it was worth less than it was, and induce her to sell for an inadequate consideration they (a) refrained from declaring a fair dividend, and declared one of only 3 per cent; (b) increased the salaries of each from \$2,500 to \$7,500; (c) represented that the company suffered such reverses that it could not then pay more than a 3 per cent dividend, and it was doubtful if it ever could pay any more. The proof sustained these charges and further that the company had paid from 9 to 14 per cent dividends for several years before, that the losses had not been unusual, and that within a month after purchasing plaintiff's stock a 10 per cent dividend was declared, and salaries reduced to \$4,000 each. The court said "While the wrong now being considered was not technically a deceit its effect was to defraud plaintiff, and, in respect of the remedy at least should be treated as a fraud. It was a species of fraud; by the wrongful acts of the defendants the plaintiff was led to think that her stock was worth less than in fact it was, and we should not indulge in hair-splitting discriminations between that kind of deceit and a

⁴⁰ *Von Au v. Magenheimer*, 126 App. Div. (N. Y.) 257.

fraudulent misrepresentation or concealment respecting an existing fact, in view of the relations of the parties. If their relation was not strictly of the fiduciary character of trustee and *cestui que trust*, it was in a sense fiduciary; at least the parties did not deal on equal terms; indirectly if not actually, the defendants were the agents or trustees of the plaintiff, for in truth the entity called the corporation but represents the stockholders; in law the two are distinct, as the stockholders own merely their shares, not the property of the corporation; but in fact each share represents a given interest in the property of the corporation. While the defendants did not have control of the plaintiff's shares, they had control of the property represented by said shares, and their management of that property affected the value of the shares precisely as though the corporate property and the shares were one and the same. The defendants were not under the disabilities of trustees in respect of dealings with a *cestui que trust*, but their superior position imposed upon them some duty to the plaintiff as well as to the corporation, at least the duty not to take advantage of the opportunity afforded by their position to wrong her by any affirmative act designed to injure. Having the power to so manage the affairs of the corporation as to affect the value of her shares, they owed her the duty to refrain from intentionally abusing that power actually or apparently to depress the value of those shares for the purpose of acquiring them at an undervaluation. When they succeeded in securing her stock by that misuse of power they committed a breach of duty to her resulting in injury, and it is immaterial that their act may also have wronged the corporation. In view of the conditions under which business is now conducted it will be very unfortunate if it shall be held that the duty of corporate managers in respect of their conduct of the corporate affairs is solely to the corporate entity, and that however great a designed injury to an individual stockholder may be, he can only get redress through the corporation. The purpose of the wrong being to injure the plaintiff that should be held to have been its effect." GAYNOR, J.; dissents, on the ground there was no concealment or misstatement of any fact.

In *Steinfeld v. Nielsen*⁴¹ (1909), Steinfeld, though not an officer of the smelting company, yet by ownership of a large part of the stock, and having two of the three directors in the employ of a firm of which he was the managing agent, and to which the smelting company was largely indebted, caused the smelter to be shut down, in order that he might get rid of plaintiff as a director and superin-

⁴¹ *Steinfeld v. Nielsen*, — Ariz. —, 100 Pac. 1094.

tendent of the company, and purchase his stock at a low price; and in order to do this he falsely represented to plaintiff that the indebtedness was not being paid, caused him to be discharged, caused a false entry thereof to be made, and concealed the opportunity and the purpose of purchasing adjoining mining claims at prices that would add much to the property. DOAN, J., said: "We have no hesitation in holding Steinfeld, because of his power over the board of directors and the affairs of the company, and the domination he actually exercised over the corporation, sustained such a relation to the company and to the stockholders as does an officer having such management and control, and therefore occupied such fiduciary relation as he would, had he been an officer. * * * Undoubtedly the law makes it the duty of an officer who is seeking to purchase from a stockholder the latter's holdings of stock, to disclose to the latter facts which have come to him by virtue of his relations to the company, and not known to the stockholder, or which may not be readily ascertained by the stockholder, and to disclose such plans and purposes as the corporation may have for the future which have a bearing upon the value of the stock of the company,"—citing *Stewart v. Harris*, and *Oliver v. Oliver*, supra. The court, however, by a majority, ruled that the plaintiff, Nielsen, being a director and superintendent, was in a position to know as much of the facts as Steinfeld, and for that reason could not recover. KENT, C.J., dissented on this latter point.

In *Pellio v Bull's Head Coal Co.*⁴² (1909), plaintiff sold his shares August 17, 1906, at \$1,000, at the solicitation of W., who was then secretary and treasurer of the mining company. Before selling, plaintiff consulted W., as to the condition of the mine and the value of the stock and was told the mine was about worked out and that \$300 would be a good price for his 5 shares. This was false and misleading; the company then had over \$13,000 surplus, and in November, 1906, shares sold for \$180. Within two years prior to the sale the president and secretary had drawn out \$49,000 in unauthorized salaries. Plaintiff did not at the time of the sale know whether W. bought for himself or for the company; the check given in payment was signed by W. as treasurer, and the purchase was in fact made for the company. After learning of the facts plaintiff tendered \$1,000 and interest to the company and demanded a re-transfer of the shares, and upon refusal sued both W. and the company. The trial court held plaintiff was entitled to a return of his stock, and refused a decree against W. The company appealed,

⁴² *Pellio v. Bull's Head Coal Co.*, — Pa. —, 73 Atl. 451.

and plaintiff filed a cross appeal claiming the court in the present case had the power to compel an accounting and repayment into the treasury of the sums fraudulently taken by W. This was refused, the court saying that after the plaintiff again became a shareholder he might perhaps sue in case the company refused, after demand upon it to do so. This was affirmed *per curiam* by the supreme court.

To sum up these cases upon what they say as to the existence of a trust relation between the director and the individual shareholder, without special reference to the particular facts or to the necessity of relying on such a doctrine, the following eleven cases say there is no fiduciary or trust relation of that kind: *Smith v. Hurd*,⁴³ *Carpenter v. Danforth*,⁴⁴ *Board etc. Tippecanoe County v. Reynolds*,⁴⁵ *Deaderick v. Wilson*,⁴⁶ *Gillette v. Bowen*,⁴⁷ *Crowell v. Jackson*,⁴⁸ *Krumbhaar v. Griffiths*,⁴⁹ *Percival v. Wright*,⁵⁰ *Walsh v. Goulden*,⁵¹ *O'Neile v. Ternes*,⁵² *Hooker v. Midland Steel Co.*⁵³ Such an expression occurs in some other cases, but apparently only incidentally, and without any bearing upon the facts involved. The following five cases say there is a trust or fiduciary relation so existing: *Walsham v. Stainton*,⁵⁴ *Oliver v. Oliver*,⁵⁵ *Stewart v. Harris*,⁵⁶ *Von Au v. Magenheimer*,⁵⁷ *Steinfeld v. Nielson*,⁵⁸ while *Perry v. Pearson*,⁵⁹ held that "if it be admitted" it was not violated, *Baird v. Granis*,⁶⁰ refused to pass on it, and *Strong v. Repide*⁶¹ admitted that special facts may create such a trust relation.

With reference to the facts involved in the cases reviewed above they may be grouped as follows: Those in which

(1) Misrepresentation of a material fact was made by the purchasing officer directly to the selling shareholder, as in *Fisher*

⁴³ 12 Met. (Mass.) 371 (1847).

⁴⁴ 52 Barb. (N. Y.) 581, (1868).

⁴⁵ 44 Ind. 509 (1873).

⁴⁶ 67 Tenn. (8 Bax.) 108, (1874.)

⁴⁷ 23 Fed. R. 625 (1885).

⁴⁸ 53 N. J. L. (24 Vroom.) 656 (1891).

⁴⁹ 151 Pa. St. 223 (1892).

⁵⁰ L. R. [1902] 2 Ch. 421.

⁵¹ 130 Mich. 531 (1902).

⁵² 32 Wash. 528 (1903).

⁵³ 215 Ill. 444 (1905).

⁵⁴ 1 De Gex, J. & S. 678, 66 Eng. Ch. 527, (1863).

⁵⁵ 118 Ga. 362 (1903).

⁵⁶ 69 Kans. 498 (1904).

⁵⁷ 126 App. Div. (N. Y.) 257 (1908).

⁵⁸ 100 Pac. 1094 (Ariz. 1909).

⁵⁹ 135 Ill. 218 (1890).

⁶⁰ 208 Mo. 426 (1907).

⁶¹ 213 U. S. 419 (1909).

v. *Budlong*,⁶² *Hume v. Steele*,⁶³ *Morrison v. Snow*,⁶⁴ and *Pellio v. Bulls Head Coal Co.*⁶⁵ These do not depend upon, and yet are not inconsistent with, any trust or confidential relation existing between corporate officers and individual shareholders.

(2) False reports either by false statements of facts, or partial and incomplete statements intentionally made to the corporation or to the public, upon which the injured party has relied, as *Walsham v. Stainton*,⁶⁶ *Oliver v. Oliver*,⁶⁷ and *Stewart v. Harris*.⁶⁸ Likewise these cases are neither dependent upon nor inconsistent with fiduciary relations between officer and shareholder. The same principle extends however to those who sell shares to other parties as in *Rothmiller v. Stein*,⁶⁹ or purchase shares, as in *Prewitt v. Trimble*⁷⁰ and *Gerner v. Mosher*⁷¹ (not reviewed above) in reliance on false statements made by the officers to such seller or purchaser, even though the officer may not know at the time that his statement is false.

(3) False statements of fact designed to induce action were made, but which were not relied on, *O'Neile v. Ternes*;⁷² or the party relied upon his own independent investigation, *Percival v. Wright*,⁷³ *Hooker v. Midland Steel Co.*;⁷⁴ or had equal knowledge, *Brown v. DeYoung*,⁷⁵ *Rafferty v. Donnelly*;⁷⁶ or there was equal opportunity to know, *Steinfeld v. Neilson*;⁷⁷ or the representations made did not relate to an existing fact, but only to a future contingency, *Grant v. Attrill*,⁷⁸ *Boulden v. Stilwell*.⁷⁹ These cases in holding there is no liability, apply the ordinary rules relating to fraud. *Von Au v. Magenheimer*,⁸⁰ however, goes further and holds that misrepresentation of a future contingency by the corporate officer, to the shareholder inducing him to sell his shares to the

⁶² 10 R. I. 525 (1873).

⁶³ 59 S. W. 812 (Tex. Civ. App. — 1900).

⁶⁴ 26 Utah 247 (1903).

⁶⁵ 73 Atl. 451 (Pa. — 1909).

⁶⁶ 1 De Gex, J. & S. 678, 66 Eng. Ch. 527 (1863).

⁶⁷ 118 Ga. 362 (1903).

⁶⁸ 69 Kans. 498 (1904).

⁶⁹ 143 N. Y. 581 (1894).

⁷⁰ 92 Ky. 176 (1891).

⁷¹ 58 Neb. 135, 46 L. R. A. 244 (1899).

⁷² 32 Wash. 528 (1903).

⁷³ L. R. [1902] 2 Ch. 421.

⁷⁴ 215 Ill. 444 (1905).

⁷⁵ 167 Ill. 549 (1897).

⁷⁶ 197 Pa. St. 423 (1900).

⁷⁷ 100 Pac. 1094 (Ariz. 1909).

⁷⁸ 11 Fed. R. 469 (1882).

⁷⁹ 100 Md. 543 (1905).

⁸⁰ 126 App. Div. 257, (N. Y. 1908).

officer, is actionable because of the trust relation. There were other material defaults in this case.

(4) Full disclosure of all the material facts then known to the corporate officer affecting or likely to affect the value of the shares at the time of the purchase was made, as in *Carpenter v. Danforth*,⁸¹ *Krumbhaar v. Griffiths*⁸² and *Baird v. Grannis*.⁸³ Here there is no liability, whether a trust relation exists or not:

(5) The purchasing officer has been made the *special agent* of the shareholder to sell the shares, as in *Fisher v. Budlong*,⁸⁴ *Mulvane v. O'Brien*,⁸⁵ *Walsh v. Goulden*,⁸⁶ *Oliver v. Oliver*,⁸⁷ and *Wann v. Scullin*.⁸⁸ Here of course the special agency creates a fiduciary relation; but it was held not to be violated in the last two cases.

(6) There was fraudulent misappropriation of corporate funds by corporate officers, with concealment of this fact, in order to depress the value of the shares for the purpose of purchasing them at less than their value, as in *Walsham v. Stainton*,⁸⁹ *Ritchie v. McMullen*,⁹⁰ *Brown v. DeYoung*,⁹¹ *Rafferty v. Donnelly*,⁹² *Von Au v. Magepheimer*,⁹³ and *Pellio v. Bull's Head Coal Co.*⁹⁴ In the *Walsham*, *Ritchie*, and *Brown* cases, although the primary injury had been done to the corporation, it was held the shareholder had an action for the direct injury done him, although in the first case there had been a partial recovery by the corporation. In the *Rafferty* and *Pellio* cases this point is not made very clear, but seems to indicate there is a liability directly to the selling shareholder, and the *Von Au* case so holds, basing it upon the fiduciary relation of the purchasing officer to the selling shareholder. This view is inconsistent with *Wells v. Dane*,⁹⁵ and *Ninneman v. Fox*⁹⁶ (not reviewed above),—holding that the right of action if any, when the injury is to the corporation, and is such as to impair the value of the shares, passes to

⁸¹ 52 Barb. (N. Y.) 581 (1868).

⁸² 151 Pa. St. 223 (1892).

⁸³ 208 Mo. 426 (1907).

⁸⁴ 10 R. I. 525 (1873).

⁸⁵ 58 Kans. 463 (1897).

⁸⁶ 130 Mich. 531 (1902).

⁸⁷ 117 Ga. 362 (1903).

⁸⁸ 109 S. W. 688 (Mo. 1908).

⁸⁹ 1 De Gex, J. & S, 678, 66 Eng. Ch. 527 (1863).

⁹⁰ 79 Fed. 522 (1897).

⁹¹ 167 Ill. 549 (1897).

⁹² 197 Pa. St. 423 (1900).

⁹³ 126 App. Div. 257 (1908).

⁹⁴ 73 Atl. 451 (Pa. 1909).

⁹⁵ *Wells v. Dane* (1905), — Me. —, 63 Atl. 324.

⁹⁶ *Ninneman v. Fox* (1906), 43 Wash. 43, 86 Pac. 213.

the transferee,—unless a different rule is to be applied when the purchaser is the wrongdoing officer.

(7) There was concealment,—(a) *active*, by misleading reports or statements, as in the *Walsham, Oliver*, and *Stewart* cases above, holding there is a liability. (b) *passive*, silence merely: 1. As to existing conditions or future prospects of the company, as in *Tipppecanoe County v. Reynolds*,⁹⁷ *Deaderick v. Wilson*,⁹⁸ *Crowell v. Jackson*,⁹⁹ *Haarstick v. Fox*,¹⁰⁰ all holding there was no liability for such non disclosure. 2. As to a completed or pending profitable sale of all the property, as in *Tipppecanoe County v. Reynolds*,¹⁰¹ *Crowell v. Jackson*,¹⁰² *Krumbhaar v. Griffiths*,¹⁰³ *Percival v. Wright*,¹⁰⁴ *Hooker v. Midland Steel Co.*,¹⁰⁵ all holding there is no fiduciary relation requiring disclosure. In *Mulvane v. O'Brien*,¹⁰⁶ and *Oliver v. Oliver*,¹⁰⁷ where the sale of the property was completed at a better price than had been proposed, and this fact was concealed, there was a liability to account to the shareholder for the extra price received so far as wrongfully appropriated by the officer, but not, so far as appropriated to the payment of existing corporate debts, as in *Walsh v. Goulden*,¹⁰⁸ 3. As to the existence of conflicting interests, *Wann v. Scullen*,¹⁰⁹ or an independent collateral agreement, *Walsh v. Goulden*,¹¹⁰ neither of which operated to the injury of the selling shareholder,—in such cases there was no liability for not disclosing such interest. 4. As to the identity of the purchasing officer,—*Strong v. Repide*¹¹¹ is the only case that seems to consider this of much importance, although it is referred to in *Carpenter v. Danforth*,¹¹² *Fisher v. Budlong*,¹¹³ *Krumbhaar v. Griffiths*,¹¹⁴ *Rafferty v. Donnelly*,¹¹⁵ and *Baird v. Grannis*.¹¹⁶

⁹⁷ 44 Ind. 509 (1873).

⁹⁸ 67 Tenn. 8 (Bax.) 108 (1874).

⁹⁹ 53 N. J. L. (24 Vroom.) 656 (1891).

¹⁰⁰ 9 Utah 110 (1893).

¹⁰¹ 44 Ind. 509 (1873).

¹⁰² 53 N. J. L. 656 (1891).

¹⁰³ 151 Pa. St. 223 (1892).

¹⁰⁴ L. R. [1902] 2 Ch. 421.

¹⁰⁵ 215 Ill. 444 (1905).

¹⁰⁶ 58 Kans. 463 (1897).

¹⁰⁷ 118 Ga. 362 (1903).

¹⁰⁸ 130 Mich. 531 (1902).

¹⁰⁹ 109 S. W. 688 (1908).

¹¹⁰ 130 Mich. 531 (1902).

¹¹¹ 213 U. S. 419 (1909).

¹¹² 52 Barb. 581 (1868).

¹¹³ 10 R. I. 525 (1873).

¹¹⁴ 151 Pa. St. 223 (1892).

¹¹⁵ 197 Pa. St. 423 (1900).

¹¹⁶ 208 Mo. 426 (1907).

From this review, there is a liability for actual fraud; for the abuse of the confidence of a special agency; for fraudulent acts affecting the value of the shares, concealing this for the purpose of purchasing at the depressed value, or for *active* or *intentional concealment* as some of the cases say,¹¹⁷ but not for mere silence or passive concealment, and there is no presumption of fraud, or duty to disclose, arising out of the relation alone of director and shareholder.

In *Strong v. Repide* the court held there was such a combination of facts as raised a duty to speak,—the dominating power of the defendant in making the sale of all the property, and his concealment of his identity as a purchaser and of the progress of the negotiations relating to the sale of the land. His dominating power was exercised for the benefit of the company, and not to depress the value of the shares as in the *Walsham* and other cases in No. 6 of the summary above. It seems to be then in the last analysis only a case of concealment of material facts,—his own identity as a purchaser and the real value of the property; as to the latter it seems the defendant was only passively silent, but as to the first he *took steps* to conceal, and this perhaps is sufficient to bring it within the rules laid down in other cases.

The rule in *Smith v. Hurd*,¹¹⁸ on which the foregoing doctrine of the non-existence of a trust relation between the corporate officer and individual shareholders, has grown up, had to be modified or limited almost immediately afterward, by recognizing that the shareholder was the real party in interest, and in order to prevent a failure of justice, must be allowed to sue in equity where the corporation refuses to protect his interest after demand to do so is made.¹¹⁹ Mr. Pomeroy¹²⁰ found it necessary to call the directors *quasi trustees* for individual shareholders, and admirably classified the cases into four classes: (1) Where parties are induced to purchase shares by fraudulent statements or concealments in a prospectus or report, the individual shareholder has an action; (2) Ultra vires transactions,—individual shareholders can sue for their own damage; (3) Wrongful dealing with the corporate property,—the corporation has the primary right to sue,—but (4),

¹¹⁷ *Carpenter v. Danforth*, *Crowley v. Jackson*, *Haarstick v. Fox*, *Von Au v. Magenheim*, *supra*.

¹¹⁸ 12 Met. (Mass.) 371 (1847).

¹¹⁹ *Dodge v. Woolsey*, 18 How. 331 (1855), *Howes v. Oakland*, 104 U. S. 450 (1881).

¹²⁰ *Equity* §§ 1088-1096.

if it cannot or will not upon proper demand, the shareholder may sue in a representative capacity for the benefit of all.

It is usual to argue that to extend the rule further than to make a liability for active concealment, and to make a duty of disclosure by the officer to the shareholder before purchasing his shares, would deprive a director of the valuable right to purchase shares in open market that other shareholders have, lessen the market for shares, require constant information to be given whenever the shareholder wishes to buy as well as sell, and of losses as well as gains, and place various other imaginary hardships upon the director.

Such considerations do not appeal to the writer as formidable. That the director may take advantage of his position to secure the profits that all have won, offends the moral sense; no shareholder expects to be so treated by the director he selects; no director would urge his friends to select him for that reason; that the law yet allows him to do this, does more to discourage legitimate investment in corporate shares than almost anything else, and allows the fiction of the corporate entity to obstruct instead of advance justice. Would it not be well to go back to the original theory of *Walsham v. Stainton*, followed by several later cases and ably contended for by Judge JOHNSON in the Philippine Supreme Court? The writer believes it would.

H. L. WILGUS.

UNIVERSITY OF MICHIGAN.