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CORPORATIONS --VOTING TRUSTS -- NON-COMPLIANCE WITH STATUTE AS A BASIS FOR JUDICIAL TERMINATION

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CORPORATIONS — VOTING TRUSTS — NON-COMPLIANCE WITH STATUTE AS A BASIS FOR JUDICIAL TERMINATION—It is not the purpose of this comment to discuss the history of the voting trust, to re-

capitulate the controversy over its legality,[1] or to examine the many grounds for termination of the trust.[2] It is sufficient to say that in all but perhaps three states this important business device has been made legal by statute or by judicial decision.[3] We are here concerned with finding the degree of statutory compliance necessary in order that the voting trust will be sustained.

In a leading case, *Matter of Morse*, the court laid down this widely quoted principle of law: "Whether they (voting trusts) would be valid at common law in the absence of a statute defining and regulating them is immaterial....No voting trust not within the terms of the statute is legal and any such trust, so long as its purpose is legitimate, coming within its terms is legal. The test of validity is the rule of the statute. When the field was occupied by the Legislature it was fully occupied and no place was left for other voting trusts."[4]

Strangely enough, however, there are but few cases wherein this principle was cited in an attack upon the validity of a particular voting trust. In a recent Michigan case,[5] a voting trust, irrevocable for ten years, was formed in October of 1939. The voting trustees voted the stock assigned them in a stockholders' meeting held in December of that year for the election of directors. These directors then elected officers of the corporation, and not until 1940 was a certificate for the stock in the trust issued in the trustees' names. After the voting trust had been in existence for several years, a minority in interest of the participants of the trust brought suit for termination on the ground, among others not important to this comment, that the trust was invalid under the Michigan statute.[6] The statutory provision violated was the one re-

[1] See 5 FLETCHER, CYCLOPEDIA CORPORATIONS, perm. ed., § 2078 (1931); Burke, "Voting Trusts Currently Observed," 24 MINN. L. REV. 347 (1940); Wormser, "The Legality of Corporate Voting Trusts and Pooling Agreements," 18 COL. L. REV. 123 (1918).

[2] If formed for a fraudulent purpose, Venner v. Chicago City Ry. Co., 258 Ill. 523, 101 N.E. 949 (1913). To perpetuate control, Lebus v. Stansifer, 154 Ky. 444, 157 S.W. 727 (1913). Restraint upon alienation, Moses v. Scott, 84 Ala. 608, 4 S. 742 (1887).

[3] Dougherty and Berry, "The Voting Trust—Its Present Status," 28 GEO. L. J. 1121 (1940).

[4] 247 N.Y. 290 at 298, 160 N.E. 374 (1928).

[5] Herman v. Dereszewski, 312 Mich. 244, 20 N.W. (2d) 176 (1945).

[6] Michigan General Corporation Act, § 34, Mich. Consol. L. (Mason, Supp. 1940) § 10135-34. The pertinent terms are: "After filing an unexecuted copy of such agreement in the registered office of the corporation in this state, which copy shall be open to the inspection of any shareholder of the corporation or any depositor under said agreement daily during business hours, the certificates for shares so transferred shall be surrendered and cancelled, and new certificates therefor shall be issued to such transferee or transferees, who may be designated voting trustees, and in the entry of such transferee or transferees as owners of such shares in the proper books of the issuing corporation that fact shall be noted, and thereupon said transferee or transferees may

quiring that the certificates of stock be issued to the trustees before they are allowed to vote the shares of stock covered by the voting trust agreement. The court held that "there was substantial compliance with the statute in the execution of the agreement and the issuance of stock to the voting trustees,"[7] and therefore the agreement was valid.

We can derive no assistance from the writers in our search for the solution to our problem, for their statements that strict statutory compliance is necessary are based upon the *Morse* case,[8] and that case does nothing to dispel the confusion. The distinction between mandatory and directory provisions in a voting trust statute was not involved in the case; it was concerned with the basis for voting trusts, for the statutory authorization of voting trusts had been withdrawn from banking corporations by amendment to the statute. We find the statement that "statutes authorizing the creation of a voting trust agreement have been held to be mandatory, so that unless the agreement is executed in conformity with the regulations prescribed, the trust is void, irrespective of what the common law rule might have been in the particular jurisdiction."[9] Of the three cases cited as authority for this statement only two have any bearing upon our problem. One of the two also leaves the cloud upon our picture, for therein it is said that a trust not complying with the statutory provisions is invalid; but there is no disclosure of what provision was not complied with, the issue was not pressed, and there were other grounds for holding the trust invalid.[10] The remaining one cites the *Morse* case in holding that a voting trust which violates the statutory limitation on duration is completely void.[11] Thus we may be satisfied that such a provision is mandatory, but we see that a difference of opinion exists as to the results of a violation of such a limitation. In the same state which gave birth to the *Morse* case it was held that the trust was not invalidated by such a violation, but rather only the portion beyond the statutory duration was invalidated.[12] In

vote upon the shares so transferred during the period in such agreement specified and thereafter until those entitled to receive certificates of stock under such agreement shall have received the same."

[7] 312 Mich. 244 at 248, 20 N.W. (2d) 176 (1945).

[8] 5 FLETCHER, CYCLOPEDIA CORPORATIONS, perm. ed., § 2080 at p. 285 (1931); 33 MICH. L. REV. 804 (1935); Burke, "Voting Trusts Currently Observed," 24 MINN. L. REV. 347 at 361 (1940); 105 A.L.R. 123 at 146 (1936).

[9] 18 C.J.S. 1261.

[10] Davidson v. American Paper Manufacturing Co., 188 La. 69, 175 S. 753 (1937). The discarded member of the trio actually displayed a liberal attitude toward voting trusts in holding that a trustee may delegate his votes to another trustee where the terms of the agreement permit it, Chandler v. Bellanca Aircraft Corp., 19 Dela. Ch. 57, 162 A. 63 (1932).

[11] Perry v. Missouri-Kansas Pipe Line Co., 22 Dela. Ch. 33, 191 A. 823 (1937).

[12] Kittinger v. Churchill Evangelistic Assn., 151 Misc. 350, 271 N.Y.S. 510 (1934).

holding that the entire trust fails, the Delaware court said that the "provisions of our statute governing voting trusts are mandatory";[13] but in a recent case, the Delaware court upheld an injunction to force a trustee to exchange stock, "although for a considerable part of the term of the trust neither of the voting trustees attempted to obtain a record transfer of the stock assigned to them. . . ."[14] In a later hearing of the same case, the court sustained the demand of the holders of a minority in interest of the trust that the other holders transfer their stock to the defendant corporation, and that the corporation reissue to the stockholders new certificates in the name of the voting trustees, "although for more than two years after the execution of the agreement no attempt was made to comply with the statutory provisions concerning the filing of a copy of the agreement and the issuance of stock certificates in the names of the voting trustees. . . ."[15]

In the Michigan case the issue as to whether substantial compliance with the statute is sufficient was squarely before the court, and the trust was upheld. This decision gains significance when we realize that it was rendered in a jurisdiction which, prior to the enactment of the statute, apparently could find no common law basis for upholding voting trusts.[16] Although the report of the Delaware case does not disclose that the court dealt specifically with the question, there, too, the trustees had elected the directors of the corporation before the statutory requirements were fulfilled, and it was made apparent that strict compliance with statutory provisions is not necessary. Again we find that this result was reached in a jurisdiction which found it necessary to rely upon a statute in order to sustain voting trusts, rather than attempt to find any basis for them at common law.[17] In those states which upheld voting trusts before legislation was passed supporting them, the principle anounced in *Matter of Morse* should cause little difficulty.

At the present time, the broad statement that provisions in a voting trust statute are mandatory appears to be disapproved by the courts. We may agree that limitations on duration, rights of trustees, control and voting rights are mandatory. But the Michigan case demonstrates the relaxation by modern courts of the strict compliance principle voiced in *Matter of Morse*, and indicates a realization that the voting trust is a valuable business device which should not be condemned without a hearing.[18] A recent decision of the New York court indicates a change

[13] Perry v. Missouri-Kansas Pipe Line Co., 22 Dela. Ch. 33, 191 A. 823 (1937).

[14] Hirschwald v. Erlebacher, (Dela. Ch. 1943) 29 A. (2d) 798 at 801.

[15] Id., 33 A. (2d) 148 at 154 (1943), affirmed per curiam, (Dela. 1944) 36 A. (2d) 167.

[16] Billings v. Marshall Furnace Co., 210 Mich. 1, 177 N.W. 222 (1920).

[17] Chandler v. Bellanca Aircraft Corp., 19 Dela. Ch. 57, 162 A. 63 (1932).

[18] Gose, "Legal Characteristics and Consequences of Voting Trusts," 20 WASH. L. REV. 129 (1945).

in attitude toward statutory voting trusts; in *Wolf v. Roosevelt*[19] the court held that a statute limiting the duration of voting trusts to five years does not limit a ten year trust formed prior to the statute. In voicing their dissent, the minority of the court heavily relied upon *Matter of Morse*. While it is true that the voting trust may lend itself to dishonest purposes,[20] the same can be said concerning other devices invented to supplement the corporate structure. An intelligent supervision by the courts, and a realistic approach by the legislature will do much toward eliminating the vices of the voting trust, and yet save its desirable features. The recognition of the voting trust is now almost universal, and should carry as a necessary corollary the abandonment of the strict construction theory.

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[19] 290 N.Y. 400, 49 N.E. (2d) 502 (1943). See also Mannheimer v. Keehn, 41 N.Y.S. (2d) 542 (1943), wherein the voting trust law of New York was examined, and it was said that voting trusts in New York are prima facie valid, and not presumed void until the contrary appears.

[20] Ballantine, "Voting Trusts, Their Abuses and Regulation," 21 TEXAS L. REV. 139 (1942).