

1910

Corporation Liens on Stock

Edson R. Sunderland

University of Michigan Law School

Follow this and additional works at: <http://repository.law.umich.edu/articles>

 Part of the [Business Organizations Law Commons](#), [Securities Law Commons](#), and the [State and Local Government Law Commons](#)

Recommended Citation

Sunderland, Edson R. "Corporation Liens on Stock." Mich. L. Rev. 8 (1910): 555-71.

This Article is brought to you for free and open access by the Faculty Scholarship at University of Michigan Law School Scholarship Repository. It has been accepted for inclusion in Articles by an authorized administrator of University of Michigan Law School Scholarship Repository. For more information, please contact mlaw.repository@umich.edu.

CORPORATION LIENS ON STOCK.

THE law of corporations is essentially a modern creation, made necessary by modern business conditions. But the courts, not legislative bodies, have been largely instrumental in giving it its comprehensive scope and symmetrical form. Perhaps nowhere has the inherent power of the common law to develop new principles to meet changed conditions been more strikingly shown than in this field.

The primary problems connected with the development of the corporation relate to its organization and powers and the means employed to enable it to perform its proper function as the chief commercial and industrial agency of the times. The rights, duties, powers and liabilities of the corporation, of its stockholders, and of its officers and directors, and their legal relations respecting one another and the parties with whom they deal in their corporate and official capacity, are all essential features of corporation law, and an understanding of these subjects is necessary to an intelligent appreciation of the nature of the corporation.

But every corporation organized with capital stock is not only a corporation but a producer of instruments of credit. A certificate of stock is evidence of the stockholder's interest in the company, but it is also an instrument which may be used in commercial transactions and in banking relations as a foundation for credit in innumerable ways. A corporation, like a bank, is in fact a creator of credit through its issuance of securities. The money which the stockholders invest in the property of the company comes back to them in the form of these stock certificate credits. Indeed, the corporation often issues more credit than it incorporates in its physical properties, for earning power is frequently capitalized, and it may thus become the basis for the issuance of additional credit instruments. The common stock of the United States Steel Corporation is largely of this sort, and the same is true of the common stocks of many other large corporations.

Thus, wholly apart from its character as an artificial person or an industrial agency, the corporation has become immensely important in modern commercial life as a fiscal agency, or creator and issuer of securities. Corporation stocks and bonds probably constitute the principal commercial securities of the age. Of these it is safe to say that stock issues much outweigh corporate bond issues

in amount, and transactions in stocks are said to far exceed those in bills and notes.¹

It is therefore of the highest importance to the commercial and financial world that dealings in corporate stocks should be made as safe as possible, and that barriers and restrictions to their free transfer should be as few and as slight as is consistent with their character. As universally used instruments of credit they should as nearly as possible approximate the transferable quality of that other great group of credit instruments, bills and notes.

It must be conceded that the courts have so far been unwilling to declare corporate stock certificates fully negotiable, though they have accorded them most of the qualities of such instruments. The Supreme Court of the United States, in *Bank v. Lanier*,² said that while neither in form nor character negotiable paper, "they approximated it as nearly as practicable." In *Jarvis v. Manhattan Beach Co.*,³ the Court of Appeals of New York said: "While such certificates do not possess all the qualities of commercial paper, they do possess some or them, and innocent parties, dealing with them, will be protected upon analogous principles." The extent of this protection is predicated upon an estoppel against the true owner to claim adversely to one who purchases in good faith from a party lawfully clothed with the *indicia* of title.⁴ This is a substantial protection, and makes stock certificates practically negotiable as against claims of prior holders, except in case of loss or theft.⁵

But there is another sort of claim beside that of the true owner, which is often asserted against stock certificates, namely a claim of lien on behalf of the corporation itself, for the unpaid portion of the subscription price of the stock or for debts due to the corporation from the past or present holder. The recognized validity and common occurrence of such liens would make a striking distinction between stock certificates and negotiable instruments, and would in fact materially diminish the commercial utility of such certificates as instruments of credit. It is the purpose of this article to investigate the methods by which such liens can be created and their validity as against the various parties who may be interested in the stock represented by the certificates.

¹ 1 Dos Passos, *Stock & Stock Brokers*, p. 702.

² 11 Wall. (U. S.) 377.

³ 148 N. Y. 659.

⁴ *McNeil v. Tenth Nat. Bank*, 46 N. Y. 325.

⁵ *East Birmingham Land Co. v. Dennis*, 85 Ala. 565; *Knox v. Eden Musee American Co.*, 148 N. Y. 441.

At common law a corporation had no lien upon its stock for assessments unpaid or for debts due it from its shareholders.⁶ There are therefore but four possible methods by which liens could be created in favor of the corporation upon the stock which it issues, (1) by statute, (2) by charter, (3) by by-law, (4) by contract.

LIENS CREATED BY STATUTE.

There is a great variety in the statutes of the different states of this country respecting their provision for liens in behalf of corporations upon their stock. A summary of them all would unduly extend the limits of this article. But the following details of the general corporation acts, omitting all reference to specific acts relating to particular classes of corporations, such as banks, railroads, mining companies, etc., will illustrate their variety and disclose their scope.

One class of statutes gives a lien to the corporation, upon stock issued by it, for all debts due to it by a stockholder. In this group belong Alabama,⁷ Arkansas,⁸ Connecticut⁹ and Minnesota.¹⁰

In New York the corporation has such a lien for all debts, in the discretion of the directors, provided, the section of the statute creating it is written or printed on the face of the certificate.¹¹

Another group of statutes authorizes a forfeiture or sale of stock, or prohibits transfer, or otherwise provides for a lien, in case of unpaid and delinquent assessments. Such statutes are found in Arizona,¹² Delaware,¹³ District of Columbia,¹⁴ Florida,¹⁵ Idaho,¹⁶ Kentucky,¹⁷ Maryland,¹⁸ Massachusetts,¹⁹ Missouri,²⁰

⁶ *Bank of Attica v. Manufacturers' & Traders' Bank*, 20 N. Y. 501, 507; *Steamship Dock Co. v. Heron's Adm'x*, 52 Pa. St. 280; *Merchants' Bank v. Shouse*, 102 Pa. St. 488, 492; *Driscoll v. West Bradley & Cary Mfg. Co.*, 59 N. Y. 96, 102; *Neale v. Janney*, 2 Cranch C. C. 188, 17 Fed. Cas. No. 10068.

⁷ Code, 1886, § 1674.

⁸ Kirby's Digest, 1904, § 853.

⁹ Conn. Gen. St., Revision of 1902, § 3332.

¹⁰ Rev. St., 1905, § 2863.

¹¹ Consolidated Laws, 1909, Ch. 59, § 51.

¹² Act No. 38, Laws 1907.

¹³ Rev. Code, as amended 1893, p. 577.

¹⁴ Code, § 613.

¹⁵ Rev. St., 1892, § 2131.

¹⁶ Civil Code, § 2769, Amended by Session Laws 1909, p. 163.

¹⁷ Ky. St., 1903, § 543.

¹⁸ Pub. Gen. Laws, 1904, Art. 23, Sec. 71.

¹⁹ R. L., 1902, Chap. 110, § 41.

²⁰ Ann. St., 1906, § 965.

Montana,²¹ Nevada,²² New Hampshire,²³ New Mexico,²⁴ North Carolina,²⁵ North Dakota,²⁶ Ohio,²⁷ New Jersey,²⁸ New York,²⁹ Pennsylvania,³⁰ South Dakota,³¹ Texas,³² Utah,³³ Vermont,³⁴ Virginia,³⁵ Washington,³⁶ Wisconsin,³⁷ and Wyoming.³⁸

Another group authorizes by-laws to be made which shall provide for a lien through forfeiture and sale or restriction on transfer or otherwise, for unpaid installments or assessments, and in this group belong Colorado,³⁹ Indiana,⁴⁰ Maine,⁴¹ Maryland,⁴² Mississippi⁴³ and Oregon.⁴⁴

Another group authorizes the corporation, by means of its by-laws, to create a lien on stock for any debts due to the corporation from the stockholder. Georgia⁴⁵ and South Carolina⁴⁶ have such statutes.

In West Virginia⁴⁷ and Kansas⁴⁸ a lien for unpaid assessments may be had in the discretion of the board of directors. In Oklahoma⁴⁹ forfeiture for non-payment of assessments may be provided for by the terms of subscription. In Rhode Island⁵⁰ the original articles of incorporation may provide for a lien for unpaid assessments or other indebtedness, enforceable as the by-laws may pre-

²¹ Rev. Codes, 1907, § 3877.

²² C. L., 1900, § 875.

²³ P. S., Chap. 149, § 17.

²⁴ C. L., 1897, § 425.

²⁵ Revisal of 1905, § 1170.

²⁶ Rev. Codes, 1905, § 4245.

²⁷ Bates' St., 1908, § 3253.

²⁸ Gen. St., 1895, Title Corporations, § 28.

²⁹ Consolidated Laws, 1909, Ch. 59, § 50.

³⁰ Purdon's Digest, 1903, p. 802, Title Corporations, § 93.

³¹ Civil Code, 1903, § 460.

³² Sayles' Tex. Civ. St., § 668.

³³ Comp. Laws, 1907, § 333.

³⁴ Pub. St., 1906, § 4268.

³⁵ Code, 1904, § 1105 c (28).

³⁶ Pierce's Code, 1905, § 7064.

³⁷ St., 1898, § 1754.

³⁸ R. S., 1899, § 3038.

³⁹ Mills' Ann. St., 1891, § 480.

⁴⁰ Burns' St., 1908, § 4046.

⁴¹ R. S., 1903, Ch. 47, § 47.

⁴² Pub. Gen. Laws, 1904, Art. 23, § 63.

⁴³ Code, 1906, § 908.

⁴⁴ Bellinger & Cotton's Codes, § 5056.

⁴⁵ Code, 1895, § 2825.

⁴⁶ Code, 1902, § 1848.

⁴⁷ Code, 1906, § 2251.

⁴⁸ G. S., 1905, § 1366.

⁴⁹ St., 1903, § 956.

⁵⁰ G. L., 1896, Title XIX, § 91.

scribe. In Iowa⁵¹ the corporation has a lien on its shares for taxes paid thereon, the law requiring such taxes to be assessed against the stockholders but to be paid by the company.

In California, Illinois, Louisiana, Nebraska, Michigan and Tennessee there seems to be no provision for such liens in the general incorporation acts.

As to the validity of these statutory liens, there can be no question. Such liens are valid against anyone, whether he be a taker with or without actual notice, for the statute itself constitutes constructive notice to all who deal in the shares of corporations organized under its authority.

Thus, in *Birmingham Trust and Savings Co. v. East Lake Land Co.*,⁵² it is said that when a lien is given to a corporation by statute, "there is constructive notice to all persons dealing with the corporation, that they must, at their peril, without reference to what the certificate recites, inform themselves as to any debts to the corporation that may affect the shares they propose to buy. If there is a lien they are held to have known it, whether the certificate declares it or not." The same rule was stated by the Supreme Court of Michigan in *Citizens' Bank v. Kalamazoo County Bank*,⁵³ by the Supreme Court of Arkansas in *Oliphint v. Bank of Commerce*,⁵⁴ and in *Springfield Wagon Co. v. Bank of Batesville*,⁵⁵ by the Supreme Court of Wisconsin in *H. W. Wright Lumber Co. v. Hixon*,⁵⁶ by the Supreme Court of Connecticut in *Platt v. Birmingham Axle Co.*⁵⁷ and in *First National Bank v. Hartford Life Ins. Co.*,⁵⁸ by the Supreme Court of Kansas in *Battery v. Bank*,⁵⁹ and by the Supreme Court of the United States in *National Bank v. Watsonstown Bank*.⁶⁰

LIENS CREATED BY CHARTER.

Morawetz, in his work on Corporations, says: "If the lien is provided for by the company's charter or articles of incorporation, or by general law, all persons purchasing shares are bound thereby, and must, at their peril, inquire of the company's officers whether the holders of the shares are indebted to it or not."⁶¹ Clark &

⁵¹ Code, 1897, § 1325.

⁵² 101 Ala. 304, 309.

⁵³ 111 Mich. 313.

⁵⁴ 60 Ark. 198.

⁵⁵ 68 Ark. 235.

⁵⁶ 105 Wis. 153.

⁵⁷ 41 Conn. 255.

⁵⁸ 45 Conn. 22.

⁵⁹ 62 Kan. 384.

⁶⁰ 105 U. S. 217.

⁶¹ 1 Morawetz on Corporations, § 203.

Marshall say on this question: "A lien may also be given by a provision in the articles of association, if such provision is not contrary to the charter or general law."⁶² And Cook says: "Such a lien as this in favor of the corporation may be created by statute or by charter."⁶³

The cases cited in support of these statements do not sustain them in the broad form in which they are made, and they do not appear to correctly state the law without certain qualifications.

The charter of a corporation may be granted by special act of the legislature or it may be provided for and authorized under a general incorporation act. Formerly the first method was common; in more recent times incorporation under general statutes has become almost universal.

Where the charter is the special act of the legislature, a lien clearly authorized therein obviously stands upon essentially the same footing as a strict statutory lien. The same rules apply in determining its force and effect as apply to statutory liens, and accordingly all takers of stock affected by such a charter lien take with constructive notice thereof, and their titles are subject to the prior claim of the corporation, whenever facts exist making the lien provision applicable. *Farmers' Bank of Maryland v. Iglehart*,⁶⁴ *Cross v. Phoenix Bank*,⁶⁵ *Brent v. Bank of Washington*,⁶⁶ *Reese & Fisher v. Bank of Commerce*,⁶⁷ *Stebbins v. Phoenix Fire Ins. Co.*,⁶⁸ *Hodges v. Planters' Bank*,⁶⁹ *Bank of Utica v. Smalley*,⁷⁰ *Union Bank v. Laird*,⁷¹ *Bohmer & Osterloh v. City Bank*,⁷² *Mechanics' Bank v. Merchants' Bank*,⁷³ *German National Bank v. Kentucky Trust Co.*,⁷⁴ *Kenton Ins. Co. v. Bowman*.⁷⁵ In all these cases the charter expressly and unequivocally provided for a lien.

When the charter consists of a general act under which articles of incorporation are executed and filed, the validity of the lien, as against the world, depends upon the terms of the general act. That is to say, unless the legislature has authorized it, the incorporators

⁶² 3. Clark & Marshall on Corporations, § 575.

⁶³ 2. Cook on Corporations, § 522.

⁶⁴ 6 Gill (Md.) 50.

⁶⁵ 1 R. I. 39.

⁶⁶ 10 Pet. (U. S.) 596.

⁶⁷ 14 Md. 271.

⁶⁸ 3 Paige (N. Y.) 350.

⁶⁹ 7 Gill & J. (Md.) 306.

⁷⁰ 2 Cow. (N. Y.) 770.

⁷¹ 2 Wheat. (U. S.) 390.

⁷² 77 Va. 445.

⁷³ 45 Mo. 513.

⁷⁴ 19 Ky. L. Rep. 361.

⁷⁵ 84 Ky. 436.

cannot, by means of the articles of incorporation, create a lien which will be effectual against all parties. It is immaterial whether the legislature declares directly that a lien shall exist, or declares that the articles of incorporation may create it. In either case it is the act of the legislature which ordains the lien. So that, in seeking to determine whether, in a given case, a lien exists, the act of the legislature must be examined, and not merely the provisions of the articles of incorporation. The question of the validity of the lien under charters of this kind is therefore essentially the same question as that arising under special legislative charters.

Thus, in *New Orleans National Banking Ass'n v. Wiltz*,⁷⁶ where an insurance company asserted a lien upon certain shares of its own stock, the Circuit Court of the United States said: "The insurance company was formed under the general incorporation law of the state by public act passed. * * * It has no legislative charter. This charter could not create any privilege unknown to the law of the state, unless the power were expressly given in the general law." And in *Driscoll v. West Bradley & Cary Mfg. Co.*,⁷⁷ the Court of Appeals of New York said that in order to sustain the validity of a lien, the corporation "must point out the authority either in its articles of association, and show that they are authorized by law, or in some statute."

A very thorough discussion of this principle is found in a recent decision of the Appellate Division of New York. *Lyman v. State Bank of Randolph*.⁷⁸ In that case article nine of the articles of association of the bank provided that no shareholder who had failed to respond to any call for an installment of capital or any interest upon such installment, or who was indebted to the bank either as drawer or indorser, or as surety for any payments due the bank, should be permitted to transfer his shares without the consent of a majority of the board of directors. The general act under which the bank was established was silent upon the subject of a lien. One Adams was a stockholder and officer of the bank, and was indebted to the bank in a large sum. The plaintiff's wife became a purchaser, in good faith and for value, of thirty shares of Adams' stock, without any actual knowledge of the existence of this provision of the articles of association or of any existing lien or equity in favor of the bank, and plaintiff took this stock from her as collateral for a loan under the same conditions. The plaintiff presented his certificate representing this stock to the bank for transfer to his own

⁷⁶ 70 Fed. 330.

⁷⁷ 59 N. Y. 96.

⁷⁸ 81 N. Y. App. Div. 367.

name, but the bank refused to transfer it until Adams' indebtedness to it was paid, claiming a lien on the stock by virtue of its articles of association.

The claim of the bank was that "the stock, having become impressed with the indebtedness due from Adams to the bank, retained that characteristic even in the hands of an innocent transferee," and that Mrs. Lyman "was bound to know of the existence of article 9 and of its inhibitory provision." But the court said: "Precisely how such information can be said to have been brought to her notice does not fully appear. It certainly could not have been gained from the certificate itself, for it contained no reference to the bank's articles of association, nor was there anything upon its face to indicate that the right to sell or assign the same was subject to any restriction or limitation whatever. On the contrary, it apparently conferred upon the holder an unconditional power of disposition, and in this respect was quite different from the certificate in *Gibbs v. Long Island Bank*,⁷⁹ which bore upon its face the statement that it was 'subject to the conditions and stipulations contained in the articles of association above mentioned.' We conclude, therefore, that in view of the elements of negotiability which the stock possessed, the omission upon the part of the bank to express, in some manner, its contingent right to or interest therein was virtually an assurance to a purchaser that the owner had full power and an unrestricted right to dispose of the same, and if such be the case, it would seem to follow that, aside from any question of negotiability, the bank under the undisputed facts contained in the record before us, is now estopped from asserting its claim as against title of the plaintiff. This view is in harmony with well settled principles and is supported by abundant authority." Upon appeal to the New York Court of Appeals, the decision was affirmed.⁸⁰

It would thus appear that the familiar statements found in the text books, such as those above quoted, to the effect that a lien created by charter is valid against everyone, must be restricted by the qualification that in case the charter consists of a general statute together with articles of association executed in pursuance thereof, the authority for the lien must be found in that part of the charter which comes directly from the legislature. The legislature may authorize the articles of association to be so drawn that they shall in terms provide for a lien, as in the Rhode Island statute above cited, and in such a case the provisions for the lien would be found in the

⁷⁹ 83 Hun, 92; aff'd, 151 N. Y. 657.

⁸⁰ *Lyman v. Bank of Randolph*, 179 N. Y. 577.

non-legislative portion of the charter, but such provisions would seem to derive all their coercive force and effect from the legislative act pursuant to which the articles were drawn.

A single case has been found which holds that the articles of incorporation may, in the absence of any authorization from the legislature, create a valid lien for debts due to the corporation, against a *bona fide* purchaser for value and without notice. This is *Dempster Mfg. Co. v. Downs*.⁸¹ The court says: "Such a lien is not prohibited, and may be created by the articles of incorporation." In support of this statement the court cites four cases. The first is *Bradford Banking Co. v. Briggs & Co.*,⁸² where it was held that the articles of association might create a lien valid only against takers of stock *with actual notice* of the articles. The second is *Sabin v. Bank of Woodstock*,⁸³ where a special legislative charter expressly authorized the lien. The third is *Bohmer v. City Bank of Richmond*,⁸⁴ where a special legislative charter expressly authorized the lien. The fourth is *Leggett v. Bank of Sing Sing*,⁸⁵ where it was held that one who purchased stock *with knowledge* that the articles of association provided for a lien in favor of the corporation, took subject to such lien. It thus appears that none of the cases cited by the court sustain its decision. Seemingly the court attached too much weight to the general statements of the text-books, several of which it cites.

LIENS CREATED BY BY-LAW.

The leading case of *Child v. Hudson's Bay Co.*⁸⁶ held that a by-law purporting to create a lien upon stock of a corporation for debts due to it from the stockholders, is effectual for that purpose, though neither charter nor statute authorize such a lien. However, in this case the lien was asserted against the assignee in bankruptcy of a stockholder who himself owed a debt to the company, so that the case is authority only for the rule that a by-law lien, unauthorized by law, is nevertheless valid against one who is not a *bona fide* purchaser for value and without notice.

Does the law go farther than this, and permit a corporation to establish a by-law lien which shall be good against the world, unless such lien is authorized by statute? There would seem to be less reason for recognizing the binding force of a by-law lien than of a

⁸¹ 126 Iowa, 80.

⁸² 31 Ch. Div. 19.

⁸³ 21 Vt. 353.

⁸⁴ 77 Va. 445.

⁸⁵ 24 N. Y. 283.

⁸⁶ 2 Perc Wms. 207.

charter lien, where no direct authority for it can be traced to the act of the legislature, for the reason that articles of association are almost invariably filed with public officers and are open to public inspection.

It is clear that a by-law can have no force which seeks to create a lien in the face of a statutory prohibition. This has several times been held, both by the federal and by the state courts, in cases involving the powers of national banks. The National Bank Act of 1863 provided for a lien upon stock to secure debts due from the stockholders to the bank. The Act of 1864 was enacted as a substitute for the earlier act, and omitted this section respecting liens. The Act of 1864 also prohibited national banks from making loans or discounts on the security of their own shares. These features of the Act of 1864 have been held to disclose a policy on the part of Congress to restrain national banks from acquiring liens on their own stock, and in view of such policy, a by-law of a national bank providing for such a lien is ineffectual for that purpose. *Bullard v. Bank*,⁸⁷ *Bank v. Lanier*,⁸⁸ *Conklin v. Second National Bank*,⁸⁹ *Hagar v. Union National Bank*,⁹⁰ *Second National Bank v. National State Bank*,⁹¹ *Lee v. Citizens' National Bank*,⁹² *Evansville National Bank v. Metropolitan National Bank*,⁹³ *Rosenbach v. Salt Springs National Bank*,⁹⁴ and *Buffalo German Ins. Co. v. Third National Bank*.⁹⁵ And a state statute copied from the National Bank Act of 1864 has been held to carry with it the construction previously given to that act, so that no lien could be acquired by virtue of a by-law. *Nicollet National Bank v. City Bank*.⁹⁶

But a different question arises where the corporation seeks to create a by-law lien, if the legislature has declared no law or policy on the subject.

The leading case in this country on this question is *Driscoll v. West Bradley & Cary Mfg. Co.*,⁹⁷ decided by the Court of Appeals of New York. In this case the defendant corporation had made a by-law providing that it should have a lien on its stock to secure any indebtedness due to it from its stockholders. One Bradley was

⁸⁷ 18 Wall. (U. S.) 589.

⁸⁸ 11 Wall. (U. S.) 369.

⁸⁹ 45 N. Y. 655.

⁹⁰ 63 Me. 509.

⁹¹ 10 Bush (Ky.) 367.

⁹² 2 Cin. Sup. Ct., 298.

⁹³ 2 Biss. 527; 8 Fed. Cas. No. 4573.

⁹⁴ 53 Barb. (N. Y.) 495.

⁹⁵ 162 N. Y. 163.

⁹⁶ 38 Minn. 85.

⁹⁷ 59 N. Y. 96.

a stockholder and was indebted to the company. He assigned and transferred his stock to a third person, from whom the plaintiff purchased it in good faith and for value, and without any actual knowledge of the existence of the by-law. The court said that if the defendant had any power to set up this lien, it must be found only in some statutory authority to pass the by-law. "The by-law of the defendant is sufficient in terms, but it is not sufficient in law unless it is warranted by some statute. * * * Therefore, we may treat the by-law, for the purposes of this case, as creating a lien upon the stock in favor of the defendant, if it had legal authority to enact a by-law to that effect. It can find warrant from statute law nowhere unless in the Revised Statutes, or in the general statutes for the incorporation of manufacturing companies." The court then proceeds to examine those statutes, and finds no provision authorizing such a by-law. It therefore concludes, that "Bradley and his fellow directors or trustees, had no power to make any by-law, binding on others than themselves, as actual or intended stockholders, which was not authorized by the Revised Statutes or by the general manufacturing acts. It might be good as a contract between themselves, but not as a by-law to affect strangers, or those not consenting."

The same doctrine was well stated in *Carroll v. Savings Bank*,⁹⁸ where the court said: "At common law, and independently of positive provisions of the legislature granting or authorizing the exercise of the power, a corporation cannot prohibit the transfer of its shares on account of the indebtedness of the shareholder to the corporation. When the stock is personal property, restrictions upon its transfer must have their source in legislative action, and the corporation itself cannot create these impediments." This statement was subsequently quoted with approval by the Supreme Court of Missouri in *Bank of Atchison County v. Durfee*.⁹⁹ To the same effect are *Steamship Dock Co. v. Heron's Adm'r*,¹⁰⁰ *Kinman v. Sullivan County Club*,¹⁰¹ *Merchants' Bank of Easton v. Shouse*,¹⁰² *Bank of Attica v. Manufacturers' and Traders' Bank*,¹⁰³ *Anglo-Californian Bank v. Grangers' Bank*,¹⁰⁴ *Bank of Colloden v. Bank of Forsyth* (under a statute authorizing a lien to be created by by-law, but providing further that such lien should be valid against all takers

⁹⁸ 8 Mo. App. 249.

⁹⁹ 118 Mo. 444.

¹⁰⁰ 52 Pa. St., 280.

¹⁰¹ 26 N. Y. App. Div. 213.

¹⁰² 102 Pa. St. 488.

¹⁰³ 20 N. Y. 501.

¹⁰⁴ 63 Cal. 359.

with notice),¹⁰⁵ *Graffin Co. v. Woodside*,¹⁰⁶ *Bank of Holly Springs v. Pinson*.¹⁰⁷

The *in rem* case of *McDowell v. Bank of Brandywine*,¹⁰⁸ decided in a superior court in Delaware, in a very brief opinion, seems to imply that a by-law lien is valid without statutory authority, if the articles of association provide for it, and a very old case in Alabama, *Cunningham v. Alabama Life Ins. Co.*,¹⁰⁹ appears to go almost as far, though the court did not rest the case wholly upon that proposition, but made an examination of the statute and found general language which might have authorized the lien. Aside from these two cases, there seems to be no dissent from the rule stated above.

The same rule, that statutory authority for a by-law lien is necessary to give it validity against innocent purchasers of the stock, is recognized in another class of cases which will now be examined. In each of them it was assumed that the lien must derive its vital force from the statute, and the question in each case was whether the language of the statute did in fact authorize it.

In *Mechanics' Bank v. Merchants' Bank*,¹¹⁰ the statute gave the directors of the bank authority to make by-laws "for the management of its property, the regulation of its affairs and the transfer of its stock." This was held to authorize a by-law which the directors adopted, providing for a lien on the stock of the bank for any indebtedness due to it from the stockholders. In *Lockwood v. Mechanics' Bank*,¹¹¹ statutory language identical with that just quoted was likewise held sufficient to authorize such a lien. In *St. Louis Perpetual Ins. Co. v. Goodfellow*,¹¹² a provision in a special charter declared that the stock of the company should be deemed personal property, and should be assignable and transferable according to such rules and restrictions as the board of directors should make and establish, and this was held sufficient to authorize a by-law lien for debts due to the company. In *Pendergast v. Bank of Stockton*,¹¹³ a statute authorizing a corporation "to make by-laws for the management of its property, the regulation of its affairs and the transfer of its stock," and declaring that "the stock of the

¹⁰⁵ 120 Ga. 575.

¹⁰⁶ 87 Md. 146.

¹⁰⁷ 58 Miss. 421.

¹⁰⁸ 1 Harr. (Del.) 27.

¹⁰⁹ 4 Ala. 652.

¹¹⁰ 45 Mo. 513.

¹¹¹ 9 R. I. 308.

¹¹² 9 Mo. 149.

¹¹³ 2 Sawy. 108; 19 Fed. Cas. No. 10918.

company shall be transferable in such manner as shall be prescribed by the by-laws of the company," was held to authorize a by-law lien, though the holding was perhaps *obiter*, since the plaintiff took the stock with actual notice of the by-law.

But it is very doubtful if any of the foregoing cases are entitled to much weight. In view of the immense importance attaching to the free commercial transfer of stock certificates, clearer language than that relied upon in those cases ought to be employed, if purchasers are to be put upon inquiry in taking stock certificates in due course of business, and the overwhelming weight of authority so declares.

As for the cases cited above, the two Missouri cases have been practically overruled by *Bank of Atchison County v. Durfee*,¹¹⁴ where the court held that a statute providing that the stock of the company should be deemed personal estate and should be transferable in the manner prescribed by the by-laws, and that the company might make by-laws for the regulation of its affairs and for the transfer of its stock, did not authorize a by-law attempting to create a lien in the company's favor for debts due to it. The Rhode Island case was decided in 1869; it involved the construction of the National Bank Act of 1864, and held that a by-law lien was authorized by that act; but the Supreme Court of the United States, in the following year, passed upon the same question and came to a directly opposite conclusion, in *Bank v. Lanier*.¹¹⁵ The *Pendergast* case is likewise of little value by reason of the contrary holding by the United States Supreme Court.

The rule seems now to be clearly established that general language, of the kind above shown, is not sufficient to authorize a by-law lien. Thus, in *Bullard v. Bank*,¹¹⁶ it was held by the United States Supreme Court that a statutory provision authorizing a bank to make by-laws for the regulation of its business and the conduct of its affairs, and providing further that the stock should be transferable on the books of the corporation in such manner as might be prescribed in the by-laws or articles of association, did not authorize a by-law lien on the stock of the bank in its own favor. In *Bank of Holly Springs v. Pinson*,¹¹⁷ it was held that a by-law lien was not authorized by a charter and corporation act empowering the company to make by-laws to regulate the management of its business and the mode and manner of transferring its stock. In *Grafflin Co.*

¹¹⁴ 118 Mo. 431.

¹¹⁵ 11 Wall. (U. S.) 369.

¹¹⁶ 18 Wall. (U. S.) 589.

¹¹⁷ 58 Miss. 421.

v. *Woodside*,¹¹⁸ authority for the company to make by-laws for the management of its property and the transfer of its stock, did not give the company a right to create a by-law lien good against a *bona fide* purchaser. In *Anglo-Californian Bank v. Grangers' Bank*,¹¹⁹ it was held that the power of a corporation to make by-laws for the transfer of its stock, did not include the power to create liens thereon, affecting purchasers for value without notice. In *Driscoll v. West Bradley & Cary Mfg. Co.*¹²⁰ general power to make by-laws for the management of property, regulation of affairs and transfer of stock, was held not to authorize the creation of a by-law lien. In *Kinnan v. Sullivan County Club*,¹²¹ statutory authority to make by-laws for the regulation of the company's affairs and the transfer of its stock, was held not to authorize a by-law lien. And in *Bryon v. Carter*,¹²² it was held that statutory authority to direct the manner of transfer of stock, does not empower the company to prohibit the transfer so long as the owner owes it a debt.

The foregoing review of the cases seems to establish the rule that a mere by-law lien in favor of a corporation can never be legally asserted unless power to enact the by-law has been given to the corporation by the legislature; and further, that general statutory language authorizing the company to make by-laws regulating its business or property or the mode of transferring its stock, does not confer upon the company the power to make a by-law creating a lien in its own behalf for claims against its stockholders.

LIENS CREATED BY CONTRACT.

The law has never prohibited parties from creating liens upon property by agreement, which shall be valid against all who are parties to the agreement or take the property with actual notice of it. And under this general principle it has often been held that liens may exist in favor of corporations upon their stock by reason of agreement to that effect entered into between the corporation and its stockholders. Such agreements may be express or implied, and are subject largely to the same rules as apply to ordinary contracts. The cases in which the question has arisen are mostly those in which the contract is implied, and arises from a purchase of stock with a knowledge of the claim which the corporation makes upon it. Such claim may be asserted by an unauthorized provision in the

¹¹⁸ 87 Md. 146.

¹¹⁹ 63 Cal. 362.

¹²⁰ 59 N. Y. 96.

¹²¹ 26 N. Y. App. Div. 213.

¹²² 22 La. Ann. 98.

articles of association or in the by-laws, or by a statement to that effect in the certificate of stock, or by virtue of a usage.

If a lien is sought to be created in the articles of association, but is invalid as against the world because the statute does not authorize it, it may nevertheless be valid against anyone who takes the stock with knowledge of the provision for a lien, on the ground that by his own act he voluntarily consents to hold title subject to the lien. *Leggett v. Bank of Sing Sing*,¹²³ *Bradford Banking Co. v. Briggs & Co.*¹²⁴ And, generally, one who is not a *bona fide* purchaser for value takes subject to equities against his assignor, so that if his assignor held subject to such a lien by implied contract, the assignee takes a title equally subject to it. The case of *Mohawk National Bank v. Schenectady Bank*,¹²⁵ can be reconciled with other New York cases on this ground.

Similarly, if a by-law is made which in terms provides for a lien in favor of the corporation upon its own shares, but no statutory authority warrants such a lien, it may nevertheless be held good against all takers with notice, or against those who, not being innocent purchasers for value, are limited to a subordinate title held by their assignors, on the theory that while it is invalid as a by-law, it is good as a contract. Cases which are frequently cited as authority for the general validity of a by-law lien, such as *Child v. Hudson's Bay Co.*, referred to *supra*, are cases of this kind, and are only authority for the proposition that a by-law lien is good against those who consent to be bound by it and others standing in their shoes. The same may be said of *Farmers' & Traders' Bank v. Haney*,¹²⁶ *Planters' & Merchants' Mut. Ins. Co. v. Selma Bank*,¹²⁷ *In re Bachman*,¹²⁸ *Costello v. Portsmouth Brewing Co.*,¹²⁹ *Des Moines National Bank v. Warren County Bank*,¹³⁰ *Peoples' Home Bank v. Sadley*,¹³¹ *Bank of Culloden v. Bank of Forsyth*,¹³² *Tuttle v. Walton*,¹³³ and *Young v. Vough*.¹³⁴

A contract lien in favor of a corporation may also be asserted by a statement to that effect on the face of the certificate. Thus, in

¹²³ 24 N. Y. 283.

¹²⁴ 31 Ch. Div. 19.

¹²⁵ 78 Hun, (N. Y.) 90.

¹²⁶ 27 Iowa, 101.

¹²⁷ 63 Ala. 585.

¹²⁸ 2 Fed. Cas. No. 707.

¹²⁹ 69 N. H. 405.

¹³⁰ 97 Iowa, 204.

¹³¹ 1 Cal. App. 189.

¹³² 120 Ga. 575.

¹³³ 1 Ga. 43.

¹³⁴ 23 N. J. Eq. 328.

Jennings v. Bank of California,¹³⁵ a provision was inserted in a certificate of stock that no transfer would be made upon the books until after the payment of all indebtedness due to the corporation from the record holder of the stock. There was no statute or charter provision or by-law or usage to sanction the claim of lien, but the court held that by accepting the certificate the purchaser assented to a contract lien upon his stock. So, in *Vansands v. Middlesex County Bank*,¹³⁶ the certificate in controversy contained this provision on its face, "transferable at said bank only by him or his attorney, on surrender of this certificate, subject nevertheless to his indebtedness and liability at the bank, according to the charter and by-laws of said bank." Nothing in the charter or by-laws purported to give the bank a lien, but it was held that the statement in the certificate was binding on the purchaser, since his acceptance of it was tantamount to an agreement between him and the bank that his stock should be subject to a lien to secure his indebtedness to the bank.

And finally, a contract lien may arise from usage, of which the taker has notice and to which he gives his express or implied approval. In *Waln v. Bank of North America*,¹³⁷ there was no charter or by-law or written regulation of the board of directors, giving the bank a lien on its stock for debts due from its stockholders, but it was shown that there was a usage to that effect, which was known to the purchaser. The court said: "A course of dealing—a usage, an understanding, a contract, express or implied,—is the lien of the parties and a law to them. * * * The understood notice to Mr. Waln, his continuing to deal with the bank, with full knowledge of this term and condition, is equally binding on him and the present plaintiffs as if it were a written regulation, a by-law, a provision in the charter, or clause inserted in the very certificate of stock."

CONCLUSIONS.

The result of the foregoing study of the law relating to the creation and effect of liens in favor of corporations upon their own stock, seems to be, that such liens, in the absence of an agreement to which the holder is held to have assented, are not valid unless authorized by the legislature either through a special charter or a general act; that liens sought to be created by articles of association or by by-laws are equally ineffectual unless authority to create them

¹³⁵ 79 Cal. 323.

¹³⁶ 26 Conn. 143.

¹³⁷ 8 Serg. & R. (Pa.) 89.

can be traced to legislative action; and that in view of the great importance of certificates of stock in commercial transactions, and the vital necessity of preserving their commercial qualities, authority to create a lien cannot be derived from vague and general terms, but express and explicit language clearly empowering the corporation to assert such a lien must be found in the statute, if the claim of the corporation is to prevail against a *bona fide* purchaser for value and without notice.

EDSON R. SUNDERLAND.

UNIVERSITY OF MICHIGAN.