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CORPORATIONS-VALIDITY OF STOCKHOLDERS' VOTING CONTROL AGREEMENT

Bernard Goldstone
University of Michigan Law School

CORPORATIONS—VALIDITY OF STOCKHOLDERS' VOTING CONTROL AGREEMENT—*A*, *B*, and *C*, petitioners, and *X* and *Y*, respondents, owned all the stock in a corporation. On September 20, 1946, they entered into a ten year agreement which provided that *A*, *B*, *X* and *Y* should constitute the board of directors of the corporation as long as they remained stockholders. It was also agreed that *A*, *B*, *C*, *X* and *Y* were to be the officers of the corporation. At a meeting on January 21, 1948, attended by *X* and *Y*, three directors were elected, not including *A* and *B*. One week later these newly elected directors made themselves officers of the corporation. Petitioners claimed the elections of directors and officers violated the original agreement, and asked the court to set aside the election of the directors. *Held*, petition granted. The stockholders' agreement was valid, and the directors provided for in the agreement must be reinstated. *Application of Kirshner*, (Sup. Ct., Spec. Term, Queens County, Part 1), 81 N.Y.S. (2d) 435 (1948).

At common law stockholders may make an enforceable contract to vote their shares as a unit for the election of directors, if the contract does not contemplate fraud or tend to injure other stockholders.[1] Agreements by some of the stockholders or directors of a corporation which tend to control the voting of directors on matters within their official discretion, such as the election, compensation or tenure of officers, are held invalid,[2] because they violate the usual statutory provision that the business of a corporation shall be managed by its board of directors,[3] and because these limitations imposed upon the judgment of the directors are presumed injurious to stockholders who are not parties to the agreement.[4] When all the stockholders of a corporation are parties to the contract, as in the principal case, courts allow them to control corporate management by their agreement, to the extent of election, compensation or tenure of officers.[5] Although such contracts

[1] 5 FLETCHER, CYC. CORP., perm. ed., § 2064 (1931); Manson v. Curtis, 223 N.Y. 313, 119 N.E. 559 (1918); 18 C.J.S., Corporations, § 551; 71 A.L.R. 1289 (1931). Contra: Haldeman v. Haldeman, 176 Ky. 635, 197 S.W. 376 (1917). This type of agreement should be distinguished from a voting trust agreement where different principles apply. Hellier v. Achorn, 255 Mass. 273, 151 N.E. 305 (1926).

[2] West v. Camden, 135 U.S. 507, 10 S.Ct. 838 (1890); Haldeman v. Haldeman, 176 Ky. 635, 197 S.W. 376 (1917); Manson v. Curtis, 223 N.Y. 313, 119 N.E. 559 (1918); Cf., Bausch & Lamb Optical Co. v. Wahlgren, (D.C. Ill. 1932), 1 F. Supp. 799.

[3] See BALLANTINE, CORPORATIONS, § 183(4) (1946).

[4] Seitz v. Michel, 148 Minn. 80, 181 N.W. 102 (1921); McQuade v. Stoneham, 263 N.Y. 323, 189 N.E. 234 (1934).

[5] Clark v. Dodge, 269 N.Y. 410, 199 N.E. 641 (1936); Davis v. Argus Gas & Oil Sales Co., 167 Misc. 377, 3 N.Y.S. (2d) 241 (1938); Hayden v. Beane, 293 Mass. 347, 199 N.E. 755 (1936); Baran v. Baran, 59 D. & C. (Pa.) 556 (1947). Courts construe such agreements as providing that the persons named as officers will be retained only so long as they are efficient and faithful. In re Block's Will, (Surr. Ct. Bronx Co. 1946) 60 N.Y.S. (2d) 639 (1946); In re Roosevelt Leather Hand Bag Co., (Sup. Ct. Spec. Term, New York County, Part 1) 68 N.Y.S. (2d) 735 (1947).

impinge upon the broad statutory provisions concerning the exercise of directors' discretion,[6] there are no minority stockholders to be injured by the agreement, and, in the case of a closed corporation where the stockholders and directors are the same persons, independent judgment of the directors is a fiction.[7] Furthermore, it would seem desirable for courts to uphold agreements among less than all the stockholders, which deal with phases of corporate management, if an inquiry into the facts shows that no damage will result to any non-participating group, and if there is no substantial departure from the statutory requirement that the corporate affairs will be managed by the board of directors.[8] The principal case is one of the few decisions granting specific performance of a voting agreement, where the sole consideration of the contract is found in the mutual promise of the stockholders.[9] Although text writers state that specific performance will seldom be granted,[10] it is the only type of relief which can remedy the breach of the agreement in the instant case, since a suit for damages would not be feasible.[11]

Bernard Goldstone

[6] Where the corporation will be damaged by enforcement of the agreement it will not be held valid. Fells v. Katz, 256 N.Y. 67, 175 N.E. 516 (1931).

[7] 3 UNIV. CHI. L. REV. 640, 647 (1936). Some writers and courts argue that such corporations are little more than chartered partnerships and, as such, stockholders should be able to contract freely. Ripin v. U.S. Woven Label Co., 205 N.Y. 442, 98 N.E. 855 (1912).

[8] Meck, "Employment of Corporate Executives by Majority Stockholders," 47 YALE L. JOUR. 1079 (1938); 3 UNIV. CHI. L. REV. 640 (1936).

[9] Davis v. Argus Gas & Oil Co., 167 Misc. 377, 3 N.Y.S. (2d) 241 (1938); Baran v. Baran, 59 D. & C. 556 (Pa.) (1947). Contra: Johnson v. Spartanburg County Fair Assn., 210 S.C. 56, 41 S.E. (2d) 599 (1947); Roberts v. Whitson, (Texas Civ. App., 1945), 188 S.W. (2d) 875. Some courts will enforce specific performance only where there is present, in addition to mutual promises, an irrevocable proxy or a power coupled with an interest. Smith v. San Francisco & N.P. Ry. Co., 115 Cal. 584, 47 P. 582 (1897); Ringling Bros. Barnum and Bailey Combined Shows, Inc. v. Bailey, (Del. 1947) 53 A. (2d) 441.

[10] 5 FLETCHER, CYC. CORP., perm. ed., § 2067, (1931). But see, Clark v. Dodge, 269 N.Y. 410, 199 N.E. 641 (1936) (specific performance held unobjectionable); Fitzgerald v. Christy, 242 Ill. App. 343 (1926) (injunction sustained restraining any violation of voting agreement); Davis Gas & Oil Co. v. Argus, 167 Misc. 377, 3 N.Y.S. (2d) 241 (1938); Baran v. Baran, 59 D. & C. (Pa.) 556 (1947).

[11] See 3 COOK, CORPORATIONS, § 622a (1923); 15 UNIV. CHI. L. REV. 738 (1948).