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## CORPORATIONS--BY-LAWS--RESTRICTIONS ON TRANSFER OF BANK STOCK

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CORPORATIONS—BY-LAWS—RESTRICTIONS ON TRANSFER OF BANK STOCK—  
Plaintiff received thirty shares of bank stock by bequest. Before she presented  
the shares to the bank for transfer, the stockholders, by a majority vote (plaintiff

dissenting), amended the by-laws so as to limit to certain classes the persons to whom the bank stock could be transferred, whether by transfer inter vivos, will, or descent.<sup>1</sup> A mandamus proceeding was initiated against the bank to compel a transfer of the shares free of the restrictions. On defendants' appeal from a ruling denying a motion to quash an alternative writ, *held*, affirmed. The restrictions sought to be imposed were not authorized by statute. *Wentworth v. Russell State Bank*, (Kan. 1949) 205 P. (2d) 972.

The policy against restraints on alienation applies to shares of stock as well as to other kinds of property,<sup>2</sup> and any restriction on this inherent right of ownership should be strictly construed.<sup>3</sup> In view of the widespread adoption of the Uniform Stock Transfer Act, few cases arise today concerning the power of a corporation to restrict the transfer of its shares because the act impliedly permits such restrictions.<sup>4</sup> Where the above act is not in force,<sup>5</sup> it generally has been considered essential that a by-law which purports to restrict the transferability of shares be expressly authorized by the legislature.<sup>6</sup> This requirement rests on the belief that any attempt by a corporation to restrict the free alienation of its shares is beyond the corporate power. Such a proposition is of doubtful validity unless all restraints on alienation are to be regarded as void per se. Rather, the validity of such restraints is determined by what is reasonable in the light of (1) the extent to which practical alienability is restrained, and (2) the purpose of the restraint.<sup>7</sup> The decision in the principal case undoubtedly represents the numerical weight of authority,<sup>8</sup> and the result reached on the particular facts

<sup>1</sup> In general terms, the by-laws provided for (1) the Board to have pre-emptive right of purchase before offer to the public, (2) heirs-at-law or beneficiaries under a will or trust to be residents of a certain prescribed area, or, if residing beyond, to have been customers of the bank for a stipulated period of time, (3) heirs and beneficiaries not qualifying under (2) to have the right of disposal subject to the limitations in (1), and (4) the above restrictions to apply to the shares outstanding as well as to new issues. Principal case at 975.

<sup>2</sup> 12 FLETCHER, *CYC. CORP.*, perm. ed., §5452 (1932) and cases cited; 18 C.J.S., *Corporations*, §388, and cases cited.

<sup>3</sup> *McDonald v. Farley & Loetscher Mfg. Co.*, 226 Iowa 53, 283 N.W. 261 (1939).

<sup>4</sup> The Uniform Stock Transfer Act, §15, provides: "... and there shall be no restriction upon the transfer of shares so represented by virtue of any by-laws of such corporation, or otherwise, unless the right of the corporation to such lien or the restriction is stated upon upon the certificate."

<sup>5</sup> The Kansas legislature adopted the Uniform Stock Transfer Act, in part, in 1947, but did not enact §15, *supra*, note 4. Gen. Stat. of Kan. (Corrick, Supp. 1947) §§17-4801 to 17-4822. Also, §17-4821 states: "Except for section 13 [17-4813] hereof, the provisions of this act... shall not apply to certificates issued by domestic insurance, banking or building and loan corporations...."

<sup>6</sup> *Ireland v. Globe Mill. Co.*, 21 R.I. 9, 41 A. 258 (1898); *Kretzer v. Cole Bros. Lightning Rod Co.*, 193 Mo. App. 99, 181 S.W. 1066 (1916); but, cf. *Mason v. Mallard Tel. Co.*, 213 Iowa 1076, 240 N.W. 671 (1932).

<sup>7</sup> 2 SIMES, *FUTURE INTERESTS*, §§440, 472 (1936).

<sup>8</sup> See cases cited in 138 A.L.R. 647 (1942), supplementing annotation in 65 A.L.R. 1159 (1930).

can be defended on other grounds.<sup>9</sup> However, there is little to justify the practical effect or the underlying policy of the decision. The reasoning of the court necessarily points to a mechanical and inflexible rule that any limitation on the right of transfer is invalid in the absence of statute. Such a rule will fetter corporations in the accomplishment of their valid aims and purposes<sup>10</sup> in the name of a policy of complete freedom of alienation, which it is neither the desire nor the duty of the law to perpetuate.

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<sup>9</sup> The decision of the court made it unnecessary to consider the question of reasonableness of the restrictions, or their applicability to persons who were shareholders before the by-laws were passed. The court said, "We shall not discuss motives, good faith or the possibility of compliance, for they are not determinative of the issues presented." Principal case at 979.

<sup>10</sup> "Stock in a corporation is not merely property. It also creates a personal relation analogous otherwise than technically to a partnership. . . . there seems to be no greater objection to retaining the right of choosing one's associates in a corporation than in a firm." Holmes, C. J., in *Barrett v. King*, 181 Mass. 476 at 479, 63 N.E. 934 (1902).