

DISTINCTIONS BETWEEN TRUSTEERING STOCK AND
SELLING IT TO A CORPORATION

(1) Where stock is transferred to a trustee to hold it for the benefit of the transferor, legal title passes to the trustee, but equitable title remains in the transferor; whereas the sale of stock to a corporation in which the seller owns stock transfers both legal and equitable title to the purchasing corporation.

(2) Where stock is transferred to a trustee for the benefit of the transferor, the transferor is entitled to all the income therefrom and the entire proceeds of any sale thereof; whereas the sale of stock to a corporation in which the seller owns stock deprives the seller of any right to the income from the stock sold or the proceeds of any resale thereof in the absence of express contract to the contrary. In the latter case the seller of the stock can thereafter share in such income or proceeds of sale only if the directors of the purchasing corporation choose to declare dividends and only in the proportion which his number of shares in the purchasing corporation bears to the total outstanding shares of said corporation.

(3) If a person transfers National bank stock to a trustee for his own benefit, he remains liable for any assessment thereon; whereas a bona fide, unconditional sale of bank stock to a bona fide corporation prevents the seller from being liable for any stockholders liability incurred thereafter.

(4) Where stock is transferred to a trustee for the transferor's benefit, the transferor can retain the right to vote the same or to instruct the trustee how to vote it; whereas an unconditional sale of stock to a corporation deprives the seller of any right to vote the stock or to direct the manner in which it can be voted, unless the seller is in a position to control the management of the corporation.

(5) Where stock is transferred to a trustee for the transferor's benefit the transferor remains subject to taxation on such stock; whereas the bona fide, unconditional sale of stock to a corporation relieves the seller of any further liability for taxes subsequently levied on such shares.

(5) Where stock is transferred to a trustee for the transferor's benefit, it is not subject to the claims of the creditors of the trustee; whereas stock sold unconditionally to a corporation becomes subject to the claims of all creditors of the corporation.

Effect of the Sale

The sale by Governor Eccles of his stock in the First Security Corporation, of Ogden, to the Eccles Investment Company, of which he is a minority stockholder owning less than 9 per cent of the total stock, resulted in a material change not only in the legal and equitable situation, but in the practical situation as well.

Formerly Governor Eccles was a stockholder in the First Security Corporation; now he is not a stockholder.

Formerly he could vote at stockholders meetings of the First Security Corporation; now he cannot vote at stockholders meetings.

Formerly he had to pay taxes on such stock and on the income therefrom; whereas he no longer has to pay such taxes.

Formerly he had the absolute right to sell, pledge or give away the stock to whom he pleased; whereas he no longer has any such right.

Formerly he was entitled to the entire income from such stock and the entire proceeds of any sale thereof; now the Eccles Investment Company is entitled to the income and proceeds of sale, and Governor Eccles can obtain none of it unless the corporation chooses to pay a dividend or make a distribution of assets. Even in the latter event, instead of receiving all of such income or proceeds of sale of such stock, he would receive less than 9 per cent thereof and the other stockholders of the Eccles Investment Company would receive more than 91 per cent.

It is well settled that the ownership by a person of stock in a corporation which is a stockholder in another corporation does not make such person a stockholder in the second corporation.

This is so obvious to persons familiar with corporation law that the question has seldom been raised in court; but a hasty search has revealed at least two cases in which this question has been squarely passed upon by the courts.

In the case of Hoopes v. Basic Co., 69 N. J. Eq. 679, 61 Atl. 979, the plaintiff filed a bill to have the Basic Company placed in receivership. The bill was filed under a statute providing that "any creditor or stockholder" could request the appointment of a receiver. The defendant sought to have the bill dismissed on the ground that the plaintiff was not a creditor or stockholder. The evidence showed that plaintiff was a stockholder of the Union Dredging Company which owned stock in the Basic Company and that the plaintiff held in his own name only one directors' qualifying share of stock in the Basic Company, which admittedly belonged to the Union Dredging Company. On the basis of these facts, the court held that the plaintiff was not a stockholder of the Basic Company and therefore, the court dismissed the bill.

This case is especially notable because it was a suit brought in the Court of Chancery of the State of New Jersey, which does not hesitate to disregard corporate fictions or look through the form to the substance of a transaction whenever the ends of justice or equity required such action.

The case was appealed to the Court of Errors and Appeals of New Jersey, the highest court of the State, which affirmed the decision of the Chancery Court by a per curiam opinion (65 Atl. 1118) as follows:

"We agree with the Vice Chancellor that the proofs show that Mr. Hoopes was not a stockholder within the meaning of the statute, and therefore could not maintain this suit. It is not necessary to express any opinion upon other matters discussed by the Vice Chancellor."

In the case of Sabre v. United Traction and Electric Co. et al., 225 Fed. 601, the court held that stockholders in holding companies are not stockholders or entitled to the rights of stockholders in other corporations, a part of whose stock is owned by the holding company and that, therefore, a sale or lease of all the property of a corporation controlled by the holding company through its ownership of stock does not require the unanimous consent of the stockholders of the holding company; but it is sufficient if there is unanimous consent of the stockholders of the company whose property is leased or sold. In so holding the court said:

"It is impossible, however, to accept the contention that the nonassent of a shareholder of the Traction Company should be given the same effect as the nonassent of a shareholder in each of the lessor street railway companies. Neither as a matter of form nor as a matter of substance can the complainant be regarded as a shareholder, or entitled to claim the rights of a shareholder in any one of the lessor companies. He is merely a shareholder in a corporate owner of all the stock of the street railway corporations, each of which is still a distinct corporation whose individual existence cannot be ignored."

In the course of its opinion, in the case of Breck v. Poor, 216 N. Y. 387, 111 N. E. 229, 234, the Court of Appeals of New York said:

"One who by purchase or otherwise becomes the owner of all the capital stock of a private corporation does not

thereby become the legal owner of its property, but title to the latter is vested in the corporate entity. *Button v. Hoffman*, 61 Wis. 20, 20 N. W. 667, 50 Am. Rep. 131.

"In no legal sense can the business (or in an equal sense the property) of a corporation be said to be that of its individual stockholders. It is true that they have an interest in the business carried on, and an influence in controlling its conduct, but they have created a legal entity, * * * and that entity is alone responsible to persons dealing with it for the conduct of such business.' *People v. Am. Bell Telephone Co.*, 117 N. Y. 241, 255, 22 N. E. 1057, 1062."