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STATUTORY MERGER AND CONSOLIDATION OF CORPORATIONS

FOR over a hundred years, corporations in the United States have tended to unite into larger forms of organization. In the various periods in which this tendency has been most pronounced, the motives for, and the forms of combination have frequently been quite different. In the period prior to 1900, the desire to monopolize was the principal motivating force, later it was the economies of large-scale production, and most recently it appears to be the advantages of large-scale marketing. The forms of combination have included pools, trusts, interlocking directorates, leases, holding companies, sales of entire corporate assets, and statutory merger or consolidation.[1] Of these,

1. BURCHETT, CORPORATION FINANCE (1934) c. 16; OWENS, BUSINESS ORGANIZATION AND COMBINATION (1934) c. 11; Thorp, *The Persistence of the Merger Movement* (1931) 21 AM. EC. REV. SUPP. 77. Compare motives and factors leading to the recent sale of assets by the Corrigan, McKinney Steel Company to the Republic Steel Corporation. N. Y. Times, Sept. 24, 1935, at 35, col. 1; Business Week, Sept. 1, 1934, at 27.

the device of statutory merger or consolidation is among the oldest, having had its origin in state statutes in the eighteen-twenties. It has since been consistently used up to the present, during which time the legislatures and courts have combined to attach to merger and consolidation peculiar legal incidents and attributes which make them forms of combination strikingly unlike any other.[2]

While it is not uncommon to treat the terms merger and consolidation as synonymous, at the present time the tendency is to regard each as representing a distinct type of combination. Thus, merger signifies the absorption of one or more existing corporations by another existing corporation which retains its corporate identity; its rights, privileges, franchises and properties, however, being enlarged to the extent of the rights, privileges, franchises and properties of the absorbed corporations, whose existence thereupon terminates.[3] Consolidation, on the other hand, is the unification of two or more existing corporations into a new corporate entity which has the combined rights, privileges, franchises and properties of the original or constituent corporations, all of which lose their corporate existences.[4] These technical meanings have gradually evolved over the period of years since the origin of statutory merger and consolidation. In some statutes the distinction between the two has been recognized for a comparatively long time, in others it has been made very recently, while in still others the two terms continue to be used loosely and interchangeably.[5] But despite the fact that the two terms are still used inter-

2. However, save for the period prior to 1860, the merger and consolidation device has never been the most widely used form of combination. The likelihood of increase in its use today is considered *infra,* p. 133.

3. See Cortland Specialty Co. v. Commissioner, 60 F. (2d) 937, 939 (C. C. A. 2d, 1932); News Publishing Co. v. Blair, 29 F. (2d) 955, 958 (App. D. C. 1928); Fordyce v. Helvering, 76 F. (2d) 431, 434 (App. D. C. 1935); State v. Atlantic Coast Line Rr. Co. 202 Ala. 558, 560, 81 So. 60, 62 (1918); Graeser v. Phoenix Finance Co., 218 Iowa 1112, 1121, 254 N. W. 859, 864 (1934); 15 FLETCHER, PRIVATE CORPORATIONS (rev. ed. 1932) § 7041; 8 THOMPSON, CORPORATIONS (3d ed. 1927) § 6012; Field, *Nature of and Procedure for Direct Property Owning Consolidations* (1933) 5 ROCKY MT. L. REV. 230, 231.

4. See Pinellas Ice & Cold Storage Co. v. Commissioner, 57 F. (2d) 188, 190 (C. C. A. 5th, 1932); Carolina Coach Co. v. Hartness, 198 N. C. 524, 528, 152 S. E. 489, 491 (1930); Collinsville Nat. Bank v. Esau, 74 Okla. 45, 47, 176 Pac. 514, 516 (1918); Union Indemnity Co. v. Railroad Comm., 187 Wis. 528, 536, 205 N. W. 492, 495 (1925); also the cases and authorities cited *supra,* note 3. The term amalgamation is used by financial writers in preference to consolidation, to indicate the narrow sense in which it is being used. See OWENS, op. cit. *supra* note 1, at 368.

5. Examples of statutes which do not distinguish between merger and consolidation include ALA. CODE ANN. (Michie, 1928) § 7037; CONN. GEN. STAT. (1930) §§ 3462, 3465; N C. CODE ANN. (Michie, 1931) § 1224(a). The Federal Banking Act uses the term "consolidation" but provides only for merger. 44 STAT. 1224 (1927), as amended 48 STAT. 190 (1933), 12 U. S. C. A. § 34a (1934). Courts as well are prone to use the two interchangeably. See in re Buist's Estate, 297 Pa. 537, 540, 147 Atl. 606, 607 (1929). Some courts recognize the distinction, but refuse to apply it as too technical. See Jewett City Savings Bank v. Board of Equalization, 116 Conn. 172, 182, 164 Atl. 643, 646 (1933). For a suggestion that in the future the tendency will be to disregard the distinction, see BURTCHETT, op. cit. *supra* note 1, at 765 n. 1.

changeably the distinction is an important one, and becomes highly significant in certain cases.[6]

Nevertheless, while merger and consolidation differ from each other in this fundamental respect, they have so many features in common that they are ordinarily treated together as a single type of device for combination, as distinguished from other means of combination which also result in bringing several existing corporations under one common control.[7] Most similar to the merger and consolidation device is the combination effected in the case where one corporation sells all of its assets to a second corporation in return for stock, after which the selling corporation distributes the stock received to its stockholders and then formally dissolves. Although merger and consolidation is strictly statutory and a sale of assets is essentially contractual, as a practical matter in a given case it may be extremely difficult to decide whether the device employed was merger and consolidation or a sale of assets inasmuch as today, the latter also usually follows a statutory procedure.[8] Nevertheless, the statutory procedure of effecting a merger or consolidation is different from that of a sale of assets, and different incidents ensue upon following the different procedures. Both of these factors may serve to distinguish them. Thus, for example, in merger and consolidation, all the participating corporations, save the surviving corporation in the case of merger, lose their corporate identities by virtue of the transaction itself, while upon a sale of assets the selling corporation retains its corporate identity until some formal dissolution

6. Organization taxes, federal jurisdiction, and special privileges and exemptions, are instances in which the distinction becomes important. See *infra* p. 128.

7. Where only one corporation is involved as in a reorganization, the process can scarcely be termed a device for combination. In this connection, however, notice should be taken of the expanded meaning given merger and consolidation in the Revenue Act of 1924, 43 STAT. 257 (1924), 26 U. S. C. A. § 934 (h) (1) (A) (1928). In the Revenue Act of 1934, 48 STAT. 705 (1934), 26 U. S. C. A. § 112 (g) (1) (A) (1935), statutory merger and consolidation seems to be confined to its true meaning, although still designated as a type of reorganization for the purposes of the Act. Cf. also Pinellas Ice & Cold Storage Co. v. Commissioner, 57 F. (2d) 188 (C. C. A. 5th, 1932), aff'd 287 U. S. 462 (1933); Ahles Realty Corp. v. Commissioner, 71 F. (2d) 150 (C. C. A. 2d, 1934); Helvering v. Winston Bros. Co., 76 F. (2d) 381 (C. C. A. 8th, 1935); Comment (1935) 45 YALE L. J. 134.

8. In the absence of a statutory procedure, a prosperous corporation may always sell all its assets and dissolve when all the stockholders consent. In some jurisdictions this could be done by majority consent. See Warren, *Voluntary Transfers of Corporate Undertakings* (1916) 30 HARV. L. REV. 335; (1932) 41 YALE L. J. 908. At the present time statutory provisions in forty states authorize sales of entire corporate assets on the consent of proportions of stockholders varying from a majority to four-fifths. But this statutory procedure is usually quite distinct from that of the merger and consolidation statutes, and the objects of a sale of assets are quite outside the purposes of the merger and consolidation statutes. See Cortland Specialty Co. v. Commissioner, 60 F. (2d) 937, 939 (C. C. A. 2d, 1932). There must usually be an intent to follow the merger or consolidation statute. Blackstone v. Chandler, 15 Del. Ch. 1, 130 Atl. 34 (Ch. 1925); Graeser v. Phoenix Finance Co., 218 Iowa 1112, 254 N. W. 859 (1934); Beardstown Pearl Button Co. v. Oswald, 130 Ill. App. 290 (1906). However, the fact that courts will frequently call a sale of assets a merger or consolidation complicates the problem. See United States v. Republic Steel Corp., 11 F. Supp. 117 (N. D. Ohio, 1935); cf. Polk County Lumber Co. v. Dwiggins, 100 Fla. 559, 129 So. 859 (1930).

process has been carried out; and in merger and consolidation no instruments are necessary to pass title, but in a sale of assets deeds and bills of sale must be used.[9] More easily distinguishable from the process of merging and consolidating by reason of the procedure followed and incidents attaching thereto, are the processes employed to bring corporations under common control by means of a sale of assets in return for cash or obligations of the purchasing corporation,[10] by means of a holding company,[11] and of long term leases by one corporation of all the properties of another corporation.[12]

The Process of Merger or Consolidation. Statutory authorization is essential before a merger or consolidation may be effected, and an attempt to merge or consolidate without such authorization is an absolute nullity; not even a *de facto* surviving or consolidated corporation is formed.[13] It has been fundamental from the very origin of the merger and consolidation device that the general grant of corporate powers does not constitute a sufficient authorization; there must be an express grant by the legislature to each of the corporations wishing to participate in the merger or consolidation. This grant may exist in a special or general act, in the corporate charter, or by virtue of special legislative confirmation of a previously unauthorized merger or consolidation.[14]

9. Other points of difference are that in merger and consolidation, the plan by which the stockholders exchange their shares in the constituents for shares in the surviving or consolidated corporation is part of the merger or consolidation agreement; in a sale of assets the distribution of the shares received is not part of the sale contract. The stockholders of each corporation participating in a merger and consolidation, must give their approval, but in a sale of assets only the stockholders of the selling corporation must consent. In merger and consolidation the surviving or consolidated corporation will be liable for the debts, liabilities, and obligations of the constituents, usually by express statutory imposition; in a sale of assets such statutory imposition is exceedingly rare. Hills, *Consolidation of Corporations by Sale of Assets and Distribution of Shares* (1931) 19 CALIF. L. REV. 349. But the vendee corporation in the latter case may be held liable on other grounds. See *infra* note 95.

10. Drovers' & Mechanics' Nat. Bank v. First Nat. Bank, 260 Fed. 9 (C. C. A. 4th, 1919); Prairie Oil & Gas Co. v. Motter, 66 F. (2d) 309 (C. C. A. 10th, 1933).

11. Bee Bldg. Co. v. Daniel, 57 F. (2d) 59 (C. C. A. 8th, 1932); Coudon v. Tait, 56 F. (2d) 208 (D. Md. 1932); cf. Venner v. Chicago City Ry. Co., 258 Ill. 523, 101 N. E. 949 (1913); Gallatin Natural Gas Co. v. Public Service Comm., 79 Mont. 269, 256 Pac. 373 (1927).

12. State v. Montana Ry. Co., 21 Mont. 221, 53 Pac. 623 (1898); cf. Black v. St. Louis & S. F. Rr. Co., 110 Mo. App. 198, 85 S. W. 96 (1905).

13. Gott v. Live Poultry Transit Co., 17 Del. Ch. 288, 153 Atl. 801 (Ch. 1931); American Loan & Trust Co. v. Minnesota & N. W. Rr. Co., 157 Ill. 641, 42 N. E. 153 (1895); First State Bank of Mangum v. Lock, 113 Okla. 30, 237 Pac. 606 (1925).

14. Pearce v. Madison & I. Rr. Co. and Peru & I. Rr. Co., 21 How. 441 (U. S. 1858); Mead v. New York, Housatonic & Northern Rr. Co., 45 Conn. 199 (1877); Gunggoll v. Outer Drive Athletic Club, 349 Ill. 406, 182 N. E. 409 (1932); State v. Bailey, 16 Ind. 46 (1861); Riker & Son v. United Drug Co., 79 N. J. Eq. 580, 82 Atl. 930 (Ct. Errors and App. 1912); New York & Sharon Canal Co. v. Fulton Bank, 7 Wend. 412 (N. Y. 1831); Jones v. Rhea, 130 Va. 345, 107 S. E. 814 (1921). The power to merge or consolidate cannot be implied from the power to dissolve. Garrett v. Reid-Cashion Land & Cattle Co., 34 Ariz. 245, 270 Pac. 1044 (1928); Doe Run Lead Co. v. Maynard, 283 Mo. 646, 223 S. W. 600 (1920). Where a consolidation agreement was entered into prior to the repeal of the statute and the stockholders' approval was obtained thereafter, the consolidation was held valid. Cameron

At the time the merger and consolidation device originated, corporations were created solely by special legislative acts. Consequently, the earliest sources of the power to merge or consolidate were also special acts. When the lines of two railroads or canals happened to connect, the advantages to be derived from a single continuous line under unified control appear to have first suggested the use of merger or consolidation, and special acts authorizing such were passed.[15] These early acts were invariably brief, simply authorizing the corporations involved to "unite" their capital stocks[16] or interests,[17] or they merely stated that the stockholders of one corporation were thereby constituted stockholders of the second corporation, and vice-versa.[18] As railroads expanded, their incorporators began to foresee that authority to merge or consolidate might be useful, so at their instigation, legislatures often included this power in the original charter.[19]

The first general statute authorizing the consolidation of railroads was passed in Indiana in 1853,[20] and soon thereafter similar general statutes were enacted in most of the states in which railroads had become important.[21] As

v. N. Y. & Mt. Vernon Water Co., 133 N. Y. 336, 31 N. E. 104 (1892). Where merger and consolidation are recognized as distinct, authority to merge is no authority to consolidate, and vice-versa. Adams v. Yazoo & Miss. Valley Rr. Co., 77 Miss. 194, 24 So. 200 (1898). But cf. Meyer v. Johnston & Stewart, 64 Ala. 603 (1879); Chicago, S. F. & C. Ry. Co. v. Ashling, 160 Ill. 373, 43 N. E. 373 (1896).

15. It has been suggested that the merger or consolidation device originated in connection with turnpike roads. Bisbee, *Consolidation and Merger*, 8 LECTURES ON LEGAL TOPICS (1931) 365, 368; OWENS, op. cit. *supra* note 1, at 369. But it seems that the advent of the railroad, and to a lesser degree, that of the canal, was the beginning of this method of combination, at least insofar as true statutory merger and consolidation are concerned. A survey of the statutes of Delaware, Massachusetts, Maryland, New Jersey, New York, Ohio, Pennsylvania and Virginia for the period from 1820 to 1850 indicates that the number of grants of power to merge and consolidate to railroads far exceeded those to any other corporations, and the statutes granting this power to turnpike companies, in particular, are very few.

16. E. g. Del. Laws 1833, c. 241; Pa. Laws 1837, No. 1; N. J. Acts 1853, c. 90.

17. E. g. Pa. Laws 1832, No. 68, § 4.

18. E. g. Mass. Laws 1827, c. 74, § 1; Mass. Laws 1840, c. 50, § 1. "Union" or "unite" were the terms most commonly used in these early statutes, and while "consolidate" occasionally appeared, the term "merge" was rarely used. E. g. Md. Laws 1854, c. 250, § 1; N. J. Acts 1831, p. 124, § 1; N. Y. Laws 1850, c. 236, § 1; Pa. Laws 1832, No. 68, § 4. Where the corporations were of different states a grant of authority from each legislature was necessary, each one making its own grant dependent on the other legislatures making similar grants. E. g. Del. Laws 1835, c. 9, § 1; Va. Acts 1848, c. 146, § 3. This type of legislation is within the powers of the respective legislatures and does not involve extra-territorial legislation. Railroad Co. v. Harris, 12 Wall. 65, 82 (U. S. 1870); Ashley v. Ryan, 153 U. S. 436 (1894); Alabama City, G. & A. Ry. Co. v. Kyle, 202 Ala. 552, 81 So. 54 (1918); Boardman v. Lake Shore & M. S. Ry. Co., 84 N. Y. 157 (1881); see Mackay v. N. Y., N. H. & H. Rr. Co., 82 Conn. 73, 90, 72 Atl. 583, 589 (1909).

19. E. g. Del. Laws 1831, c. 83, § 24; Mass. Acts & Resolves 1844, c. 134, § 6; N. Y. Laws 1836, c. 262, § 11.

20. Ind. Laws 1853, c. 85.

21. See Ill. Laws 1854, p. 9; Ohio Acts 1856, p. 143; N. Y. Laws 1869, c. 917; S. C. Acts 1870, No. 232. The Ohio statute of 1856 was in many respects similar to the ordinary merger and consolidation statutes of today.

industrial and business corporations grew in importance, general merger or consolidation statutes were passed in relation to them. At first the privilege was usually extended only to such corporations as were engaged in the same or similar business, but today this restriction has largely disappeared save in connection with public utility corporations, insurance companies, and banks and trust companies.[22] At the present time, thirty-three states have what might be called general statutes authorizing merger or consolidation, or both,[23] while in the remainder of the states a special act would still be necessary to effectuate this type of combination.[24] Of those states having general merger or consolidation statutes, thirteen seem to confine the power to mergers or consolidations of domestic corporations with other domestic corporations,[25] and while the other twenty expressly authorize domestic corporations to merge or consolidate with corporations of other states, at least three of these require that the surviving or consolidated corporation shall be a corporation of that state only.[26] Several general statutes allow merger or consolidation of corporations of their state with federal corporations.[27]

Practically all statutes require as an initial step that a joint agreement be

22. E. g. CONN. GEN. STAT. (1930) § 3462; MD. ANN. CODE (Bagby, 1924) art. 23, § 33; N. Y. STOCK CORP. LAW (1923) § 85, §1, as amended, N. Y. Laws 1924, c. 441, § 15 (merger only). As to what is the same or similar kind of business, see Colgate v. United States Leather Co., 75 N. J. Eq. 229, 72 Atl. 126 (Ct. Errors and App. 1909); York Haven Water & Power Co. v. Public Service Comm. 287 Pa. 241, 134 Atl. 419 (1926); cf. Neff v. Gas & Electric Shop, 232 Ky. 66, 22 S. W. (2d) 265 (1929).

23. The remaining states, however, often have merger or consolidation statutes in respect to certain classes of corporations, such as railroads, banks, insurance companies. E. g. MISS. CODE ANN. (1930) §§ 6082, 6105, sanctioning merger and consolidation of railroad companies. A recent tendency is to enact general merger and consolidation statutes for non-profit corporations, which as a general rule do not fall within the ordinary merger and consolidation statute. E. g. ILL. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 188a; PA. STAT. ANN. (Purdon, 1934) tit. 15, § 2851-801.

24. However, in those states having no merger or consolidation statutes, substantially similar results can be attained by a sale of assets or some other device. The absence of a merger or consolidation statute does not indicate that a state has a policy against attaining the practical results of merger or consolidation by another device. J. H. Lane & Co. v. Maple Cotton Mills, 226 Fed. 692 (C. C. A. 4th, 1915).

25. Connecticut, Colorado, Illinois, Indiana, Maryland, Minnesota, Missouri, North Carolina, North Dakota, Ohio, South Carolina, Utah, and West Virginia. However, in those thirteen states, certain special classes of corporations, particularly railroads, may have the power to merge or consolidate with railroad corporations of other states.

26. The twenty states are Alabama, Arkansas, California, Delaware, Florida, Idaho, Kansas, Kentucky, Louisiana, Maine, Michigan, Montana, Nevada, New Jersey, New York, New Mexico, Pennsylvania, Tennessee, Virginia, and Washington. Of these, statutes in Kentucky, Maine, Virginia, and possibly Montana require that the surviving or consolidated corporation shall be a corporation of that state only. In New Jersey, there may be some doubt as to whether the consolidated corporation can become a corporation of any state other than New Jersey. See N. J. COMP. STAT. (Supp. 1930) tit. 47, § 104.

27. E. g. Ark. Laws 1031, c. 255, § 67; TENN. CODE ANN. (Williams, 1934) § 3755. However, this situation is usually dealt with under the banking statutes, for the case most frequently arising is where a state bank or trust company wishes to merge into a national bank.

drawn up by the boards of directors of the corporations desiring to merge or consolidate, setting forth the "terms and conditions of the merger or consolidation," and the "mode of carrying the same into effect."[28] It is at this stage of the process of effecting a merger or consolidation that many of the most difficult problems are encountered. Originally, negotiations preparatory to the drawing up of the joint agreement were conducted by committees of the boards of directors of the corporations, or occasionally by the boards themselves.[29] Today, however, this intermediate role frequently will be filled by professional promoters or groups of investment bankers, in which case it is desirable but not essential that they have no interest in any one corporation.[30] At this stage of the proceedings, from the point of view of those promoting the transaction, the prevention of the formation of any dissentient groups, either among the stockholders or the managements of the constituent corporations, is extremely important, for once formed, such groups may be able materially to impede the progress of the merger or consolidation, and possibly even to prevent its completion.[31] This problem is obviated, of course, where a holding company undertakes to merge or consolidate a number of its wholly owned subsidiaries, and in such a case merger or consolidation becomes little more than a matter of drafting an agreement which will accomplish the desired purposes. But where the holding company owns only a controlling interest in the subsidiaries, care must be taken so that the agreement will not prejudice the interests of minority stockholders, for otherwise such stockholders may be able to enjoin the transaction.[32]

In preparation of the agreement of merger or consolidation, the principal problem concerns a basis for the exchange of shares which will properly reflect the relative rights, privileges, and interests of the stockholders of the constituents in the surviving or consolidated corporation. This basis should be such that the stockholders of each constituent will receive an amount of stock of the surviving or consolidated corporation proportionate to the value of the contribution which their constituent is making to the surviving or consolidated corporation. In valuing these contributions, two elements are usually to be considered: the net assets and the earning power of each constituent. In order to evaluate net assets and earning power properly, they must be examined from a uniform accounting approach, thus eliminating discrepancies which might arise from different methods and rates of depreciation, from different ways of determining costs, and from other sources. Once the contributions have been valued, the particular manner in which the shares are exchanged depends on the circumstances of each individual case, although

28. E. g. DEL. REV. CODE (1915) § 1973, as amended Del. Laws 1929, c. 135, § 18; N. J. COMP. STAT. (1911) tit. 47, § 105.

29. See STEVENS, THE BEGINNINGS OF THE NEW YORK CENTRAL RAILROAD (1920) c. 17.

30. See OWENS, op. cit. *supra* note 1, at 372.

31. See Field, *Holding Corporation Control as a Provisional Form of Consolidation* (1932) 8 J. LAND & PUB. UTIL. EC. 87, 89; Business Week, Sept. 21, 1929, at 22.

32. Field, *supra* note 31, at 87. Among the suggested advantages of the holding company as an intermediate step in the merger and consolidation process are the elimination of opposition by corporate officers and minority stockholders, of difficulties of negotiating comparative values, and of harmonizing corporate constituents.

a common practice is for the surviving or consolidated corporation to issue preferred stock to represent the contributions of net assets, and common stock to represent the prospective earnings which are expected to accrue as a result of the transaction.[33]

Provisions for secured and unsecured creditors of the constituents normally give rise to few problems at the agreement stage. Today all statutes expressly protect such groups, and the ordinary procedure is simply for the surviving or consolidated corporation to assume all debts, liabilities, and obligations in the agreement of merger or consolidation.[34] However, in regard to bonded indebtedness, in the interest of simplicity in financial structure it may be desirable to provide for an exchange of bonds of the surviving or consolidated corporation for the bonds of the constituents which are outstanding.[35] Since the value of a bondholder's interest is usually ascertainable, an exchange of bonds involves but few difficulties, and in the absence of any impairment of his security, the bondholder will generally find it desirable to make the exchange.

After the joint agreement of merger or consolidation has been consummated, the statutes require its submission for approval or rejection to the stockholders of each corporation participating in the transaction, frequently at a meeting called specially for that purpose.[36] In the earliest mergers and consolidations the principles became firmly established that a stockholder of a constituent corporation could not be forced to become a stockholder of the surviving or consolidated corporation,[37] and that the unanimous consent of the stockholders was necessary to effectuate a merger or consolidation, unless some provision for approval by a lesser proportion could be read into the contract between the constituent corporation and its stockholders.[38] The basis of both

33. See 2 FINNEY, PRINCIPLES OF ACCOUNTING (1924) c. 47; GERSTENBERG, FINANCIAL COMBINATION AND MANAGEMENT OF BUSINNESS (1924) c. 29; KESTER, ADVANCED ACCOUNTING (3d rev. ed. 1933) c. 30.

34. See *Rights and Remedies of Creditors, infra* p. 122.

35. BURTCHETT, op. cit. *supra* note 1, at 774. Problems in connection with bonds which may arise in drafting the agreement of merger or consolidation include: (1) Where by the terms of the trust indentures of the mortgages of the constituents, the after-acquired property clauses will operate so as to extend the liens of those mortgages to the property which the surviving or consolidated corporation may thereafter acquire. To avoid confusion in the future from overlapping liens, it may be possible to provide for the replacement of the old bonds with new ones. (2) Where a constituent has outstanding bonds convertible into stock at the option of the holder, if the conversion instrument is such that the surviving or consolidated corporation will be required to convert bonds into stock in accordance with the terms of exchange of the merger or consolidation agreement, it is desirable to make some provision for setting aside stock for this purpose.

36. E. g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, §§ 157.63, 157.64; N. Y. STOCK CORP. LAW (1923) § 86 (8) (b).

37. Booe v. Junction Rr. Co., 10 Ind. 93 (1857); Lauman v. Lebanon Valley Rr. Co., 30 Pa. 42 (1858).

38. Nugent v. The Supervisors, 19 Wall. 241 (U. S. 1873); In re Interborough Consolidated Corp. 277 Fed. 455 (S. D. N. Y. 1921); Botts v. Simpsonville & B. C. Turnpike Road Co., 88 Ky. 54, 10 S. W. 134 (1888); Kirby v. Saginaw Hotels Co., 253 Mich. 308, 235 N. W. 153 (1931); cf. Garrett v. Reid-Cashion Land & Cattle Co., 34 Ariz. 245, 270 Pac. 1044 (1928).

propositions seems to have been that a merger or consolidation involved such a radical change in the nature and extent of the corporate enterprise to which the stockholder had subscribed, that it amounted to an impairment of the obligation of the contract between the stockholder and the corporation.[39] Since the requirement of unanimous consent greatly diminished the utility of the device, at an early period statutes began to provide for merger or consolidation by a lesser proportion of stockholders.[40] If this statute was in existence when a stockholder subscribed to stock, the statute became part of the contract, and thereafter, while he still could not be forced to become a stockholder in the surviving or consolidated corporation,[41] he could no longer prevent the stipulated proportion of stockholders from bringing about a merger or consolidation.[42] Today the statutes provide for approval by proportions of total shares outstanding varying from a simple majority in some states to two-thirds and three-fourths in others.[43] By some statutes only voting stock is entitled to vote on the question,[44] in one the transaction is regarded as

39. Mowrey v. Indianapolis & C. Rr. Co., 17 Fed. Cas. No. 9, 891, p. 930 (C. C. D. Ind. 1866); Botts v. Simpsonville & B. C. Turnpike Road Co., 88 Ky. 54, 10 S. W. 134 (1888); see Mills v. Central Rr. Co., 41 N. J. Eq. 1, 4, 2 Atl. 453, 454 (Ch. 1886). *Contra:* Mayfield v. Alton Ry., Gas & Electric Co., 198 Ill. 528, 65 N. E. 100 (1902).

40. E. g. Mass. Acts & Resolves 1849, c. 223, § 11 (majority); N. J. Acts 1831, p. 124, § 1 (seven-eighths); Pa. Laws 1856, No. 197, § 3 (two-thirds).

41. McCray v. Junction Rr. Co., 9 Ind. 358 (1857); Patterson v. Shattuck Arizona Copper Co., 186 Minn. 611, 244 N. W. 281 (1932); Lauman v. Lebanon Valley Rr. Co., 30 Pa. 42 (1858); cf. Black v. Delaware & Raritan Canal Co., 24 N. J. Eq. 455 (Ch. 1873). Nor will the clause in the merger and consolidation statute, providing that in the absence of an express objection, a stockholder will be deemed to have assented to the transaction, having the effect of making such stockholder a stockholder in the surviving or consolidated corporation against his will. Rivers v. McIntire, 160 S. C. 462, 158 S. E. 816 (1931); Rivers v. Stevenson, 169 S. C. 422, 169 S. E. 135 (1933).

42. Norton v. Union Traction Co., 183 Ind. 666 110 N. E. 113 (1915); Colgate v. U. S. Leather Co., 73 N. J. Eq. 72, 67 Atl. 657 (Ch. 1907); see Jones v. Missouri-Edison Elec. Co., 144 Fed. 765, 770 (C. C. A. 8th, 1906). It also seems that a reserved power by the legislature to alter or amend corporate characters will be available to permit a merger or consolidation, though no express power existed at the time the stockholders subscribed. Market St. Ry. Co. v. Hellman, 109 Cal. 571, 42 Pac. 225 (1895); Bingham v. Savings Investment & Trust Co., 101 N. J. Eq. 413, 138 Atl. 659 (1927); Winfree v. Riverside Cotton Mills, 113 Va. 717, 75 S. E. 309 (1912). However, some courts have held this reservation of power insufficient to authorize so radical a change in the corporate enterprise. Botts v. Simpsonville & B. C. Turnpike Road Co., 88 Ky. 54, 10 S. W. 134 (1888); Kenosha, Rockford & Rock Island Rr. Co. v. Marsh, 17 Wis. 13 (1863).

43. E. g. COLO. COMP. STAT. (1921) § 2287 (three-fourths); FLA. COMP. GEN. LAWS ANN. (1927) § 6562 (majority); MICH. COMP. LAWS (Mason Supp. 1933) § 10135-52 (two-thirds); MINN. STAT. (Mason, 1927) § 7457-12 (nine-tenths); MO. STAT. ANN. (Vernon, 1932) § 4954 (three-fifths). As a general rule the required proportion must be of the total capital stock outstanding, though the Virginia statute seems to require only that there be approval by a majority of the votes cast. VA. CODE (Michie, 1930) § 3822(b). In some states if the articles of incorporation provide for approval by a lesser proportion than that named in the statute, the statute provides that the former shall prevail. MINN. STAT. (Mason, 1927) § 7457-12; OHIO GEN. CODE (Page, Supp. 1934) § 8623-67.

44. E. g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.64; N. Y. STOCK CORP. LAW (1923) § 86 (8) (b); WASH. REV. STAT. ANN. (Remington, 1935) § 3803-43 (2);

so fundamental a change that all the stock, preferred, common, or otherwise, is given the right to vote.[45] Where there are classes of stock, all of which are entitled to vote, the vote is taken by classes and the required proportion in each class must approve.[46]

After the approval by the stockholders of the constituent corporations, it is usually required that articles of merger or consolidation be filed with the secretary of state in the state or states of which the constituents had been corporations. A not infrequent provision today, particularly in respect to public utility and railroad companies, is to make the approval of some state regulatory board or commission a condition precedent to the filing of these articles.[47] More recently the federal government has imposed similar restrictions on corporations engaged in interstate commerce.[48] Once the articles have been filed, the merger or consolidation is regarded as complete and it is effective forthwith.[49]

The Rights and Remedies of Dissenting Stockholders. Two courses of action are open to the dissenting stockholder who does not wish to become a stockholder in the surviving or consolidated corporation. First, if the merger or consolidation has not yet become effective, he may seek by injunction to prevent it from ever taking effect, or if it has been completed, he may ask equity to set it aside. Secondly, he may sue for the value of his interest in the constituent corporation represented by his shares of stock.[50]

To have a standing in equity to enjoin a merger or consolidation, the dissenting stockholder must usually have been a stockholder at the time the merger or consolidation agreement was submitted to the stockholders of his

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UNIFORM BUSINESS CORP. ACT § 44. In many statutes, simply the term "stockholders" is used, without any express designation one way or the other. E. g. DEL. REV. CODE (1915) § 1973, as amended Del. Laws 1929, c. 135, § 18; VA. CODE (Michie, 1930) § 3822 (b).

45. CAL. CIV. CODE (Deering, 1931) § 361 (3). Some merger and consolidation statutes require that notice be given to all stockholders, though only the voting stock is entitled to vote to approve or reject the agreement. FLA. COMP. GEN. LAWS ANN. (1927) § 6562; TENN. CODE ANN. (Williams, 1934) § 3750.

46. E. g. CAL. CIV. CODE (Deering, 1931) § 361 (3); LA. GEN. STAT. (Dart 1932) § 1128; PA. STAT. ANN. (Purdon, 1934) tit. 15, § 2852-902 (c).

47. E. g. OHIO GEN. CODE (Page, Supp. 1934) § 710-86 (banks); PA. STAT. ANN. (Purdon, 1931) tit. 66, § 182 (c) (public service corporations). However, in Virginia the approval of the corporation commission is essential to the merger or consolidation of any corporations. VA. CODE (Michie, 1930) § 3822 (b).

48. E. g. P. L. No. 333, 74th Cong., 1st Sess. (1935) § 203 (a) (public utilities). For problems arising under the Transportation Act of 1920, requiring the Interstate Commerce Commission to promulgate the plan of consolidation, see Snyder v. New York, Chicago, and St. Louis Rr. Co., 118 Ohio St. 72, 160 N. E. 615 (1928).

49. E. g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.67; PA. STAT. ANN. (Purdon, 1934) tit. 15, § 2852-906.

50. See *infra* p. 120. One other possible situation may arise where an individual who has been a stockholder in a constituent, through no fault of his own, fails to obtain stock in the surviving or consolidated corporation. In such a case he may compel the surviving or consolidated corporation to transfer stock to him. Cf. Seymour v. Mechanics & Metals Nat. Bank, 199 App. Div. 707, 192 N. Y. Supp. 588 (1st Dep't., 1922), where in 1922 the complainant was held entitled to his shares, although the first of several mergers and consolidations took place in 1855.

constituent for their approval,[51] he must not have voted in favor of the agreement,[52] and his application for relief must be timely. The latter is of special importance, for in their dislike of suits by minority stockholders, the courts often seize upon any indication of laches as a ground for denying injunctive relief.[53] If it appears to the court that the bill is a mere "strike suit" by which the dissenting stockholder is trying to blackmail the constituent into settling his claim, it is likely that he will be relegated to his action for the value of his shares.[54] If the dissenting stockholder is seeking only to enjoin or set aside the merger or consolidation, his bill is sufficient if it is directed against his constituent alone, but if the complainant asks for relief in the alternative, that is, an injunction or if that be denied, the value of his shares, the surviving or consolidated corporation must be joined as a party defendant.[55] The action is regarded as one by the dissenting stockholder in his own right, and it seems to be unnecessary to allege or prove a demand upon the officers of the corporation to prevent the merger or consolidation, since under the circumstances this would be virtually a useless procedure.[56] Finally, to complete his standing in equity, the complainant must show that his remedy

51. Norton v. Union Traction Co., 183 Ind. 666, 110 N. E. 113 (1915); cf. Cooper v. Central Alloy Steel Corp., 43 Ohio App. 455, 183 N. E. 439 (1931). *Contra:* Pollitz v. Gould, 202 N. Y. 11, 94 N. E. 1088 (1911).

52. Carr v. Rochester Tumbler Co., 207 Pa. 392, 56 Atl. 945 (1904). But where at the time of the stockholders' meeting, the complainant did not know of fraud on the part of the promoters of the transaction, and had no means of knowing it, he may later seek to enjoin the merger or consolidation. Alabama Fidelity Mortgage & Bond. Co. v. Dubberly, 198 Ala. 545, 73 So. 911 (1917); cf. Cole v. Nat. Cash Credit Ass'n., 18 Del. Ch. 47, 156 Atl. 183 (1931).

53. Rankin v. Interstate Equities Corp., 180 Atl. 541 (Del. Ch. 1935); Bradford v. Frankfort, St. Louis & Toledo Rr. Co., 142 Ind. 383, 40 N. E. 741 (1895); Dana v. American Tobacco Co., 72 N. J. Eq. 44, 65 Atl. 730 (Ch. 1907); cf. Cole v. Birmingham Union Ry. Co., 143 Ala. 427, 39 So. 403 (1905); Auten v. St. Louis, Iron Mt. & Southern Ry. Co., 110 Ark. 24, 160 S. W. 873 (1913); Blatchford v. Ross, 54 Barb. 42 (N. Y. Sup. Ct. 1869).

54. See Windhurst v. Central Leather Co., 101 N. J. Eq. 543, 551, 138 Atl. 772, 775 (Ch. 1927); cf. Comment (1934) 34 COL. L. REV. 1308.

55. General Investment Co. v. Lake Shore & M. S. Ry. Co., 260 U. S. 261 (1922); Jones v. Missouri-Edison Elec. Co., 144 Fed. 765 (C. C. A. 8th, 1906); Bonner v. Terre Haute & I. Rr. Co., 151 Fed. 985 (C. C. A. 7th, 1907); Luehrmann v. Lincoln Trust & Title Co., 192 S. W. 1026 (Mo. 1917); cf. Alabama Fidelity Mortgage & Bond Co. v. Dubberly, 198 Ala. 545, 73 So. 911 (1917). A court of equity will frequently grant the complainant the value of his shares in lieu of enjoining or setting aside the transaction. This is particularly true as to the latter, since interminable confusion might ensue. Dana v. American Tobacco Co., 72 N. J. Eq. 44, 65 Atl. 730 (Ch. 1907), aff'd 73 N. J. Eq. 736, 69 Atl. 223 (Ct. Errors and App. 1908). Another influential factor in deciding what relief to give may be the size of the complainant's interest. This is especially true at the present time when the tendency of the courts seems to be to prevent dictation of corporate policies by minority interests. MacFarlane v. North American Cement Corp., 16 Del. Ch. 172, 157 Atl. 396 (Ch. 1928); Paterson v. Shattuck-Arizona Copper Co., 186 Minn. 611, 244 N. W. 281 (1932); cf. Tanner v. Lindell Ry. Co., 180 Mo. 1, 79 S. W. 155 (1904).

56. General Investment Co. v. Lake Shore & M. S. Rr. Co., 250 Fed. 160 (C. C. A. 6th, 1918).

at law is inadequate,[57] and establish some ground of equitable jurisdiction. Some such ground will have been established if the dissenting stockholder can prove that the merger or consolidation was illegally brought about, or that the transaction was fraudulent and subjected him to unfair treatment.[58]

As a general rule, lack of statutory authority to merge or consolidate, is a ground of illegality which is sufficient under any circumstances to enable a dissenting stockholder to obtain an injunction.[59] Likewise, ample grounds to invoke equitable interference seem to be present where the procedure as outlined in the merger or consolidation statute has not been complied with, such as the failure to obtain the consent of the requisite number of stockholders,[60] or where the transaction violates some state or federal statute, such as by a provision in the agreement authorizing an issue of stock in excess of the true value of the assets of the surviving or consolidated corporation.[61] Another objection on the grounds of illegality, somewhat limited by the difficulties of proof, would seem to be the fact that, although the forms of the statute have been complied with, there has been no substantial compliance with the purposes of the statute or with the procedure outlined therein.[62] While these grounds of objection are important, today they constitute the exceptional grounds for invoking equitable interference. The bulk of the cases where

57. General Investment Co. v. Lake Shore & M. S. Rr. Co., 250 Fed. 160 (C. C. A. 6th, 1918); cf. Clarke v. Gold Dust Corp., 6 F. Supp. 313 (D. N. J. 1934).

58. MacFarlane v. North American Cement Corp., 16 Del. Ch. 172, 157 Atl. 396 (Ch. 1928); Rankin v. Interstate Equities Corp., 180 Atl. 541 (Del. Ch. 1935); Raff v. Darrow, 184 Ind. 353, 111 N. E. 189 (1916); Morse v. Equitable Life Assurance Society, 124 App. Div. 235, 108 N. Y. Supp. 986 (1st Dep't 1908); cf. Gamble v. Queens County Water Co., 123 N. Y. 91, 25 N. E. 201 (1890). But cf. Terhune v. Midland Rr. Co., 38 N. J. Eq. 423 (Ch. 1884) semble.

59. Riker & Son Co. v. United Drug Co., 79 N. J. Eq. 580, 82 Atl. 930 (Ct. Errors and App. 1912); Knapp v. Supreme Commandery, United Order of the Golden Cross of the World, 121 Tenn. 212, 118 S. W. 390 (1908).

60. Cf. Agoodash Achim of Ithaca v. Temple Beth-El, 147 Misc. 405, 263 N. Y. Supp. 81 (Sup. Ct. 1933); Tuttle v. Michigan Air Line Rr. Co., 35 Mich. 247 (1877).

61. Taylor v. Citizens' Oil Co., 182 Ky. 350, 206 S. W. 644 (1918). The line of cases holding that the state alone can question the validity of a merger or consolidation on grounds of such illegality are usually situations where it is alleged that the combination will violate a statutory or constitutional prohibition against the merger or consolidation of competing or parallel roads. Cf. Warrener v. Kankakee County, 29 Fed. Cas. No. 17,205, at 293 (C. C. N. D. Ill. 1875); Chicago & Western Ind. Rr. Co. v. Heidenreich, 254 Ill. 231, 98 N. E. 567 (1912); Bell v. Pennsylvania, S. & N. E. Rr., 10 Atl. 741 (N. J. Ch. 1887). But cf. Pearsall v. Great Northern Rr. Co., 161 U. S. 646 (1896).

62. Cf. Small v. Sullivan, 245 N. Y. 343, 157 N. E. 261 (1927), in which directors of a corporation were held liable where they had used the consolidation device solely as a means to create a surplus from which to declare dividends; Compton v. Wabash, St. Louis & Pacific Ry. Co., 45 Ohio St. 592, 619, 16 N. E. 110, 119 (1888), where the court said that "the object of the legislature in authorizing the consolidation of railway companies was . . not to enable the new company to obtain credit by impairing the security of existing creditors . . . but to enable existing companies to unite, and form a continuous line." See Goodbar, *The Youngstown Litigation* (1931) 11 B. U. L. Rev. 376. But cf. Wick v. Youngstown Sheet & Tube Co., 46 Ohio App. 253, 188 N. E. 514 (1932), error dismissed, 127 Ohio St. 379, 189 N. E. 4 (1933).

injunctions are sought are based on allegations of fraud on the part of the majority stockholders and promoters of the transaction, and of unfairness to the dissenting stockholder in the plan for the exchange of shares.

Fraud and unfairness are normally found together, and where they result in a substantial detriment[63] to the dissenting stockholder, equity will generally grant injunctive relief. Considered apart from the facts of a given case, generalizations as to fraud and unfairness are of little utility. However, generalizations may be made to the extent that the facts that the constituent corporations have common directors, or that the majority stockholders in each constituent are the same, are in themselves insufficient to establish any fraud or unfairness in the transaction.[64] While such facts may induce a court of equity to scrutinize the transaction more closely, the burden remains on the dissenting stockholder to prove other facts pointing to fraud and unfairness.[65]

But while generalizations as to fraud and unfairness are difficult, there are three frequently recurring factual situations, which, with slight variations, appear to embrace virtually every case in which fraud and unfairness have been alleged. The first of these situations is where by the terms of the plan for the exchange of shares, the stockholders of one or more of the constituents are given preferential treatment over the stockholders of the constituent in which the complainant owns stock. As a result, the complainant is receiving stock which represents a proportional interest in the surviving or consolidated corporation less than that which his shares in his constituent represented. Thus, his interest is being diluted both in respect to the value of his shares and to the amount of his control over the corporate affairs. When this is the substance of a complainant's allegation, the court of equity must necessarily investigate the financial structures of the constituent corporations in order to compare the value of the contribution of one constituent with that of the others. In making such valuations courts of equity usually seize upon the two elements of net assets and earning power. If upon being tested by these two elements, it appears to the court that there has been a substantial diminution of the dissenting stockholder's interest, adequate basis for the issuance of an injunction ought to exist even in the absence of a showing of any fraudulent purpose on the part of the majority stockholders.[66] Often, however, an

63. The term "substantial" clearly seems to beg the question. But since it is solely a question of degree, apart from a given set of circumstances, it is impossble to tell what will be regarded as a substantial detriment.

64. Homer v. Crown Cork & Seal Co., 155 Md. 66, 141 Atl. 425 (1928); Bingham v. Savings Investment & Trust Co., 101 N. J. Eq. 413, 138 Atl. 659 (Ch. 1927); Armstrong v. Hayden, 126 Misc. 786, 214 N. Y. Supp. 747 (Sup. Ct. 1926); see Voight v. Remick, 260 Mich. 198, 244 N. W. 446, 450 (1932).

65. Allied Chemical & Dye Corp. v. Steel & Tube Co., 14 Del. Ch. 1, 120 Atl. 486 (Ch. 1923); Homer v. Crown Cork & Seal Co., 155 Md. 66, 141 Atl. 425 (1928).

66. Colby v. Equitable Title & Trust Co., 124 App. Div. 262, 108 N. Y. Supp. 978 (1st Dep't 1908); Langan v. Francklyn, 20 N. Y. Supp. 404 (N. Y. City Cts. 1892); cf. Allied Chemical & Dye Corp. v. Steel & Tube Co., 14 Del. Ch. 1, 120 Atl. 486 (Ch. 1923); Pridmore v. Whiting Corp., 268 Ill. App. 592 (1932); Cooper v. Central Alloy Steel Corp., 43 Ohio App. 455, 183 N. E. 439 (1931). In respect to unfairness standing alone, the courts will often say, as did the court in Allied Chemical & Dye Corp. v. Steel & Tube Co., at 19, 494,

apparent unfairness because of a considerable disparity in the net asset contributions of constituents will be balanced by an inverse disparity in their respective earning powers.[67] Likewise, what on the surface may appear to be grossly unfair plans of exchange may be explained by the presence of overvalued assets, insufficient reserves for depreciation, or failure to make adequate allowance for bad debts.[68] The possibility of objections on the basis of this type of unfairness can be lessened greatly by taking the precaution of having an accurate appraisal and audit at the time the agreement of merger or consolidation is drawn up.

The second factual situation in which a court of equity may find fraud and unfairness in a merger or consolidation is where, as a result of the plan of exchange of shares, one class of stockholders within a constituent corporation is given preferential treatment over the class of which the complainant is a member. His complaint is not that all the stockholders of his constituent are being treated unfairly, but only that the stockholders of his class are being discriminated against, so that after the transaction his shares will not represent the same proportional interest as they did formerly, neither in respect to value nor to control.[69] This situation normally arises where the common stockholders, by virtue of statute, are the only group entitled to approve or reject the agreement of merger or consolidation, and by this means have made the distribution of shares more beneficial to themselves than to the preferred or some other class of stockholders. If the court is satisfied that the dilution of the complainant's interest is substantial, adequate grounds for the issuance of an injunction exist, especially since some element of fraud is invariably present.[70]

Somewhat distinct from the two foregoing situations is the third where the agreement of merger or consolidation calls for the surrender or diminution of some special right. Examples of this type of unfairness may differ widely, but usually arise in connection with preferred stock. Thus, where a stockholder has a high-grade security such as stock in a corporation, the properties

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that "when the price . . . is so far below what is found to be a fair one that it can be explained only on the theory of fraud, or a reckless indifference to the rights of others interested, it would seem that it should not be allowed to stand." See also Matter of American Telegraph & Cable Co., 139 Misc. 625, 248 N. Y. Supp. 98 (Sup. Ct. 1931). But see Homer v. Crown Cork & Seal Co., 155 Md. 66, 83, 141 Atl. 425, 433 (1928).

67. Colby v. Equitable Title & Trust Co., 124 App. Div. 262, 108 N. Y. Supp. 978 (1st Dep't, 1908).

68. Cole v. Nat. Cash, Credit Ass'n, 18 Del. Ch. 47, 156 Atl. 183 (Ch. 1931).

69. In this connection, assuming the complainant is a preferred stockholder and that the actual value of his preferred stock is less than the liquidation value provided for in the preferred stock contract, it would seem that the complainant is not entitled to have stock of the surviving or consolidated corporation issued to him in proportion to that liquidation value, but only in proportion to the actual value. This result is consistent with the basic theory of merger and consolidation that such a transaction is not a dissolution of the enterprise, but a method of continuing the enterprise in a larger entity.

70. Jones v. Missouri-Edison Elec. Co., 144 Fed. 765 (C. C. A. 8th, 1906); Eagleson v. Pacific Timber Co., 270 Fed. 1008 (D. Del. 1920); MacFarlane v. North American Cement Corp., 16 Del. Ch. 172, 157 Atl. 396 (Ch. 1928); cf. Elyton Land Co. v. Dowdell, 113 Ala. 177, 20 So. 981 (1896).

of which are under long term leases to another corporation, a plan of merger or consolidation calling for the exchange of this stock for ordinary stock of the surviving or consolidated corporation may be sufficiently detrimental to the dissenting stockholder to warrant issuance of an injunction.[71] Similarly, equity may find adequate grounds to enjoin where the preferred stock to be issued in the exchange is callable within a shorter time than the old preferred stock; where the new preferred stock is callable at the option of the surviving or consolidated corporation; where the preferred stockholders were about to acquire voting rights because of a default in preferred dividends, and the merger or consolidation will prevent this from occurring; or where arrears of dividends exist which the merger or consolidation will wipe out.[72] However, in cases where there is no prospect that the constituent will ever pay off arrears in preferred dividends, the propriety of enjoining the merger or consolidation on the latter ground may well be questioned.[73] Although fraud as well as unfairness is usually present in this third situation, the latter alone should be sufficient if the complainant proves a substantial injury to his interest.

The judicial decisions on all three of these factual situations are not clear as to whether, in the absence of any fraud, substantial unfairness alone is a sufficient basis for equitable intervention. To protect adequately the interests of minority stockholders, such unfairness alone should be sufficient. Indeed, it would seem very reasonable as a means of assuring fair treatment to all stockholders to insert in the merger and consolidation statutes a requirement that before articles of merger or consolidation may be filed with the secretary of state, the fairness of the transaction be confirmed by some judicial or administrative body.[74] In corporate reorganizations the fairness of the reorganization plan is judicially determined, and like considerations exist to

71. Boyd v. N. Y. & H. Rr. Co., 220 Fed. 174 (S. D. N. Y. 1915); Outwater v. Public Service Corp. of N. J., 103 N. J. Eq. 461, 143 Atl. 729 (Ch. 1928), aff'd, without opinion, 104 N. J. Eq. 490, 146 Atl. 916 (Ct. Errors and App. 1929); cf. Simon Borg & Co. v. New Orleans City Rr. Co., 244 Fed. 617 (E. D. La. 1917).

72. Colgate v. U. S. Leather Co., 73 N. J. Eq. 72, 67 Atl. 657 (Ch. 1907); Outwater v. Public Service Corp. of N. J., 103 N. J. Eq. 461, 143 Atl. 729 (Ch. 1928), aff'd without opinion, 104 N. J. Eq. 490, 146 Atl. 916 (Ct. Errors and App. 1929); see Cole v. Nat. Cash Credit Ass'n, 18 Del. Ch. 47, 56, 156 Atl. 183, 187 (Ch. 1931); cf. Windhurst v. Central Leather Co., 101 N. J. Eq. 543, 138 Atl. 772 (Ch. 1927); Lonsdale Securities Corp. v. International Mercantile Marine Co., 101 N. J. Eq. 554, 139 Atl. 50 (Ch. 1927). For the factual background of Colgate v. U. S. Leather Co., see DEWING, CORPORATE PROMOTIONS AND REORGANIZATIONS (1914) c. 2.

73. Thus, as a result of merger or consolidation the surviving or consolidated corporation may be able to pay dividends on its preferred stock, while to force the constituent corporation to continue without the financial aid to be received from the other constituents may lead to bankruptcy. See Bisbee, *supra* note 15, at 379.

74. In practical effect some such requirement may exist in some states in respect to certain classes of corporations such as public utilities and banks. Thus, in American Malt Corp. v. Board of Public Utility Comm'rs, 86 N. J. L. 668, 92 Atl. 362 (Ct. Errors and App. 1914), it was held that the Board of Public Utility Commissioners could withhold their approval to a merger on the ground that it was unfair to the preferred stockholders. See also OHIO GEN. CODE (Page, Supp. 1934) §§ 710-86. Where the corporations participating in the transaction are of different states, such a requirement might create certain juris-

justify a similar procedure in connection with mergers and consolidations.[75] Thus, minority stockholders would be protected, and once the fairness of the transaction had been confirmed, the merger or consolidation could proceed free from any attack. Should this be regarded as too drastic an extension of the reorganization procedure, at least the right should be granted to any stockholder to have the fairness of the plan judicially determined, irrespective of any element of fraud on the part of the management or majority stockholders.[76]

As mentioned previously, should a stockholder desire neither to become a stockholder in the surviving or consolidated corporation, nor to prevent the merger or consolidation from taking place, there are invariably one and occasionally two methods by which he may obtain the value of his shares in his constituent corporation from the surviving or consolidated corporation. The normal procedure is to have his shares appraised under the appraisal statutes which form a part of practically every merger or consolidation statute.[77] In a few states these appraisal statutes originated almost as early as the first special acts authorizing merger or consolidation, and their history and procedure form a complete topic of discussion in themselves.[78] Suffice it to mention here that this form of relief can be invoked only by a strict compliance with the procedure outlined in the appraisal statute of the particular jurisdiction of which the constituent was a corporation.[79]

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dictional problems, especially in the case of a consolidation. To make the requirement workable in this respect, it would first seem highly desirable for all statutes to require that the consolidated corporation become a corporation of a state of one of the constituents, thus eliminating the difficulties created by the "interstate corporations." Then the judicial or administrative body of the state of the consolidated corporation would be the only tribunal to pass on the fairness of the plan, and its decision would be binding in all states. Secondly, the statute should make the requirement applicable only where the statutes of the states of the other constituents contain similar requirements. If such reciprocal provisions were not present, there would always be the possibility that a plan approved as fair by the judicial or administrative body of one state, might be found to be unfair in a dissenting stockholder's suit in a state where there was no requirement of having the fairness passed upon as a condition precedent.

75. Cf. Eagleson v. Pacific Timber Co., 270 Fed. 1008 (D. Del. 1920).

76. That possibly a stockholder would have such a right by statute in Michigan, see MICH. COMP. LAWS (Mason, Supp. 1933) § 10135-4 (3).

77. N. J. COMP. STAT. (Supp. 1924) tit. 47, § 108a; MICH. COMP. LAWS (Mason, Supp. 1933) § 10135-54.

78. Complete discussions of the appraisal statutes and their procedure are to be found in Lattin, *Remedies of Dissenting Stockholders under Appraisal Statutes* (1931) 45 HARV. L. REV. 233; Robinson, *Dissenting Shareholders: Their Right to Dividends and the Valuation of Their Shares* (1932) 32 COL. L. REV. 60; Weiner, *Payment of Dissenting Stockholders* (1927) 27 COL. L. REV. 547; see Ballantine, *Questions of Policy in Drafting a Modern Corporation Law* (1931) 19 CALIF. L. REV. 465, 482; Comment (1932) 41 YALE L. J. 577.

79. Typical requirements are that, first the dissenting stockholder must have voted against the merger or consolidation, or if not entitled to vote, he must have objected in writing prior to the taking of the vote. Secondly, within twenty days after the agreement of merger or consolidation has been filed with the secretary of state, he must make a written demand on the surviving or consolidated corporation for payment of his stock. If the latter does not make payment, within thirty days after the making of his demand

A second means still available in some states to the dissenting stockholder is by a direct action at law for the conversion of his shares,[80] or more usually in equity, upon the basis that the complainant's property is being taken from him against his consent.[81] Originally this form of relief was granted because a stockholder of a constituent could not be compelled to become a stockholder in the surviving or consolidated corporation, and, in the absence of an appraisal statute, some means of compensating him for his shares was necessary.[82] At the present time, where the proportion of stockholder approval required by the statute has been obtained, the decisions are not agreed as to whether this form of relief exists concurrently with that of the appraisal statutes. In some states the appraisal statutes, while not a bar to injunctive relief,[83] are regarded as the exclusive remedy in a suit for the value of stock;[84] in others a suit in equity for the "actual" value of the stock remains available.[85] This latter relief may prove very valuable where the dissenting stockholder cannot invoke the aid of the appraisal statute by reason of his failure to comply with its conditions precedent. If in a given jurisdiction a dissenting stockholder would be assured a judicial review of the fairness of the plan of merger or consolidation, either by virtue of case law or by some statutory provision,[86] it would seem desirable as a matter of policy to make the appraisal remedy exclusive in any action for the value of stock. The surviving or consolidated corporation is entitled to know the extent of dissenting stockholders' claims which it must meet within a reasonable time after the merger or consolidation has been effected, and moreover, the appraisal pro-

for payment, the dissenting stockholder must petition the county court of the county in which the principal office of the surviving or consolidated is located to appoint three appraisers to appraise the value of his stock. The award of the appraisers, if not opposed within ten days after it has been filed in court, becomes final and conclusive. If opposed, the award will be reviewed by the court, in the same manner as it reviews awards made pursuant to eminent domain proceedings. N. C. CODE ANN. (Michie, 1931) § 1224(c). The requirements of appraisal statutes are discussed in Stephenson v. Commonwealth & Southern Corp., 18 Del. Ch. 91, 156 Atl. 215 (Ch. 1931). The surviving or consolidated corporation is the true defendant, but the inclusion of a constituent as a defendant is usually not fatal. Southern Power Co. v. Cella, 143 Atl. 755 (N. J. Sup. Ct. 1928); Budd v. Logan Bldg. & Loan Ass'n, 112 Pa. Super. 65, 170 Atl. 325 (1934). The expenses of the appraisal proceedings are imposed ordinarily upon the surviving or consolidated corporation. Cf. Manning v. Brandon Corp., 161 S. E. 405 (S. C. 1931).

80. Nice Ball Bearing Co. v. Mortgage Bldg. & Loan Ass'n, 310 Pa. 560, 166 Atl. 239 (1933).

81. Barnett v. Philadelphia Market Co., 218 Pa. 649, 67 Atl. 912 (1907).

82. Lauman v. Lebanon Valley Rr. Co., 30 Pa. 42 (1858).

83. But see CAL. CIV. CODE (Deering, 1931) § 369.

84. In re Interborough Consolidated Corp., 277 Fed. 455 (S. D. N. Y. 1921); Spencer v. Seaboard Air Line Ry. Co., 137 N. C. 107, 49 S. E. 96 (1904).

85. The remedy of the appraisal statute is regarded as a remedy additional to, but not supplanting, the equitable remedy. Barnett v. Philadelphia Market Co., 218 Pa. 649, 67 Atl. 912 (1907); cf. Nice Ball Bearing Co. v. Mortgage Bldg. & Loan Ass'n, 310 Pa. 560, 166 Atl. 239 (1933).

86. In New Jersey, at least, it seems that a dissenting stockholder is usually able to have the fairness of the plan reviewed, even in the absence of any element of fraud.

cedure seems to afford the dissenting stockholder a more summary and satisfactory method of relief than that of an equitable action, which in some states at least, might involve a considerable length of time. However, since at the present time the dissenting stockholder's right to a judicial review of the fairness of the plan is so uncertain, it seems better not to make the appraisal remedy exclusive, and thereby deprive him of what protection the equitable action may afford.

One unusual proceeding for the value of stock is an action by a preferred stockholder for the specific performance of his preferred stock contract which usually entitles him to the par value of his shares upon the dissolution of the corporation. Where the proportional interest represented by the preferred shares is less in value than their par value, in at least one state it has been held that the merger or consolidation amounted to a dissolution of the constituent corporation, and that consequently the dissenting stockholder was entitled to receive the par value of his preferred stock.[87] However, elsewhere this result has been expressly denied.[88] The correct solution would seem to depend on whether the legislature in stating that the constituent corporations are dissolved upon merger or consolidation, except for the surviving corporation in the case of merger, intended "dissolved" to mean a cessation of their corporate existences, to which the preferred stock contract has reference, or to mean merely a technical dissolution within the purview of the dissolution statute.[89]

The Rights and Remedies of Creditors. It is universally agreed that upon merger or consolidation, the surviving or consolidated corporation is always liable for the debts, liabilities, and duties of each of its constituents. Generally the basis of this liability is an express statutory imposition,[90] and express assumption thereof in the agreement of merger or consolidation, [91] or both.[92]

87. Petry v. Harwood Elec. Co., 280 Pa. 142, 124 Atl. 302 (1924).

88. Windhurst v. Central Leather Co., 101 N. J. Eq. 543, 138 Atl. 772 (Ch. 1927).

89. See Simms, *An Application of the Doctrine that Consolidation Effects Dissolution* (1929) 15 VA. L. REV. 757; Comment (1932) 45 HARV. L. REV. 1401; Comment (1932) 30 MICH. L. REV. 1074.

90. E. g. CAL. CIV. CODE (Deering, 1931) § 361 (7); DEL. REV. CODE (1915) § 1974, as amended by Act of April 18, 1935; ILL. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.69 (e); N. Y. STOCK CORP. LAW (1923) §§ 85 (2), 90; PA. STAT. ANN. (Purdon, 1934) tit. 15, § 2852-907. For an early statute imposing such liability, see Md. Laws 1838, c. 30, § 4. See Greene v. Woodland Ave. & W. S. St. Rr. Co., 62 Ohio St. 67, 79, 56 N. E. 642, 646 (1900); Camden Safe-Deposit & Trust Co. v. Burlington Carpet Co., 33 Atl. 479, 480 (N. J. Ch. 1895). Under the New York merger statute, prior to 1923, the surviving (possessor) corporation was not liable for the debts, liabilities, and obligations of the corporations merged into it. The existences of the latter were preserved for the purposes of suit. Irvine v. N. Y. Edison Co., 207 N. Y. 425, 101 N. E. 358 (1913); Syracuse Lighting Co. v. Maryland Casualty Co., 226 N. Y. 25, 122 N. E. 723 (1919); see Ducasse v. American Yellow Taxi Operators, Inc., 224 App. Div. 516, 518, 231 N. Y. Supp. 51, 54 (2d Dep't, 1928).

91. State v. American Bonding & Casualty Co., 213 Iowa 200, 238 N. W. 726 (1931); American Bank v. Port Orford Cedar Products Co., 140 Ore. 138, 12 P. (2d) 1014 (1932); cf. Fears v. State Bank of Naylor, 224 Mo. App. 632, 31 S. W. (2d) 94 (1930). See also 15 FLETCHER, op. cit. *supra* note 3, §§ 7109-7116.

92. It is not unusual for the surviving or consolidated corporation to assume the debts,

In the absence of such bases of liability, the surviving or consolidated corporation is nevertheless liable, either fully as if it had incurred the liability in question itself,[93] or partially to the extent of the assets received from the constituent,[94] upon either the theory of an implied assumption of liability by the surviving or consolidated corporation, or upon that of a fraudulent conveyance.[95] Where, however, the constituent was under a duty to perform a positive act, such as use a product exclusively in its business, the surviving or consolidated corporation will be subject to that duty only to the extent that the constituent was subject to it at the time of the merger or consolidation; that duty will not extend to the entire business of the surviving or consolidated corporation.[96] Where bonds or other obligations have been issued by a constituent with a privilege in the holder of converting them into stock at his option, it usually is held that the conversion privilege is extinguished by the

liabilities, and obligations of its constituents, even though a statute also expressly imposes such liability.

93. Atlantic & B. Ry. Co. v. Johnson, 127 Ga. 392, 56 S. E. 482 (1907); see Morrison v. American Snuff Co., 89 Am. St. Rep. 604, 637 (1903). However, there has been no actual case where the liability of the surviving or consolidated corporation has been held to be greater than the value of the assets received. See McKee v. Standard Minerals Corp., 18 Del. Ch. 97, 101, 156 Atl. 193, 195 (1931). But see statement by the same chancellor in Cole v. Nat. Credit Ass'n, 18 Del. Ch. 47, 52, 156 Atl. 183, 185 (1931), a case decided in the same month as the preceding case.

94. United States Capsule Co. v. Isaacs, 23 Ind. App. 533, 55 N. E. 832 (1899); Berry v. Kansas City, Ft. S. & M. Rr. Co., 52 Kan. 774, 36 Pac. 724 (1894); Morrison v. American Snuff Co., 79 Miss. 330, 30 So. 723 (1901), and note thereto in 89 Am. St. Rep. 604, 638 (1903).

95. These theories are discussed in GLENN, CREDITORS' RIGHTS AND REMEDIES (1915) § 126. Typical cases utilizing the theory of an implied assumption include Cox v. Baltimore & O. S. W. Rr. Co., 180 Ind. 495, 103 N. E. 337 (1913); Berry v. Kansas City, F. S. & M. Rr. Co., 52 Kan. 774, 36 Pac. 724 (1894); see Gueringer v. St. Louis, B. and M. Ry. Co., 23 S. W. (2d) 704, 706 (Tex. Comm. of App. 1930); cf. Morlock v. Mt. Forest Farms of America, 269 Mich. 549, 257 N. W. 880 (1934). Cases proceeding on the theory of fraudulent conveyance are Jackson v. Knights and Ladies of the Orient, 101 Kan. 383, 466, 167 Pac. 1046 (1917); Morrison v. American Snuff Co., 79 Miss. 330, 30 So. 723 (1901); cf. Drug, Inc. v. Hunt, 5 W. W. Harr. 339, 168 Atl. 87 (Del. Sup. Ct. 1933), noted in (1933) 82 U. OF PA. L. REV. 172. The question of whether these theories are tenable is rendered academic by the virtually universal imposition of liability on the surviving or consolidated corporation by statute. However, a similar problem arises frequently today in a combination by a sale of entire corporate assets. While here, too, the purchasing corporation often assumes the seller's liabilities, in the absence of such assumption the creditor must proceed on one or the other of the two theories above. See Erhard v. Boone State Bank, 65 F. (2d) 48 (C. C. A. 8th, 1933); West Texas Refining & Dev. Co. v. Comm'r of Int. Rev., 68 F. (2d) 77 (C. C. A. 10th, 1933); Mallory S. S. Co. v. Baker & Holmes Co., 117 Fla. 196, 157 So. 504 (1934); Harlan Public Service Co. v. Eastern Construction Co., 254 Ky. 135, 71 S. W. (2d) 24 (1934); Comment (1930) 44 HARV. L. REV. 260; (1927) 11 MINN. L. REV. 372.

96. Pullman's Palace Car Co. v. Missouri Pac. Rr. Co., 115 U. S. 587 (1885); Ducasse v. American Yellow Taxi Operators, Inc., 224 App. Div. 516, 231 N. Y. Supp. 51 (2d Dep't, 1928).

merger or consolidation, unless some provision therefor is made in the agreement.[97]

Since creditors are fully protected upon merger or consolidation, injunctive relief will be denied to them except under very unusual circumstances.[98] Hence, the principal problem of the creditor is that of proceeding to enforce his claim. This procedure varies in accordance with the statutes of the various states and with the practice within those states. If the creditor commenced his suit prior to the date on which the merger or consolidation became effective, his action is usually saved by express statutory provision, even though the existence of the constituent has not been preserved for the purpose of creditors' suits in general.[99] The normal procedure in such a case is to substitute the surviving or consolidated corporation as defendant in the place of the constituent.[100] If the creditor had not commenced his suit prior to the time the merger or consolidation became effective, he may have a choice of several methods of proceeding. Where the statutes expressly impose liability or where there has been an express assumption, the creditor may proceed at

97. Tagart and Bennett v. Northern Central Ry. Co., 29 Md. 557 (1868); Parkinson v. West End St. Ry. Co., 173 Mass. 446, 53 N. E. 891 (1899). However, the holders of such convertible bonds have been held to be entitled to notice of the transaction so as to be given an opportunity to convert. Rosenkrans v. Lafayette, B. & M. Ry. Co., 18 Fed. 513 (C. C. D. Ind. 1883). See Hills, *Convertible Securities—Legal Aspects and Draftmanship* (1930) 19 CALIF. L. REV. 1, 33-38, in which three Massachusetts cases pointing to a contrary result are distinguished. John Hancock Mut. Life Ins. Co. v. Worcester, Nashua & Rochester Rr. Co., 149 Mass. 214, 21 N. E. 364 (1889); Day v. Worcester, N. & R. Rr. Co., 151 Mass. 302, 23 N. E. 824 (1890); India Mutual Ins. Co. v. Worcester, N. & R. Rr. Co., 25 N. E. 975 (Mass. 1890). See also 1 QUINDRY, BONDS AND BONDHOLDERS (1934) § 11. For a suggestion that the general rule should be different today in at least certain cases, consult Berle, *Convertible Bonds and Stock Purchase Warrants* (1927) 36 YALE L. J. 649, 662. For the situation where the conversion contract has provided for merger or consolidation, see *supra* note 35.

98. Where the security of the creditors of the constituent would be endangered by the merger or consolidation, it would seem that the creditors could enjoin the transaction. Cf. Booth v. Bunce, 33 N. Y. 139 (1865). However, in Cole v. Nat. Cash Credit Ass'n, 18 Del. Ch. 47, 156 Atl. 183, 186 (1931), the court stated that even if the surviving corporation was a less desirable debtor than the constituent because of a poorer quick asset condition, the merger would not be enjoined. Nor would the fact that the debtor constituent was subject to service of process as a foreign corporation doing business within a state, and that the surviving corporation would not be, afford an adequate basis for an injunction. See (1932) 32 COL. L. REV. 143.

99. E. g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.69 (e); N. Y. STOCK CORP. LAW (1923) § 90; OHIO GEN. CODE (Page, Supp. 1934) § 8623-69. Employers' Liability Assur. Corp., Ltd. v. Astoria Mahogany Co., 299 Fed. 579 (C. C. A. 2d, 1924); Wells v. Missouri-Edison Electric Co., 108 Mo. App. 607, 84 S. W. 204 (1904); Baltimore & Susquehanna Rr. Co. v. Musselman, 2 Grant's Cas. 348 (Pa. 1856).

100. Franklin Life Ins. Co. v. Hickson, 197 Ill. 117, 64 N. E. 248 (1902); Wright v. Kansas City, Fort Scott & Memphis Rr. Co., 141 Mo. App. 518, 126 S. W. 517 (1910). But cf. Prouty v. Lake Shore & Michigan Southern Rr. Co., 52 N. Y. 363 (1873). At the present time this right to substitute is expressly provided for in some general merger and consolidation statutes. E. g. IND. STAT. ANN. (Burns, Watson's Supp. 1929) § 4856 (e); N. Y. STOCK CORP. LAW (1923) § 90.

law directly against the surviving or consolidated corporation for judgment and execution.[101] The fact that the surviving or consolidated corporation may be a corporation of a state other than that of the constituent which incurred the creditor's claim ordinarily will not create any difficulties, since it is not uncommon for statutes expressly to provide that the surviving or consolidated corporation must agree to submit to process in the state in which the constituent had been a corporation, and the most recent statutes provide that the secretary of state shall be irrevocably appointed agent to accept such service.[102] Often the same statute which expressly imposes such liability will also preserve the existences of the constituent corporations for the very purpose of creditors' suits.[103] If the statute does not so preserve the constituents, the creditor's sole remedy is against the surviving or consolidated corporation.[104]

Where process may be served upon the surviving or consolidated corporation after the merger or consolidation, there seems to be no reason for preserving the existences of the constituents either from the point of view of unsecured or secured creditors, or on grounds of general policy.[105] The position of the unsecured creditor after merger or consolidation is the same whether the constit-

101. Birmingham Rr. Light & Power Co. v. Enslen, 144 Ala. 343, 39 So. 74 (1905); Mercer-Lincoln Pine Knob Oil Co. v. Payne, 206 Ky. 848, 268 S. W. 584 (1925); Boardman v. Lake Shore & M. S. Rr. Co., 84 N. Y. 157 (1881); Langhorne v. Richmond Ry. Co., 91 Va. 369, 22 S. E. 159 (1895). And even in the absence of either of these two, it has been held that the surviving or consolidated corporation can be sued directly. Warren v. Mobile & Montgomery Rr. Co., 49 Ala. 582 (1873); Indianapolis, C. & L. Rr. Co. v. Jones, 29 Ind. 465 (1868); cf. United States Fidelity & Guaranty Co. v. Citizen's Nat. Bank, 13 F. (2d) 213 (D. N. M. 1924). *Contra:* Shaw v. Norfolk County Rr. Co., 82 Mass. 407 (1860). Consult also 15 FLETCHER, op. cit. *supra* note 3, § 7171. Where some purely equitable remedy such as specific performance is desired, the surviving or consolidated corporation is to be held, of course, directly in equity. Union Pacific Rr. Co. v. McAlpine, 129 U. S. 305 (1888).

102. E. g. DEL. REV. CODE (1915) § 1973, as amended by Act of April 18, 1935; N. Y. STOCK CORP. LAW (1934) § 91 (8). In the very early special acts authorizing merger or consolidation of Massachusetts corporations with those of other states, the special act frequently provided that the surviving or consolidated corporation have one officer in each state upon whom process could be served against such corporation. E. g. Mass. Laws 1827, c. 74, § 2; Mass. Acts & Resolves 1840, c. 50, § 2.

103. E. g. ALA. CODE ANN. (Michie, 1928) § 7042; N. M. STAT. ANN. (Courtright, 1929) § 32-216; VA. CODE (Michie, 1930) § 3823. In such a case the creditor may choose to regard the constituent as his debtor, reduce his claim to judgment, and proceed to execution, in some states by levying on the property of the constituent in the hands of the surviving or consolidated corporation; in others, in equity by resort to a creditor's bill. Matter of Utica Nat. Brewing Co., 154 N. Y. 268, 48 N. E. 521 (1897); Shaw v. Norfolk County Rr. Co., 82 Mass. 407 (1860); cf. Chicago Santa Fe & California Rr. Co. v. Ashling, 160 Ill. 373, 43 N. E. 373 (1895); Shipman Coal Mining & Mfg. Co. v. Pfeiffer, 11 Ind. App. 445, 39 N. E. 291 (1895); Langhorne v. Richmond Ry. Co., 91 Va. 369, 22 S. E. 159 (1895). See GLENN, FRAUDULENT CONVEYANCES (1931), § 288.

104. Bishop v. Brainerd, 28 Conn. 288 (1859); Peoria & R. I. Rr. Co. v. Coal Valley Mining Co., 68 Ill. 489 (1873); Dalmas v. Philipsburg & S. V. Rr. Co., 254 Pa. 9, 98 Atl. 796 (1916).

105. Comment (1932) 30 MICH. L. REV. 1074, 1077.

uents are preserved or not. The merger or consolidation creates no lien in favor of such a creditor upon the property that a constituent contributed to the surviving or consolidated corporation, and although the decisions refer to a "virtual" lien being created in such a case, it has none of the legal consequences of a true lien.[106] Consequently, whether the constituents are preserved or not, the unsecured creditor will be forced to resort for purposes of execution to the general assets of the surviving or consolidated corporation. But in most cases this will afford him a greater mass of assets upon which execution may be levied than was previously the case. Nor is there any advantage to the secured creditor in the preservation of the constituent which created his lien. For whether it is preserved or not, his lien on the property of the constituent continues to be a lien on that same property in the possession of the surviving or consolidated corporation, and will be prior to any liens on such property created by the latter corporation.[107] Finally, the preservation of the constituents' existences is totally inconsistent with the basic conception of merger or consolidation that the constituents are extinguished to be re-created into a larger corporate whole.[108]

Probably the most difficult problem arising in connection with creditors is the effect of merger or consolidation upon clauses in corporate mortgages extending the lien of the mortgage to all after-acquired property. As a general rule the effect of such a clause is nullified by the merger or consolidation if the covenant to extend the lien was that of the constituent only. Consequently, in such a case, the lien neither extends to property contributed by the other constituents, nor to that subsequently acquired by the surviving or consolidated corporation.[109] However, the trust indenture to the trustee for the mortgagees may make express provision that the after-acquired clause shall continue to be effective after merger or consolidation, in which case the lien would extend to

106. Wabash, St. Louis & P. Rr. Co. v. Ham, 114 U. S. 587 (1885); Hervey v. Illinois Midland Ry. Co., 28 Fed. 169 (C. C. S. D. Ill. 1884); McMahan v. Morrison, 16 Ind. 172 (1861); Blake v. Domestic Mfg. Co., 64 N. J. Eq. 480, 38 Atl. 241 (Ch. 1897); cf. Bowden v. Central Bank & Trust Co., 2 F. (2d) 596 (C. C. A. 5th, 1924). But cf. Compton v. Wabash, St. L. & P. Ry. Co., 45 Ohio St. 592, 16 N. E. 110 (1888).

107. Irving Bank-Columbia Trust Co. v. N. Y. Rys. Co., 292 Fed. 429 (S. D. N. Y. 1923), aff'd 292 Fed. 440 (C. C. A. 2d, 1923); Columbia & Montour Electric Co. v. North Branch Transit Co., 258 Pa. 447, 102 Atl. 214 (1917). A state will retain its preferred position as a creditor. Fidelity & Casualty Co. of N. Y. v. American Surety Co. of N. Y., 313 Pa. 145, 169 Atl. 226 (1933).

108. Moreover, once the merger or consolidation has become effective, in seeking to hold the constituent the creditor may frequently be confronted with the practical difficulty of finding the proper persons upon whom to serve process. Cf. Thomson v. McMorran Milling Co., 132 Mich. 591, 94 N. W. 188 (1903).

109. Metropolitan Trust Co. v. Chicago & E. L. Rr. Co., 253 Fed. 868 (C. C. A. 7th, 1918); Susquehanna Trust & Safe Deposit Co. v. United Tel. & Tel. Co., 6 F. (2d) 179 (C. C. A. 3d, 1925); Railway Steel Springs Co. v. Chicago and E. I. Rr. Co., 246 Fed. 338 (N. D. Ill. 1912). This entire subject is discussed by Justice Cardozo with a complete citation of cases in Guaranty Trust Co. of N. Y. v. N. Y. & Queens County Ry. Co., 253 N. Y. 190, 170 N. E. 887 (1930). See also Foley and Pogue, *After-Acquired Property under Conflicting Corporate Indentures* (1929) 13 MINN. L. REV. 81.

property subsequently acquired by the surviving or consolidated corporation.[110]

Special Legal Problems and Incidents of Merger and Consolidation. Although the consolidation of two or more domestic corporations is always deemed to create an entirely new corporate entity, whether or not this same result ensues upon the consolidation of corporations of different states has been much disputed in the decisions. Under the most modern type of consolidation statute, it is clear not only that a new corporation is created but also that such new corporation is a corporation of some one state.[111] However, under the ordinary type of statute dealing with the consolidation of corporations of different states, since the consolidated corporation is not formed under the laws of any one state, it is a somewhat anomalous type of corporate entity, often described as an "interstate" corporation.[112] The weight of authority supports the view that the consolidated "interstate" corporation so created is a new corporation, and that the corporate existences of the constituents are terminated.[113] An analysis of the holdings supporting the contrary view leads to the conclusion that in many instances the courts have been misled by jurisdictional questions or by an undue solicitude for creditors, and as a result have made their language broader than was actually necessary.[114]

Regardless of whether consolidation of corporations of different states creates a new corporation, within the borders of any state in which one of its constituents had been a corporation, the consolidated corporation is subject to the control of the state legislature and to the jurisdiction of the state courts.[115] A

110. Cf. Mississippi Valley Trust Co. v. Southern Trust Co., 261 Fed. 765, 767 (C. C. A. 8th, 1919); Foley and Pogue, *supra* note 109, at 91.

111. This would seem to be the result under the statutes of Arkansas, California, Delaware, Florida, Idaho, Louisiana, Michigan, New York, Pennsylvania, Tennessee, and Washington. The Uniform Business Corporations Law brings about this result, and several of the above states have adopted its provisions, while others have been influenced by it. See UNIFORM BUSINESS CORP. ACT § 43.

112. Bisbee, *supra* note 15, at 389, 390; 15 FLETCHER, op. cit. *supra* note 3, §§ 7181-7187; Beale, *Corporations of Two States* (1904) 4 COL. L. REV. 391.

113. Shields v. Ohio, 95 U. S. 319 (1877); Keokuk & Western Rr. Co. v. Missouri, 152 U. S. 301 (1894); Southern Ry. Co. v. Lancaster, 149 Ga. 434, 100 S. E. 380 (1919); Smith v. Cleveland, C. C. & St. L. Ry. Co., 170 Ind. 382, 81 N. E. 501 (1907); Rio Grande W. Ry. Co. v. Telluride Power-Transmission Co., 16 Utah 125, 51 Pac. 146 (1897); Vermont Valley Rr. v. Conn. River Power Co., 99 Vt. 397, 133 Atl. 367 (1926).

114. See Ohio & Miss. Rr. Co. v. Wheeler, 1 Black 286 (U. S. 1861); Nashua & L. Rr. Corp. v. Boston & L. Rr. Corp., 136 U. S. 356 (1890); Racine & Miss. Rr. Co. v. Farmers' Loan & Trust Co., 49 Ill. 331 (1868), overruled in Ohio & Miss. Ry. Co. v. People, 123 Ill. 467, 14 N. E. 874 (1888); New York Tel. Co. v. State Board of Taxes and Assessments, 159 Atl. 810 (N. J. Sup. Ct. 1932); Note 89 Am. St. Rep. 604, 649 (1903). The statement is often made that whether a new corporation results from consolidation depends on the statute in question. While in most cases this begs the issue, in a few of the early consolidations in particular, possibly the statute did not contemplate a new corporation. See Farnum v. Blackstone Canal Corp., 8 Fed. Cas. No. 4,675, at 1059 (C. C. D. R. I. 1830).

115. Peik v. Chicago & N. W. Rr. Co., 94 U. S. 164 (1876); People v. Dunleith & Dubuque Bridge Co., 322 Ill. 99, 152 N. E. 526 (1926); Pollitz v. Public Utilities Comm. of Ohio, 96 Ohio St. 49, 117 N. E. 149 (1917); Vermont Valley Rr. v. Conn. River Power Co., 99 Vt. 397, 133 Atl. 367 (1926).

like result occurs in regard to the surviving corporation in case of merger.[116]

Intricate problems of jurisdiction of the federal courts on the basis of diversity of citizenship have arisen where the consolidated interstate corporation is a party plaintiff or defendant. When the consolidated corporation is sued, if one of the constituent corporations had been a corporation of the state in which the federal court is located, the consolidated corporation will be presumed to be a corporation of that state, and that state alone. It cannot be sued as a citizen of two states or of some other state. Thus, if constituents of a certain consolidated corporation had been corporations of Delaware and New York respectively, a citizen of New York may sue the consolidated corporation in the federal district court for Delaware, where it will be presumed to be a citizen of Delaware. But he could not sue it in the federal court for New York by claiming it was a citizen of Delaware.[117] This rule may be justified if at all, only on the ground that it affords a convenient method for ascertaining citizenship for the purposes of federal jurisdiction. But the rule apparently in force where the consolidated corporation is a plaintiff lacks even this virtue. It has been held that a consolidated corporation, the constituents of which were corporations of different states, may disregard any corporate existence which it may possess as a corporation of the state in which it brings suit, and sue as a citizen of another state in which one of its constituents had been incorporated. Thus, the consolidated Delaware-New York corporation could sue a citizen of New York in the federal courts in New York by suing as a Delaware corporation, and could sue a citizen of Delaware in the federal court in Delaware by suing as a New York corporation.[118] Aside from the long tradition of federal

116. However, the two cases differ in that upon consolidation the consolidated corporation will be subject to control as a domestic corporation in each state, while upon merger or consolidation under the most recent statutes, the surviving or consolidated corporation will be subject to control as a domestic corporation in only one state. Where a constituent corporation is a foreign corporation with a certificate enabling it to do business in a state, some statutes provide that upon merger or consolidation the surviving or consolidated corporation will not be required to take out a new certificate unless the name of the corporation is changed or the corporation acquires the right to engage in new lines of business. E.g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.113.

117. Railway Co. v. Whitton's Administrator, 13 Wall. 270 (U. S. 1871); Patch v. Wabash Rr. Co., 207 U. S. 277 (1907); Fitzgerald v. Mo. Pac. Ry. Co., 45 Fed. 812 (C. C. D. Neb. 1891); Peterborough Rr. v. B. & M. Rr., 239 Fed. 97 (C. C. A. 1st, 1917); Consolidated Coal Co. v. Western Md. Ry. Co., 44 F. (2d) 595 (D. Md. 1930); cf. St. Louis & S. F. Ry. Co. v. James, 161 U. S. 545 (1896); Louisville, N. A. & C. Ry. Co. v. Louisville Trust Co., 174 U. S. 552 (1899). See DOBIE, FEDERAL JURISDICTION AND PROCEDURE (1928) 203; WILLIAMS, TREATISE ON FEDERAL PRACTICE (1927) 167.

118. Nashua & L. Rr. Corp. v. Boston & L. Rr. Corp., 136 U. S. 356 (1890); cf. Carolina & N. W. Ry. Co. v. Town of Clover, 34 F. (2d) 480 (W. D. S. C. 1929); WILLIAMS, op. cit. *supra* note 117, at 169. The authority of the first of these two cases, which established this rule, is perhaps open to question on the basis that the consolidated corporation was one formed under special acts in 1838. In that period it was not nearly so clear as in 1890 that, substantively, consolidation creates a new corporation. For the rule that the consolidated corporation cannot sue as a corporation formed under the laws of two states, see Ohio & Mississippi Rr. Co. v. Wheeler, 1 Black 286, 297 (U. S. 1861); St. Joseph & G. I. Rr. Co. v. Steele, 167 U. S. 659, 663 (1897).

courts to invoke presumptions and fictions when dealing with the citizenship of corporations, there seems to be no reason for these rules. In view of the fact that the validity of the diversity of citizenship basis of federal jurisdiction has itself been questioned, and that the tendency is to relieve federal courts from unnecessary litigation, it would seem better to take cognizance of the fact that substantively the consolidated corporation may be regarded as a corporation of both states.[119] Of course, under the most modern statutes these problems should not arise, because the consolidated corporation must become a corporation of some one state. Likewise, these difficulties of federal jurisdiction are obviated upon a merger, because the surviving corporation remains solely a corporation of the state of its original creation.[120]

Upon a consolidation, whether of domestic corporations or of corporations of different states, since a new corporation is created, it becomes subject to stock issuance and organization taxes, and to incorporation fees imposed upon the privilege of incorporating.[121] Where the organization tax is measured by the amount of the capital stock of the consolidated corporation, it is liable to be taxed on the entire amount of its capital stock, even though that capital stock is merely the aggregate of those of the constituents, upon which the organization tax had previously been paid.[122] And even if the consolidated corporation is an "interstate" corporation, each state may impose such an organization tax upon the full amount of the capital stock, since each state is granting to the consolidated corporation the privilege of incorporating.[123]

119. See WILLIAMS, op. cit. *supra* note 117, at 168; Frankfurter and Landis, *A Study in the Federal Judicial System* (1927) 40 HARV. L. REV. 834, 871; Comment (1931) 44 HARV. L. REV. 1106, 1110.

120. Lee v. Atlantic Coast Line Rr. Co., 150 Fed. 775 (C. C. D. S. C. 1906); Royal Palm Soap Co. v. Seaboard Air Line Ry. Co., 296 Fed. 448 (C. C. A. 5th, 1924).

121. The issuance of stock upon a merger or consolidation clearly falls within the provisions of the Revenue Act of 1926, 44 STAT. 101, Schedule A-2, 26 U. S. C. A. § 901, Schedule A-2, (1926), as amended by Revenue Act of 1932, 47 STAT. 272, Schedule A-2 (1932), 26 U. S. C. A. § 901, Schedule A-2 (1935). However, it appears that Schedule A-3 of those acts, the stock transfer tax, has no application to the transaction, since the stock goes directly from the surviving or consolidated corporation to the stockholders of the respective constituents without those constituents ever having any right to the stock. Cf. Minnesota Mining and Mfg. Co. v. Willcuts, 2 F. Supp. 789 (D. Minn. 1932); Westmoreland Coal Co. v. MacLaughlin, 8 F. Supp. 963 (E. D. Pa. 1934). While not involving true mergers or consolidations, the principles of these cases would seem to apply to a merger or consolidation. These cases are discussed and criticized in Comment (1935) 44 YALE L. J. 1424. A slightly different problem in regard to stock transfer taxes arises where a constituent owns stock in some other corporation. While the transfer from the constituent to the surviving or consolidated corporation seems to involve a taxable transfer, at least one case has held it not taxable under the New York stock transfer tax. Rockefeller Foundation v. State, 144 Misc. 460, 258 N. Y. Supp. 812 (Ct. Claims, 1932).

122. State v. Consolidated Gas, Electric Light & Power Co., 104 Md. 364, 65 Atl. 40 (1906); People v. Rice, 57 Hun. 486, 11 N. Y. Supp. 249 (Sup. Ct. 1890); Carolina Coach Co. v. Hartness, 198 N. C. 524, 152 S. E. 489 (1930).

123. Ohio & Mississippi Rr. Co. v. Weber, 96 Ill. 443 (1880); Chicago & E. I. Rr. Co. v. State, 153 Ind. 134, 51 N. E. 924 (1898). *Contra:* State Treasurer v. Auditor General, 46 Mich. 224, 9 N. W. 258 (1881); People v. New York, C. & St. L. Rr. Co., 129 N. Y. 474, 29 N. E. 959 (1892); New York Central Rr. Co. v. Flynn, 233 App. Div. 123, 251

However, statutes expressly restrict the tax to any increase in the capital stock over the aggregate capital stocks of the constituents upon which the organization tax had originally been paid.[124] Upon a merger, the surviving corporation will not be liable for such organization taxes or incorporation fees because no new corporation is formed, but in most states the tax imposed on increases in capital stock will partially achieve the same result, for the surviving corporation invariably must increase its capital stock in order to effect the merger.

By the operation of most merger and consolidation statutes, the surviving or consolidated corporation is endowed with all the rights, privileges, powers, and franchises of its constituents, as well as with all their property, real, personal and mixed.[125] Since the surviving or consolidated corporation succeeds to all these solely by operation of law, no instruments of conveyance such as deeds or bills of sale are necessary.[126] Often this succession by operation of law may be attended by incidents different from those attending an ordinary transfer or assignment, for value or otherwise. For example, where a constituent was lessee under a lease containing a clause rendering the lease nonenforceable if assigned, it has been held that the consolidated corporation could enforce the lease.[127] In regard to title to real estate the statutes frequently provide that it shall not revert or in any way be impaired by reason of the trans-

N. Y. Supp. 343 (1931). However, these latter cases have been ones where the tax statute imposed the tax on corporations "organized" under the laws of that state, and the courts have construed this to mean organized under the laws of that state alone, and not to include the organization of a corporation under the concurrent legislation of several states.

124. E.g. DEL. REV. CODE (1915) § 1985, as amended by Del. Laws 1929, c. 135 § 20; KY. STAT. (Carroll, 1930) § 556; PA. STAT. ANN. (Purdon, 1931) tit. 72, § 1822 (c). Louisville Gas & Electric Co. v. Bosworth, 169 Ky. 824, 185 S. W. 125 (1916); cf. Southern Ill. Gas Co. v. Commerce Comm., 311 Ill. 299, 142 N. E. 500 (1924) (tax on issuance of bonds).

125. E.g. ILL. REV. STAT. ANN. (Smith-Hurd, 1933) c. 32, § 157.69(d), N. Y. STOCK CORP. Law (1923) § 89. The language of the different statutes varies, some including "interests" and "immunities" as well as rights, privileges, powers, and franchises. Thus, the surviving or consolidated corporation can sue on a guaranty or surety bond given to the constituent, Bank of America of Cal. v. Granger, 115 Cal. App. 210, 1 P. (2d) 479 (1931); and can exercise any right that a constituent had possessed, such as that of eminent domain, Smith v. Cleveland, C. C. & St. Louis Ry. Co., 170 Ind. 382, 81 N. E. 501 (1907); Reeves v. Phila. Suburban Water Co., 287 Pa. 376, 135 Atl. 362 (1926); of increasing its capital stock, Commonwealth v. Buffalo, R. & P. Ry. Co., 207 Pa. 160, 56 Atl. 412 (1903); of doing intrastate business, State v. Roach, 267 Mo. 300, 184 S. W. 969 (1916); of filing a mechanics' lien, Chambers v. George Vassar's Sons & Co., 81 Misc. 562, 143 N. Y. Supp. 615 (Sup. Ct. 1913); and of indemnifying itself from an insurer of a constituent, Syracuse Lighting Co. v. Maryland Casualty Co., 226 N. Y. 25, 122 N. E. 723 (1919).

126. See Commissioner v. Oswego Falls Corp., 71 F. (2d) 673, 676 (C. C. A. 2d, 1934); Morris v. Interstate Iron & Steel Co., 257 Ill. App. 613, 620 (1930); Silversmiths Co. v. Reed & Barton Corp., 199 Mass. 371, 375, 85 N. E. 433, 434 (1908).

127. Proprietors of Locks & Canals v. B. & M. Rr., 245 Mass. 52, 139 N. E. 839 (1923), error dismissed, 267 U. S. 573 (1925); Pittsburgh Terminal Coal Corp. v. Potts, 92 Pa. Super. 1 (1927); cf. Seaboard Air Line Ry. v. United States, 256 U. S. 655 (1921).

action.[128] In some states it is required that a copy of the articles of merger or consolidation be filed with the recorder of deeds in each county in which any constituent had owned any real estate, and, in view of the desirability of keeping the chain of title on record at all times, this does not seem to be an undue burden to impose on the corporations desiring to merge or consolidate.[129] Moreover, it would seem advantageous for the surviving or consolidated corporation to take some such steps even in the absence of statutory requirements in order to insure the marketability of its own title.

However, the surviving or consolidated corporation holds all such rights, privileges, properties, and other interests of the constituents only in the same right as did those respective constituents, and not in any higher right such as a bona fide purchaser for value would have.[130] Where a constituent had been granted some special right or exclusive privilege by the state, the surviving or consolidated corporation can have no greater right.[131] Thus, if a constituent had been granted a tax exemption in respect to its property, the surviving or consolidated corporation may retain this exemption in reference to the property contributed by that constituent, depending on the terms of the grant and the terms of the merger and consolidation statute.[132] Even this may be lost if the surviving or consolidated corporation cannot comply with the terms of the exemption.[133] Moreover, in the case of a consolidation, if between the time

128. E.g. IND. STAT. ANN. (Burns, Watson's Supp. 1929) § 4856(d); TENN. CODE ANN. (Williams, 1934) § 3751. The Ohio Statute expressly provides for the transfer of title to real estate owned by any constituent in another state "when permitted by the laws of any other state." OHIO GEN. CODE (Page, Supp. 1934) § 8623-71.

129. CAL. CIV. CODE (Deering, 1931) § 361b; IDAHO CODE ANN. (1932) § 29-151(3); IND. STAT. ANN. (Burns, Watson's Supp. 1929) § 4856.1; LA. GEN. STAT. (Dart, 1932) § 1128; N. Y. STOCK CORP. LAW (1923) § 86(8); N. C. CODE ANN. (Michie, 1931) § 1224a.

130. First Nat. Bank of Duncan v. Staley, 4 F. (2d) 324 (C. C. A. 5th, 1925); First Nat. Bank of Missoula v. Holding, 90 Mont. 529, 4 P. (2d) 709 (1931); Vilas v. Page, 106 N. Y. 439, 13 N. E. 743 (1887); cf. Charles v. Roxana Petroleum Corp., 282 Fed. 983 (C. C. A. 8th, 1922).

131. Punxsutawney Borough v. T. W. Phillips Gas & Oil Co., 238 Pa. 23, 85 Atl. 1003 (1913). And in some cases the entire special privilege will be destroyed. Storrs v. Ghinger, 166 Md. 572, 171 Atl. 849 (1934).

132. Philadelphia & Wilmington Rr. Co. v. Maryland, 10 How. 376 (U. S. 1850); Tennessee v. Whitworth, 117 U. S. 139 (1885). While the latter case held that a tax exemption was a "right and privilege" which passed to the consolidated corporation, later cases indicate that use of the word "privilege" is insufficient to pass the exemption. Rochester Ry. Co. v. Rochester, 205 U. S. 236 (1906); Wright v. Georgia Rr. & Banking Co., 216 U. S. 420 (1910); and in Phoenix Fire & Marine Ins. Co. v. Tennessee, 161 U. S. 174 (1896), it was held that the terms "immunity" or "exemption" must be in the statute to transfer the tax exemption. See 15 FLETCHER, op. cit. *supra* note 3, § 7100.

133. Thus, where a grant stipulated that the constituent should never be subject to any income tax except on any excess over a 10% return on its investment, and also provided that the constituent make an annual return of its income to the state, a commingling of the properties of that constituent with properties of others pursuant to a consolidation was held to work a forfeiture of the exemption, since it was impossible thereafter to ascertain what part of the income of the consolidated corporation was properly allocable to the constituent to which the exemption had been granted. State v. Maine

the exemption was granted and the time the consolidation took place, some statute or constitutional provision had been passed prohibiting the grant of such exemptions, the exemption is lost even as to the constituent's properties, because upon consolidation the constituent is dissolved and the new corporation created with reference to the laws existing at the time of the consolidation.[134] The same result ensues upon a merger if the exemption belonged to a constituent, because the surviving corporation can only be endowed with those rights and privileges which could lawfully be conferred at the date of the merger. But if the exemption belonged to the corporation which survived, it is not lost insofar as the survivor's original properties are concerned.[135]

A special problem arises where a constituent corporation has been named as a fiduciary, such as an executor or a trustee.[136] At the present time the legal effect of merger or consolidation in such a situation is not clear, because of the innumerable factual situations which conceivably may arise and because there are few judicial decisions thereon. Moreover, the matter has been further complicated by the attempts of legislatures to deal specifically with the problem of succession of corporate fiduciaries by means of statutes, and as a result there is always doubt as to whether the statutes will cover a given set of facts. In the absence of such statutes, where a state bank or trust company merges or consolidates with another state bank or trust company, the types of questions likely to arise are whether the right of the constituent to act as fiduciary was a right to which the surviving or consolidated corporation could succeed by virtue of the merger or consolidation statute alone,[137] and whether the designation of a corporation as a fiduciary creates a relation too personal to be delegated.[138] The problem may become even more complex where a state bank has merged or consolidated with a national bank under the McFadden Act of 1927, which not only authorizes such mergers or consolidations, but also purports to make the corporation resulting from the transaction succeed to any right to act as fiduciary which any constituent had possessed.[139] This act has been con-

Central Rr. Co., 66 Me. 488, 513 (1877); cf. St. Louis I. Mt. & S. Ry. Co. v. Berry, 41 Ark. 509 (1883).

134. Railroad Co. v. Maine, 96 U. S. 499 (1877); Railroad Co. v. Georgia 98 U. S. 359 (1878); St. Louis, I. Mt. & S. Rr. Co. v. Berry, 113 U. S. 465 (1884); cf. Shaw v. City of Covington, 194 U. S. 593 (1904) (exclusive privilege of supplying city with electric power is lost); Yazoo & M. V. Rr. Co. v. Sunflower County, 125 Miss. 92, 87 So. 417 (1921) (unlocated right of way is lost).

135. Tomlinson v. Branch, 15 Wall. 460 (U. S. 1872); Central Rr. & Banking Co. v. Georgia, 92 U. S. 665 (1875); Central of Georgia Ry. Co. v. Wright, 250 U. S. 519 (1919); cf. Southwestern Rr. Co. v. Georgia, 92 U. S. 676 (1875).

136. See Fruchtman, *The Effect of Merger or Consolidation on the Succession of Corporate Fiduciaries* (1934) 22 Ky. L. J. 378, particularly for its discussion of the possible factual situations and of statutory provisions; Comment (1930) 8 N. Y. U. L. Q. Rev. 126.

137. Matter of Bergdorf, 206 N. Y. 309, 99 N. E. 714 (1912); Matter of Stikeman, 48 Misc. 156, 96 N. Y. Supp. 460 (1905).

138. Chicago Title & Trust Co. v. Zinser, 264 Ill. 31, 105 N. E. 718 (1914).

139. 44 Stat. 1224 (1927), as amended 48 Stat. 190 (1933), 12 U. S. C. A. § 34a (1934).

strued to authorize such succession only when not in contravention of state law.[140]

Conclusion. In the past the disadvantages of merger or consolidation in comparison with other devices for effecting combination have operated to restrict its use. The principal disadvantage of merger or consolidation has been the inadequacies of statutory authorization, either in the sense of no general statutory provision for merger or consolidation at all, or no provision for the merger or consolidation of corporations of different states.[141] Aside from this fact, other forms of combination possessed advantages over merger or consolidation. In comparison with the holding company device, merger or consolidation is less adaptable to local conditions, particularly in being unable to avoid heavy state taxation upon foreign corporations in states in which the surviving or consolidated corporation must do business; it results in the permanent loss of the names and goodwills of at least some of the constituents; it is more difficult to disorganize the unprofitable units of a large single corporation than it is to dissolve single unprofitable subsidiaries; and the process of bringing about a merger or consolidation involves more difficulties than those encountered in creating a holding company structure.[142] Compared with a sale of entire corporate assets, the disadvantages of merger or consolidation center about the fact that the consent of the stockholders of each corporation participating in the transaction must be obtained, while in a sale of assets, only the consent of the stockholders of the selling corporation is necessary.[143] However, despite these disadvantages, within recent years there have been indications that the statutory merger and consolidation device is being and will be used more widely as a means of combining corporations. Factors leading to this increased use have been the tendency toward simplicity in corporate structure, in industrial as well as public utility fields;[144] the fact that merger or consolidation often proves to be a facile device by which to revamp the financial structures of two or more corporations, either with or without any connection with a true reorganization; the exemption since 1918 of mergers and consolidations from the gain or loss provisions of the federal income tax;[145]

140. Ex parte Worcester County Nat. Bank, 279 U. S. 347 (1929), aff'g with modification, Worcester County Nat. Bank, Petitioner, 263 Mass. 444, 162 N. E. 217 (1928).

141. Of course, where there was no authority to merge or consolidate in the state of which one constituent was a corporation, and there was such authority in the state of which a second constituent was a corporation, the first constituent could reincorporate in the latter state, and then the merger or consolidation could take place. However, this extra step of reincorporation adds to the inconvenience of merger or consolidation.

142. OWENS, op. cit. *supra* note 1, at 383.

143. Field, *supra* note 3, at 241.

144. See N. Y. Times, Sept. 22, § 3, at 1, col. 5; id., Oct. 3, 1935, at 43, cols. 4, 5; id. Oct. 24, 1935, at 31, col. 4; BURTCHETT, op. cit. *supra* note 1, at 774, 780.

145. 40 STAT. 1060 (1918), as amended 43 STAT. 256 (1924), as amended 44 STAT. 12 (1926), 26 U. S. C. A. § 934(h)(1)(A) (1928), as amended 48 STAT. 705 (1934), 26 U. S. C. A. § 112 (g)(1)(A) (1935). The 1934 Act may make the use of merger or consolidation an even more desirable device in this respect, since it seems to close up loop-holes in the former acts. See (1935) 45 YALE L. J. 134.

and finally, merger and consolidation appear to have had somewhat greater immunity from attack under the Clayton Act than have other forms of combination.[146]

CORPORATE REORGANIZATION TO AVOID PAYMENT OF INCOME TAX

SINCE 1918, Congress has provided that gains created by exchanges of properties in pursuance of corporate reorganizations shall not be recognized for purposes of federal income taxation until those properties are subsequently sold for cash.[1] The deferment of the recognition of such gains is allowed because it is feared that the taxation of mere paper gains may impede the effectuation of normal business adjustments by reorganization.[2] But the comprehensive scope given to this exemption in Revenue Acts prior to 1934, for the purpose of including therein virtually every possible type of legitimate reorganization,[3] has made available to taxpayers a means of escaping taxation on gains realized, by bringing within the exemption provisions, transactions otherwise taxable in the year in which they are effected.[4] For, although theoretically the taxpayers will have thereby merely deferred the recognition of their gains,[5] the opportunity thus afforded them to elect the year in which to report such gain in many cases leads to an actual avoidance of taxation.[6]

146. Section 7 of the Clayton Act forbids any corporation to acquire the whole or any part of the "share capital" of two or more corporations, where the effect of such acquisition may be substantially to lessen competition between such corporations, restrain competition in interstate commerce, or create a monopoly. It seems this section does not apply to a merger or consolidation. Arrow-Hart & Hegeman Electric Co. v. Federal Trade Comm., 291 U. S. 587 (1934). But insofar as the Sherman Act is concerned, any special immunity of merger and consolidation is very doubtful. See Handler, *Industrial Mergers —Anti-Trust Laws* (1932) 32 COL. L. REV. 179, 235, 266. Cf. OWENS, op. cit. *supra* note 1, at 384.

1. See Revenue Act of 1918, 40 STAT. 1060 (1919). For history of reorganization exemption provisions of various revenue acts since 1918 see Eisner, *Taxation Affecting Corporate Reorganization* (1933) VIII LECTURES ON LEGAL TOPICS 413; Hendricks, *Taxation of Reorganizations* (1934) 34 COL. L. REV. 1198, 1209; Satterlee, *The Income Tax Definition of Reorganization* (1934) 12 TAX MAG. 639, 641.

2. See *Hearings Before Committee on Ways and Means on Revenue Revision*, 73d Cong., 2d Sess. (1934) 59; H. R. Rep. No. 179, 68th Cong., 1st Sess. Ser. No. 8226 (1924) 13; Miller, *Corporate Reorganization* (1934) 12 TAX MAG. 459, 462; Satterlee, *supra* note 1, at 646.

3. See Eisner, *supra* note 1, at 419; Hendricks, *supra* note 1, at 1209.

4. See Altman, *Recent Developments in Income Tax Avoidance* (1934) 29 ILL. L. REV. 154, 171; GREEN, THEORY AND PRACTICE OF MODERN TAXATION (1933) 117.

5. See § 113 (a) (6) of the Revenue Acts of 1928 (45 STAT. 818), and 1932 (47 STAT. 198). This provision has been retained unchanged in the Revenue Act of 1934. 48 STAT. 706 (1934), 26 U. S. C. A. § 113 (1935).

6. See *Hearings Before Committee on Ways and Means on Revenue Revision* 73d Cong., 2d Sess. (1934) 58, 60, 75.

Consequently, the problem has often arisen under the 1928[7] and 1932[8] Acts, and probably will continue so to arise for some time, of distinguishing between a reorganization within the intent of the statutes, and one, which, although technically an exempt reorganization is being utilized solely as a device to avoid taxation on actual present gains.

Parts (A) and (B) of the definitions found in the Revenue Acts of 1928 and 1932 have, by reason of their inclusiveness been mainly responsible for making it possible to disguise otherwise taxable transactions as reorganizations, and thus obtain for them the exemptions provided by other provisions of the statutes.[9] Part (A) defines "reorganization" as a merger or consolidation and by means of a parenthetical addition includes therein as a type of merger and consolidation, the acquisition by one corporation of substantially all the assets of another.[10] Even though actually the transferor corporation may have merely sold all its assets without any purpose of effecting a business reorganization, the transaction would come within this definition of reorganization provided the transferor had conveyed substantially all its assets.[11] Consequently, in accordance with the statutory exemptions, if only stock or securities are received by the transferor corporation in exchange for its assets, no gain to the corporation is recognized at that time, and furthermore even though cash is included as part of the exchange, if this cash is distributed in pursuance of the alleged plan of reorganization, then, too, no taxable gain will accrue as to the corporation.[12] The holders of its outstanding stocks or securities will also realize no taxable gain by virtue of the exemption, if they exchange their holdings for stocks or securities of the purchasing corporation.[13] Even when they receive cash as part of their exchange, the amount of gain immediately recognized as resulting from the exchange can not be in excess of the sum of such cash.[14]

Part (B) of the statutory definitions of reorganization recognizes as a reorganization the mere transfer of assets by one corporation to another when the transferor or its stockholders are in "control" of the transferee immediately after the transfer.[15] Section 112 (G) of the 1928 and 1932 Acts further permits stock-

7. 45 STAT. 816 (1928), 26 U. S. C. A. § 2112 (1928).

8. 47 STAT. 196 (1932).

9. See § 112 of the Revenue Acts of 1928 (45 STAT. 816), and 1932 (47 STAT. 196). Similarly extensive provisions are contained in the Revenue Acts of 1926 (44 STAT. 12) and 1924 (43 STAT. 256). See also Hills, *Reorganizations under the Revenue Act of 1934* (1934) 12 TAX MAG. 411; Hendricks, *supra* note 1, at 1198, 1205, 1215; Note (1933) 33 COL. L. REV. 1456.

10. § 112 (i) (1): "The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation)."

11. See Hill, *supra* note 9, at 411; *Hearings Before Committee on Ways and Means on Revenue Revision* 73d Cong., 2d Sess. (1934) 57.

12. § 112 (B) (4), (D) (1), 45 STAT. 816 (1928); 47 STAT. 197 (1932).

13. § 112 (B) (3). 14. § 112 (C).

15. § 112 (i) (1): "The term 'reorganization' means (A) . . ., or (B) a transfer by one corporation of all or a part of its assets to another corporation if immediately after the transfer, the transferor or its stockholders or both are in control" of the transferee. By § 112 (j) "control" is defined as the ownership of at least 80% of the voting stock and at

holders of a participating corporation to receive stock of the transferee and at the same time retain their original holdings in the transferor without being held to have received taxable gain.[16] By virtue of these provisions, corporations may effect distributions of assets to their stockholders, without the latter incurring the tax liability ordinarily involved in such distributions.[17] In this type of case, the asset to be distributed is first transferred to a specially organized corporation in exchange for all of the latter's stock. Under part (B) of the definition, that transaction is a reorganization. Therefore the stock of the new corporation can then be distributed tax free to the transferor's stockholders. Thereafter the latter can liquidate the new corporation, receiving their proportionate shares of its assets as liquidating dividends. Since a liquidating dividend is treated for federal income taxation purposes as a sale of the stock, the only taxable gain thus created is the excess of that dividend over the basis for the shares in the liquidated corporation.[18] In view of the fact that that basis is determined by apportioning the basis formerly applicable to the old shares between the old and new shares in proportion to their respective values at the time of distribution of the new corporation's shares, the gain immediately recognized and taxed is far less than that which had actually accrued.[19]

There is nothing on the face of the 1928 and 1932 Statutes that would serve to withdraw these transactions, which literally satisfy all statutory requirements, from the exemption provisions. For they make no attempt to distinguish between a reorganization carried through merely to gain the benefit of the exemption and a bona fide corporate reorganization. It seems clear, however, that the

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least 80% of the total number of shares of all other classes of stock of the corporation. Besides parts (A) and (B) the definition contains two other parts: namely "(C) a recapitalization, or (D) a mere change in identity, form, or place of organization however effected."

16. § 112 (G), 45 STAT. 816 (1928); 47 STAT. 197 (1932).

17. See REPORT OF COMMITTEE ON WAYS AND MEANS, REP. No. 704, 73d Cong., 2d Sess. (1934) 12; REPORT OF SENATE COMMITTEE ON FINANCE, REP. No. 558, 73d Cong., 2d Sess. (1934) 16.

18. See § 115 (C), 45 STAT. 822 (1928); 47 STAT. 204 (1932).

19. See § 113 (A) (9). Then see U. S. Treas. Reg. 74, art. 600, rule 2 (1928) as amended by T. D. 4427 viii-2 Cum. Bull. 240 (1929); U. S. Treas. Reg. 77, Art. 600 rule 2 (1932). Thus corporation *A*, capitalized at $1,000,000 10,000 shares, had transferred its surplus of $250,000 to Corporation *B* in exchange for all of the latter's stock. This stock had been distributed to Corporation *A*'s stockholders. *X*, a stockholder has one share in Corporation *A*, cost $100, and now receives an additional share in Corporation *B*. When Corporation *B* is liquidated, *X* receives $25. The basis applicable to the share in Corporation *A*, $100, is allocated between that share and the new share in Corporation *B* in proportion to their respective market values at the date of distribution, $100 and $25 respectively. Thus the basis for the share in Corporation *A* is $80: $\frac{100}{125} \times 100 = 80$, and the basis for the share in Corporation *B* is $20: $\frac{25}{125} \times 100 = \$20$. Therefore *X* has now realized a taxable gain of only $5. See Evelyn F. Gregory, 27 B. T. A. 223, 226 (1932), citing MILLER, HENDRICKS AND EVERETT, REORGANIZATIONS AND OTHER EXCHANGES IN FEDERAL INCOME TAXATION (1931) 316. Cf. David B. Gann, 23 B. T. A. 999 (1931) aff'd 61 F. (2d) 201 (C. C. A. 7th, 1932). But cf. *Hearings Before Committee on Ways and Means*, 73d Cong., 2d Sess. (1934) 62, Exhibit D, example no. 6.

intent of Congress was to permit only the latter to go untaxed. The courts have attempted to effectuate that intention and so prevent misuse of the exemption by setting up certain criteria to differentiate between bona fide and fictitious reorganizations.[20]

Thus it has been decided that the mere fact that substantially all[21] the assets of one corporation have been transferred to another corporation is not of itself sufficient to constitute the transaction a reorganization under the statute.[22] In the absence of the element of "control" of the transferee corporation which would bring the transaction within part (B) of the definition, the process, in order to come within part (A), must resemble or partake of the nature of a merger or consolidation for the reason that, although part (A) is not strictly limited to mergers and consolidations, it is fundamentally concerned with transactions of that general character.[23] When attempting to define this "resemblance to a merger or consolidation," the federal courts found that mergers and consolidations are usually characterized by the fact that the interests of those who formerly owned the properties involved in the merger or consolidation are continued in those properties after the completion of the process. Accordingly, it was held that before a transaction may come within part (A) of the definition, there must be present a "continuance of interest" on the part of the transferor in the properties transferred.[24]

But no precise definition of "continuance of interest" exists.[25] Hence, the problem remains of affording a meaning to this standard that will serve the pur-

20. See Eisner, *supra* note 1, at 419; Note (1933) 33 COL. L. REV. 1456, 1457; cf. Satterlee, *supra* note 1, at 642.

21. "Substantially all" apparently means all the properties of any consequence as regards value at the time the transaction takes place. Cf. The Western Industries Co., 30 B. T. A. 809 (1934), 85.2% held not substantially all); The National Pipe and Foundry Co., 19 B. T. A. 242 (1930) (95% held substantially all). See also Hendricks, *The Income Tax Definition of Reorganization* (1932) 45 HARV. L. REV. 648, 655; MILLER, HENDRICKS AND EVERETT, *supra* note 19, at 115.

22. Pinellas Ice and Cold Storage Co. v. Commissioner, 287 U. S. 462 (1933); Sarther Grocery Co. v. Commissioner, 63 F. (2d) 68 (C. C. A. 7th, 1933).

23. Cortlandt Specialty Co. v. Commissioner, 60 F. (2d) 937 (C. C. A. 2d, 1932); cf. Pinellas Ice and Cold Storage Co. v. Commissioner, 57 F. (2d) 188 (C. C. A. 5th, 1932) modified in 287 U. S. 462 (1933).

24. Cortlandt Specialty Co. v. Commissioner, 60 F. (2d) 937 (C. C. A. 2d, 1932) approved in Pinellas Ice and Cold Storage Co. v. Commissioner, 287 U. S. 462, 470 (1933). Further support for this standard is found in the manner in which the term "reorganization" is used in the related exchange provisions of Section 112. See § 112 (b) (3, 4), and § 112 (C) (D). 45 STAT. 816 (1928); 47 STAT. 196 (1932). See also Minnesota Tea Co. v. Commissioner, 76 F. (2d) 797, 802 (C. C. A. 8th, 1935); The C. H. Mead Coal Co., 28 B. T. A. 599, 609 (1933), aff'd in part in 72 F. (2d) 22 (C. C. A. 4th, 1934).

25. Dissolution of the transferor corporation has been offered as a further criterion of "resemblance to a merger or consolidation." See the Minnesota Tea Co., 28 B. T. A. 591 (1933), rev'd 76 F. (2d) 797 (C. C. A. 8th, 1935); John J. Watts, 28 B. T. A. 1056 (1933), rev'd, 75 F. (2d) 981 (C. C. A. 2d, 1935). This standard is of little utility because in the absence of continuity of interest, dissolution will not make the transaction an exempt reorganization. Cf. The Pinellas Ice and Cold Storage Co. v. Commissioner, 287 U. S. 462 (1933). As to reasons for its inapplicability, see Hendricks, *supra* note 1, at 1211, 1214; Miller, *supra* note 2, at 460.

pose of preventing tax avoidance, and at the same time not contradict the express provisions of the statutes. It is, in the first place, evident that the interest continued need not be a "controlling" interest in the transferee.[18] Part (B) which requires "control," is distinct and separate from part (A) of the definition.[20] That these two provisions are intended to cover different situations is manifest from the fact that a transferor may receive stock only in exchange for his assets, and yet not obtain "control" of the transferee. To require "control" where the transferor has conveyed substantially all its properties would render part (A) entirely superfluous because all reorganizations under part (A) would then be equally within part (B). In the second place, it seems clear that "continuance of interest" cannot require continuation of exactly the same interests. A requirement of that character would automatically exclude from the exemption those exchanges in which the transferor receives any cash as part of the consideration for its transferred assets. But the statutes specifically permit the inclusion of cash in the exchange, and therefore by this provision recognize as a reorganization an exchange where exactly the same interests are not continued.[27]

Since these rigid requisites for "continuance of interest" are precluded by reason of conflict with the provisions of the statutes, the courts have commonly set up a general requirement of "some continuity of interest."[28] But a standard of this character frustrates the purposes for which "continuance of interest" was formulated for the reason that it is too vaguely inclusive to offer an effectual means of preventing tax avoidance. Therefore "some continuance of interest" has apparently been defined to require the inclusion of voting common stock of the transferee as part of the exchange for the transferred assets,[29] and accord-

26. See C. H. Mead Coal Co. v. Commissioner, 72 F. (2d) 22, 27 (C. C. A. 4th, 1934); Opinion of the General Counsel of Internal Revenue Bureau, G. C. M. 1753 VI—1 Cum. Bull. (1927) 138, 139. Legislative history bears out the contention that parts (A) and (B) represent separate alternative methods of reorganizing. See REPORT OF COMMITTEE ON WAYS AND MEANS, REP. No. 179, 68th Cong., 1st Sess. (1924) 16; Satterlee, *supra* note 1, at 642.

27. § 112 (D), 45 STAT. 816 (1928); 47 STAT. 196 (1932). Moreover when properties have been consolidated or merged, seldom can the interests of the constituent owners be exactly the same as before. For these assets have now become part of a greater mass of properties, and one's interest in the latter will be different than it previously was with respect to his individual part.

28. Cortlandt Specialty Co. v. Commissioner, 60 F. (2d) 937 (C. C. A. 2d, 1932); Minnesota Tea Co. v. Commissioner, 76 F. (2d) 797 (C. C. A. 8th, 1935).

29. Mead Coal Co. v. Commissioner, 72 F. (2d) 22 (C. C. A. 4th, 1934); Watts v. Commissioner, 75 F. (2d) 981, 982 (C. C. A. 2d, 1934); cf. Keen and Woolf Oil Co. v. Commissioner, 49 F. (2d) 45, 46 (C. C. A. 5th, 1931). But see G. & K. Manufacturing Co. v. Commissioner, 76 F. (2d) 454, 456 (C. C. A. 4th, 1935). Inclusion of voting common stock would not appear to be necessary to denote resemblance to a merger or consolidation. See note 48, *infra*. But this requirement, however, serves the purpose of making it possible to differentiate those transactions in which the speculative interest in the venture is disposed of, and only bonds or notes are received in the exchange, from those in which the speculative interest and a voice in the management of the transferee corporation are retained, apparently for the reason that the former are more likely to be sales of assets disguised as reorganizations. Cf. the Cortlandt Specialty Co. v. Commissioner 60 F. (2d) 937 (C. C. A. 2d, 1932); Nelson v. Commissioner, 75 F. (2d) 696, 698 (C. C. A. 7th, 1935).

ingly, the receipt of wholly bonds,[30] notes,[31] or non-voting preferred stock[32] has been held insufficient to constitute a continuance of interest. But there has been no attempt to require the transferor to receive some minimum percentage of total consideration in the form of the voting common stock, and without some minimum, the criterion still may easily be reduced to a virtual nullity. For, if it is held that no certain percentage is required, then any transaction in which a transferor exchanges substantially all its properties for cash, notes, or bonds plus a very small amount of voting stock may fulfill the requirement. Consequently, corporate taxpayers might sell their assets for practically all cash, and, after distributing that cash, still be permitted to defer recognition of the gains resulting from the sale.[33]

It therefore appears that if "continuance of interest" is to serve the purpose for which it exists, it must necessarily be further restricted. Some such restriction may be found in the requirement that there be a continuation of essentially the same interests.[34] Although no definition may as yet be offered as to what proportion of common stock is requisite to constitute continuance of essentially the same interests, such a standard would seem to exclude from the exemption those transactions where a substantial amount of cash, notes, or bonds is received as part of the exchange.[35] Nevertheless in the recent case of *Minnesota Tea Co. v. Commissioner*, the Circuit Court of Appeals expressly overruled the Board of Tax Appeals' requirement of continuance of essentially the same interests, and decided that the transferor cannot be required to receive any particular percentage of the stock of the transferee as a condition of coming within the exemption.[36]

Even if the criterion of continuity of essentially the same interests might serve to prevent the use of part (A) for other than legitimate reorganizations, it would still be ineffective in those cases where the transferor corporation comes within part (B) of the definition of reorganization by receiving all the stock of its transferee in the exchange, and, by thus complying with the literal provisions of

30. Worcester Salt Co. v. Commissioner, 75 F. (2d) 251 (C. C. A. 2d, 1935); Frank M. McNab, 33 B. T. A. No. 31, Oct. 11, 1935.

31. Pinellas Ice and Cold Storage Co. v. Commissioner, 287 U. S. 462 (1933); Cortlandt Specialty Co. v. Commissioner, 60 F. (2d) 937 (C. C. A. 2d, 1932).

32. Nelson v. Commissioner, 75 F. (2d) 696 (C. C. A. 7th, 1935).

33. See Woodrough, Circuit Judge, dissenting in Minnesota Tea Co. v. Commissioner, 76 F. (2d) 797, 805 (C. C. A. 8th, 1935).

34. See Nelson v. Commissioner, 75 F. (2d) 696, 698 (C. C. A. 7th, 1935). But see Minnesota Tea Co. v. Commissioner, 76 F. (2d) 797, 802 (C. C. A. 8th, 1935).

35. The Board of Tax Appeals in the Minnesota Tea Case, 28 B. T. A. 591 (1933) relied on the standard of "continuity of essentially the same interests" to hold a transaction in which the exchange consisted of less than 60% in voting stock, the balance in cash, not a reorganization. It was reversed in 76 F. (2d) 797 (C. C. A. 8th, 1935). This standard has been criticized by one authority as presenting a highly metaphysical concept, and as requiring "control" by the transferor. See Hendricks, *supra* note 1, at 1203, 1217. But on examination continuance of essentially the same interests does not require "control" but merely represents an advance in the degree of interest to be continued. See note (1933) 33 COL. L. REV. 1456, 1457.

36. 76 F. (2d) 797 (C. C. A. 8th, 1935); cf. Pinellas Ice and Cold Storage Co. v. Commissioner, 287 U. S. 462, 470 (1933).

the statute, avoids the tax on corporate dividends.[17] A further criterion is therefore required in such situations if tax avoidance by this device is to be halted. In *Gregory v. Helvering*,[37] the Supreme Court endeavored to supply that criterion. The court in that case was confronted by a transaction that fully satisfied the requirements of the statute, but held that in order to be awarded the exemption, the transaction alleged to be a reorganization must further have a corporate or business purpose; it should not be a mere device to avoid taxation.

The doctrine of the *Gregory* case, though it renders certainty or predictability impossible,[38] does present a potentially effective means of preventing tax avoidance. For the taxpayer's motives, whether to effect a business adjustment by reorganization, or merely to evade taxation, may now be scrutinized and the exemption accordingly awarded. But the *Gregory* case presented a peculiar set of facts. There was in the record an open avowal by the taxpayer that the sole purpose in employing the reorganization procedure was to avoid taxes, and the case may therefore be easily distinguished from other and more usual fact situations, where the direct avowal is absent and the purpose of the taxpayer is therefore doubtful.[39] Consequently the general utility and applicability of the *Gregory* doctrine is yet to be demonstrated.

When formulating the reorganization exemption provisions of the Revenue Act of 1934,[40] Congress was aware of the extent to which this exemption was being employed as a means of tax avoidance, notwithstanding the judicial attempts to prevent this abuse.[41] In an effort to check such tax avoidance and at the same time enable legitimate reorganizations to enjoy their previous immunity, Congress in the Revenue Act of 1934 eliminated certain provisions of the previous acts, and amended others. Such changes, would, of course, be applicable only to transactions effected after the 1934 Act. Consequently, transactions previously consummated under the 1928 and 1932 Acts, will probably continue to be litigated under the provisions of those Acts, raising the problems previously discussed.

Under the 1934 Act, the acquisition of substantially all the properties of a corporation is not a reorganization for the purposes of federal income taxation, unless the transferor receives the total consideration in voting stock of the transferee.[42] Hence, Congress has apparently incorporated in that section the

37. 293 U. S. 465 (1935) aff'g 69 F. (2d) 809 (C. C. A. 2d, 1934) which had reversed 27 B. T. A. 223 (1932), noted in (1935) 48 HARV. L. REV. 852; (1935) 23 CALIF. L. REV. 641.

38. The decision has been widely criticized on this score. See Miller, *supra* note 1, at 459, 461, 462; Thompson, *Step Reorganizations* (1934) 12 TAX MAG. 356, 360; cf. Hendricks, *supra* note 21, at 648. See also Treasury statement in *Hearings Before Committee on Ways and Means on Revenue Revision*, 73d Cong., 2d Sess. (1934) 59.

39. Cf. Minnesota Tea Co. v. Commissioner 76 F. (2d) 797 (C. C. A. 8th, 1935) and Woodrough, Circuit Judge, dissenting, at 803; George H. Chisholm, 29 B. T. A. 1334 (1934).

40. 48 STAT. 704 (1934); 26 U. S. C. A. § 112 (1935).

41. A subcommittee of the Committee on Ways and Means recommended the elimination of the reorganization exemption on the ground that "the abuses under the present policy far outweigh the advantages." *Hearings Before Committee on Ways and Means on Revenue Revision*, 73d Cong., 2d Sess. (1934) 58, 60, 75.

42. § 112 (G) (1), 48 STAT. 704 (1934), 26 U. S. C. A. § 112 (1935): "The term 'reorganization' means (A) . . . or (B) the acquisition by one corporation in exchange solely for all or a part of its voting stock: of at least 80 per cent of the voting stock and at least

standard of "continuity of essentially the same interests." Thus, an exchange whose status under what formerly was part (A) of the definition in the 1928 and 1932 Acts was doubtful because it involved the receipt of cash, notes, bonds, or preferred stock, is clearly not a reorganization under the new Act.

Although part (B) of the previous definition of reorganization is retained unchanged in the 1934 Act,[15] it cannot now provide a means of making corporate distributions that escape the taxes on dividends because the section which exempted the receipt of additional stock in pursuance of a reorganization, notwithstanding the retention of the old stocks,[16] has been eliminated. When a stockholder in one corporation now receives stock in another participating corporation, a taxable gain will immediately result unless he has surrendered his original holdings.[43] Consequently, although the corporation may by means of a corporate reorganization effect a segregation of the asset which it desires to distribute, its stockholders cannot obtain the control of this asset without being subjected to the recognition of taxable gain. This amendment therefore, appears to render unnecessary any future dependence upon the *Gregory*[37] doctrine to prevent tax avoidance in these cases.[44]

Congress effected still a third change in the definition of reorganization for the purposes of the exemption. The term "reorganization" is no longer generally defined as a "merger or consolidation" but is expressly limited to "statutory merger or consolidations."[45] Thus a merger or consolidation to be an exempt reorganization must be effected in accordance with the merger and consolidation laws of a state, territory, or district of Columbia.[46] Since a merger or consolidation is necessarily statutory, Congress has here not introduced any additional restriction, but has merely indicated more clearly the meaning to be attached to "merger and consolidation."[47] It is possible, however, that in some cases the problem will be raised as to whether a transaction that conforms to the state statutory requirements is necessarily an exempt reorganization for the purposes of federal income taxation. Some state merger and consolidation statutes permit the distribution of wholly notes or bonds to the stockholders of the constituent corporation in place of their original holdings.[48] The argument might be made

80% of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation." Cf. note 10 *supra*.

43. See U. S. Treas. Reg. 86, Art. 112 (g)-5 (1934).

44. Cf. U. S. Treas. Reg. 86, Art. 112 (a) (1); Art. 112 (g) (1) (1934).

45. § 112 (G) (1): "The term 'reorganization' means (A) a statutory merger or consolidation" 48 STAT. 704 (1934), 26 U. S. C. A. § 112 (1935).

46. U. S. Treas. Reg., Art. 112 (g)-2 (1934). No reason appears why the federal statutes, which authorize certain types of mergers and consolidations are not included. See Hills, *supra* note 9, at 412; Hendricks, *supra* note 1, at 1199n.

47. See Comment (1935) 45 YALE L. J., 105, for exhaustive discussion of the nature of a statutory merger or consolidation. See also Hills, *supra* note 1, at 411, 412.

48. See, E.g., ARK. DIG. STAT. (Crawford & Moses, Supp. 1931) § 170112: "The agreement may provide for the distribution of cash, notes or bonds in whole or in part, in lieu of stock to the stockholders of the constituent corporations or any of them." See also CAL. CIV. CODE (Deering, 1931) § 361; FLA. COMP. GEN. LAWS ANN. (1927) § 6562; NEV. COMP. LAWS (Hillyer, 1930) § 1638; OHIO GEN. CODE (Page, Supp., 1935) § 8623-67; TENN. CODE ANN. (Williams, 1934) § 3750. Cf. ILL. REV. STAT. (Cahill & Moore, 1935) c. 32 § 62, and similar statutes, permitting the distribution of "shares or other securities or obligations of the surviving corporation."

that such exchanges are not exempt reorganizations because under the decisions of the federal courts, there is no "continuity of interest." On the other hand, however, it might be pointed out that the criterion of continuity of interest was formulated in order to determine whether a transfer of substantially all the assets of a corporation sufficiently resembled a merger and consolidation when it technically was not such, and that when the transaction fully satisfies every formal requisite of a true merger or consolidation,[49] the standard is unnecessary. In the event that the transaction before the court is really a sale of assets disguised as a statutory merger or consolidation, then the purpose for which the merger or consolidation was effected may be examined and the exemption allowed or denied in accordance with the doctrines developed in the *Gregory* case.[37]

RIGHT OF INTERSTATE CARRIER TO COLLECT UNDERCHARGES

I

THE Interstate Commerce Act prohibits interstate carriers by land from charging or collecting any rates for transportation or other services different from those on file with the Interstate Commerce Commission or from refunding or remitting any portion of such rates by any device.[1] To effectuate these provisions of the Act aimed at discrimination by the carriers, the courts have established the broad principle that interstate carriers cannot be estopped by their own mistakes or negligence to collect the full legal rate from any person liable therefor.[2] This principle has been applied regardless of any intent to accomplish a discrimination both because it is felt that an inflexible rule will most effectively eliminate purposeful discrimination[3] and because even unin-

49. Cf. U. S. Treas. Reg. 86, art. 112 (g)-1 (1934), setting up the requirement of continuity of interest for all reorganizations.

1. 34 STAT. 587 (1906), 49 U. S. C. A. § 6(7) (1926).

2. Pittsburgh, Cincinnati, Chicago & St. Louis Ry. Co. v. Fink, 250 U. S. 577 (1919); Louisville & Nashville Rr. Co. v. Central Iron & Coal Co., 265 U. S. 59 (1924). And the Interstate Commerce Commission has ruled that the carrier must exhaust its legal remedies to collect such rate. I. C. C. Conference Ruling No. 314, Bulletin No. 7, issued Aug. 1, 1917. Apparently the only escapes are the running of the three-year statute of limitations [43 STAT. 633 (1924), 49 U. S. C. A. § 16, par. 3(a) (1926); Strawberry Growers Selling Co., Inc., v. American Railway Express Co., 31 F. (2d) 947 (C. C. A. 5th, 1929); Vicksburg, S. & P. Ry. Co. v. Paup, 47 F. (2d) 1069 (C. C. A. 5th, 1931)] and possibly the fraud of the carrier [American Express Co. v. Sweeney, 283 Fed. 691 (D. Mass. 1922)].

The only protection against misquotation of rates available to a person assuming a liability for freight charges is to make a written request to an agent of the carrier for a written statement of the lawful rates applicable to a given shipment. If the carrier then makes a misstatement which results in damage to the person requesting the statement, it becomes liable to the United States for a penalty. 36 STAT. 548 (1910), 49 U. S. C. A. § 6(11) (1926). But this affords no remedy to the person injured; it simply supplies an incentive to the carrier to exercise care to avoid mistakes.

3. See Robinson, *The Field Rate in Public Utility Law: A Study in Mechanical Jurisprudence* (1928) 77 U. OF PA. L. REV. 213.

tentional discrimination is considered objectionable. Overzealous judicial efforts to maintain this rule, however, have often resulted in hardship to individual shippers in cases in which its application tends to defeat rather than to execute the policy of the Act.[4]

II

In order to understand the effect of the rule that the carrier cannot be estopped to collect the full legal rate it is first essential to examine the liability of persons served by the carrier for its charges.

Liability of Consignee. If the consignee is the owner of the goods or the person on whose behalf the shipment is made, he is liable for the lawful charges as undisclosed principal of the person ordering the shipment.[5] But even if he does not fall within this rule, any consignee accepting delivery of the goods becomes liable on a contract implied in law to pay the lawful charges in return for the carrier's releasing its lien upon the goods by delivery.[6] Prior to the enactment of the Newton Amendment[7] the United States Supreme Court had held in *New York Central & Hudson River. Rr. Co. v. York & Whitney Co.*[8] that this liability arising from acceptance of the goods could not be avoided even though the consignee was a commission merchant acting only as agent for the shipper and though the carrier had notice of that fact.

Under the rule of that case any consignee accepting delivery clearly became liable to the carrier for any undercharge arising from a mistake as to the lawful rates in spite of any stipulation made at the time of acceptance that the carrier should look only to the consignor for any charges other than those then demanded which might subsequently be found to be due.[9] Where, however, the mistake was as to the amount which had been collected prior to delivery rather than as to the lawful rates, a few courts have held that the carrier is estopped

4. Pittsburgh, Cincinnati, Chicago & St. Louis Ry. Co. v. Fink, 250 U. S. 577 (1919); Davis, Director General of Railroads, v. Timmonsville Oil Co., 285 Fed. 470 (C. C. A. 4th, 1922); Central Warehouse Co. v. Chicago, R. I. & P. Ry. Co., 20 F. (2d) 828 (C. C. A. 8th, 1927), aff'g 14 F. (2d) 123 (D. Minn. 1926), noted in (1927) 27 COL. L. REV. 89; (1920) 15 ILL. L. REV. 102. But cf. St. Louis-San Francisco Ry. Co. v. Republic Box Co., 12 F. (2d) 441 (S. D. Tex. 1926).

5. Southern Flour & Grain Co. v. Seaboard Air Line Ry., 22 Ga. App. 403, 95 S. E. 997 (1918); Philadelphia & Reading Ry. Co. v. Parry, 66 Pa. Super. 49 (1917); (1917) 17 COL. L. REV. 553; Comment (1930) 28 MICH. L. REV. 910. But cf. Davis v. City Fuel Co., 157 Ark. 455, 248 S. W. 572 (1923); Chicago, Burlington & Quincy Rr. Co. v. Evans, 221 Mo. App. 757, 288 S. W. 73 (1926).

6. Pittsburgh, Cincinnati, Chicago & St. Louis Ry. Co. v. Fink, 250 U. S. 577 (1919).

7. 44 STAT. 1447, 49 U. S. C. A. § 3 (2) (1927).

8. 256 U. S. 406 (1921).

9. Western & Atlantic Rr. Co. v. Underwood, 281 Fed. 891 (N. D. Ga. 1922); Western Grain Co. v. St. Louis-San Francisco Ry. Co., 56 F. (2d) 160 (C. C. A. 5th, 1932); cf. Callaway v. Atchison, T. & S. F. Ry. Co., 35 F. (2d) 319 (C. C. A. 8th, 1929) (consignee held liable though result was unlawful rebate by consignee to shipper under Packers' and Stockyards Act).

to collect any undercharges thereby resulting.[10] The theory of these cases seems to be that the reason for refusing to allow an estoppel in the cases involving mistake as to rates is that the consignee has constructive notice of the filed tariffs and therefore is not entitled to rely upon a representation as to their contents, a reason inapplicable to the cases involving mistake as to the amount collected, since the carrier is the most reliable source of information about such collections.[11] But this distinction does not seem well taken, for it misapprehends the reason for refusing an estoppel, which is to close up any loophole for making rebates. The prohibited undercharge will just as certainly have been made where the "mistake" takes the form of false representation of the amount collected as where it results from erroneous computation of rates.[12]

Some courts, apparently desiring to limit the rule of the *York & Whitney* case, have confined its application by a narrow and technical definition of the term consignee. The rule clearly applies to the person named in the bill of lading as consignee,[13] or to his assignee,[14] if he accepts the goods. However,

10. Davis v. Akron Feed & Milling Co., 296 Fed. 675 (C. C. A. 6th, 1924), noted in (1924) 34 YALE L. J. 200; Cleveland, Cincinnati, Chicago & St. Louis Ry. Co. v. McKenzie Lumber Co., 112 Ohio St. 80, 147 N. E. 8 (1925), noted in (1925) 20 ILL. L. REV. 372; Cincinnati Northern Ry. Co. v. Beveridge, 8 F. (2d) 372 (E. D. Va. 1925) *semble*. *Contra:* Great Northern Ry. Co. v. Hyder, 279 Fed. 783 (W. D. Wash. 1922); Western & Atlantic Rr. Co. v. Underwood, 281 Fed. 891 (N. D. Ga. 1922); Central Warehouse Co. v. Chicago, R. I. & P. Ry. Co., 20 F. (2d) 828 (C. C. A. 8th, 1927), aff'g 14 F. (2d) 123 (D. Minn. 1926), noted in (1927) 27 COL. L. REV. 89; Strong v. Atchison, T. & S. F. Ry. Co., 123 Kans. 161, 254 Pac. 405 (1927); New York, New Haven & Hartford Rr. Co. v. Lord & Spencer, Inc., 273 Mass. 583, 174 N. E. 179 (1931); Houston & Texas Central Rr. Co. v. Johnson, 41 S. W. (2d) 14 (Tex. Comm. of App. 1931), noted in (1931) 18 VA. L. REV. 200; Norfolk & Western Ry. Co. v. Williamson Grocery Co., 103 W. Va. 532, 138 S. E. 102 (1927); Waters v. Pfister & Vogel Leather Co., 176 Wis. 16, 186 N. W. 173 (1922).

11. Davis v. Akron Feed & Milling Co., 296 Fed. 675 (C. C. A. 6th, 1924), noted in (1924) 34 YALE L. J. 200; Cincinnati Northern Rr. Co. v. Beveridge, 8 F. (2d) 372 (E. D. Va. 1925); Cleveland, Cincinnati, Chicago & St. Louis Ry. Co. v. McKenzie Lumber Co., 112 Ohio St. 80, 147 N. E. 8 (1925), noted in (1925) 20 ILL. L. REV. 372.

12. Great Northern Ry. Co. v. Hyder, 279 Fed. 783 (W. D. Wash. 1922); New York, New Haven & Hartford Rr. Co. v. Lord & Spencer, Inc., 273 Mass. 583, 174 N. E. 179 (1931); Norfolk & Western Ry. Co. v. Williamson Grocery Co., 103 W. Va. 532, 138 S. E. 102 (1927).

13. Illinois Central Rr. Co. v. Belson & Lurie, 237 Ill. App. 425 (1925); Davis, Director General of Railroads v. Moody, 203 Ky. 203, 261 S. W. 1101 (1924); Louisville & Nashville Rr. Co. v. Perry Ice & Bottling Co., 226 Ky. 286, 10 S. W. (2d) 1091 (1928); Transmarine Corp. v. Delaware & Hudson Co., 127 Misc. 812, 216 N. Y. Supp. 623 (Sup. Ct. 1926); Director General of Railroads v. McCormack, 82 N. H. 528, 136 Atl. 253 (1927); Southern Ry. Co. v. Calhoun Twine Mill, 180 S. E. 557 (S. C. 1935); Houston & Texas Central Ry. Co. v. Ahlers, 274 S. W. 333 (Tex. Civ. App. 1925).

14. Dare v. New York Central Rr. Co., 20 F. (2d) 379 (C. C. A. 2d, 1927), noted in (1928) 28 COL. L. REV. 95; Central Warehouse Co. v. Chicago, R. I. & P. Ry. Co., 20 F. (2d) 828 (C. C. A. 8th, 1927), aff'g 14 F. (2d) 123 (D. Minn. 1926), noted in (1927) 27 COL. L. REV. 89; Case v. Union Pacific Rr. Co., 119 Kans. 706, 241 Pac. 693 (1925); New York Central Rr. Co. v. Hendel, 123 Misc. 907, 207 N. Y. Supp. 234 (City Ct. 1924).

there are decisions refusing to apply it to notify-parties[15] or to persons to whom the carrier has been directed to make delivery.[16] But these cases reflect a dislike of the rule, rather than enunciate a distinction based upon reason, for it was the surrender of the lien by delivery of possession which formed the basis of liability in the *York & Whitney* case. The designation of the person to whom delivery was made as consignee in the bill of lading seems immaterial.

Where the consignee accepting delivery of the goods is "an agent only, and has no beneficial title in the property" and gives notice in writing to that effect to the carrier prior to delivery,[7] the Newton Amendment to the Interstate Commerce Act relieves him from the liability imposed by the rule of the *York & Whitney* case for charges other than those billed against him at the time of delivery.[7] This clearly affords relief to the sales agent or commission merchant. It ought not, however, to be applied to a consignee who has actually purchased goods f. o. b .point of destination, for while he might easily be held to have no "beneficial title" in the property prior to delivery,[17] he could hardly establish that he is an "agent only."

Liability of shipper. It seems to be assumed that there must be at least one person liable to the carrier for the lawful charges in order to satisfy the requirements of the Interstate Commerce Act.[18] Since it had been held that a consignee accepting the goods did assume such a liability,[19] the result was easily reached that the consignor might contract with the carrier that he should not be liable for the charges if the consignee accepted the goods, for the inescapable liability of the accepting consignee was sufficient.[20] Apparently, then, the shipper need only become liable as guarantor of acceptance by the consignee;[18] he must undertake to pay any difference between the lawful charges and the proceeds of a sale of the goods in satisfaction of the carrier's lien in the event of the consignee's refusal to accept delivery.

15. Davis, Director General of Railroads, v. Ducote, 145 So. 717 (La. App. 1933). *Contra:* Central Warehouse Co. v. Chicago, R. I. & P. Ry. Co., 20 F. (2d) 828 (C. C. A. 8th, 1927), aff'g 14 F. (2d) 123 (D. Minn. 1926), noted in (1927) 27 COL. L. REV. 89; Nashville, Chattanooga & St. Louis Ry. Co. v. Gilliam, 212 Ala. 120, 101 So. 889 (1924), noted in (1925) 23 MICH. L. REV. 657.

16. Smith Bros. Co. v. Charleston & Western Carolina Ry. Co., 36 Ga. App. 480, 137 S. E. 115 (1927); Cincinnati Northern Rr. Co. v. Beveridge, 8 F. (2d) 372 (E. D. Va. 1925) *semble. Contra:* Chicago Great Western Rr. Co. v. Schmit, 163 Minn. 194, 203 N. W. 618 (1925); Erie Railroad Co. v. H. Rosenstein, Inc., 249 N. Y. 241, 164 N. E. 37 (1928), noted in (1929) 29 COL. L. REV. 521, (1928) 37 YALE L. J. 939; Southern Ry. Co. v. Herndon, 175 S. C. 361, 179 S. E. 306 (1935).

17. But the only holding on the point is to the contrary. Western Grain Co. v. St. Louis-San Francisco Ry. Co., 56 F. (2d) 160 (C. C. A. 5th, 1932).

18. See Louisville & Nashville Rr. Co. v. Central Iron & Coal Co., 265 U. S. 59, 68 (1924).

19. See p. 143, *supra.*

20. Louisville & Nashville Rr. Co. v. Central Iron & Coal Co., 265 U. S. 59, 68 (1924). But cf. Chesapeake & Ohio Ry. Co. v. Glogora Coal Co., 113 W. Va. 796, 169 S. E. 471 (1933) (such a contract cannot be made when the lawful tariff requires prepayment). Perhaps liability cannot be escaped if the consignor is owner of the goods. Cf. New York Central Rr. Co. v. Union Oil Co. of Pa., 53 F. (2d) 1066 (W. D. Pa. 1931). *Contra:* Michigan Central Rr. Co. v. Saginaw Milling Co., 262 N. W. 425 (Mich. 1935).

The actual liability assumed must, therefore, be determined by the contract between the shipper and the carrier, which is ordinarily embodied in the bill of lading. The uniform bill of lading prescribed by the Interstate Commerce Commission contains a "no recourse" blank to be signed by the shipper if he is to be released from liability in case the carrier surrenders its lien without requiring payment of the charges.[21] It has been suggested that the only method now available to the shipper for avoiding liability is to sign this blank.[22] This probably goes too far,[23] but only one case has been found relieving the shipper from liability when he has signed such a bill of lading as consignor without filling in the "no recourse" blank.[24] In the absence of a specific contract provision limiting his liability the shipper is presumed to be liable as the owner of the goods and the person on whose behalf and under whose direction the shipment is being made.[25] This presumption is said to be rebuttable, but the cases hold the shipper liable even though he did not own the goods, unless he disclosed that fact and did nothing to indicate that he was

21. On the back of the bill of lading is this provision:

"Sec. 7: The owner or consignee shall pay the freight or average, if any, and all other lawful charges accruing on said property; but, except in those instances when it may be lawfully authorized to do so, no carrier by railroad shall deliver or relinquish possession at destination of the property covered by this bill of lading until all tariff rates and charges thereon have been paid. The consignor shall be liable for the freight and all other lawful charges, except that if the consignor stipulates, by signature, in the space provided for that purpose on the face of this bill of lading that the carrier shall not make delivery without requiring payment of such charges and the carrier, contrary to such stipulation, shall make delivery without requiring such payment, the consignor shall not be liable for such charges. Nothing herein shall limit the right of the carrier to require at time of shipment the prepayment or guarantee of the charges. . . ."

On the face of the bill of lading:

"If this shipment is to be delivered to the consignee without recourse on the consignor, the consignor shall sign the following statement:

"The carrier shall not make delivery of this shipment without payment of freight and all other lawful charges. (See section 7 of conditions).

.....

(Signature of consignor)"

Even signing this blank has been held ineffective to relieve the consignor from liability when he was owner of the goods. New York Central Rr. Co. v. Union Oil Co. of Pa., 53 F. (2d) 1066 (W. D. Pa. 1931). *Contra:* Michigan Central Rr. Co. v. Saginaw Milling Co., 262 N. W. 425 (Mich. 1935).

22. Western Maryland Ry. Co. v. Cross, 96 W. Va. 666, 123 S. E. 572 (1924); cf. Pennsylvania Rr. Co. v. Marcelletti, 256 Mich. 411, 240 N. W. 4 (1932); Chicago Junction Ry. Co. v. Duluth Log Co., 161 Minn. 466, 202 N. W. 24 (1925); Grand Trunk Western Rr. Co. v. Markis, 142 Misc. 807, 255 N. Y. Supp. 443 (Mun. Ct. 1932).

23. Cf. Louisville & Nashville Rr. Co. v. Central Iron & Coal Co., 265 U. S. 59 (1924); St. Louis-San Francisco Ry. Co. v. Republic Box Co., 12 F. (2d) 441 (S. D. Tex. 1926); T. S. Faulk Co. v. Chicago, Indianapolis & Louisville Ry. Co., 21 Ala. App. 617, 111 So. 196 (1926), cert. denied, 215 Ala. 488, 111 So. 199 (1927); Moss Lumber Co. v. Michigan Central Rr. Co., 219 Ala. 593, 123 So. 90 (1929).

24. Galveston, Harrisburg & San Antonio Ry. Co. v. American Salvage & Supply Co., 15 S. W. (2d) 25 (Tex. Civ. App. 1929).

25. Louisville & Nashville Rr. Co. v. Central Iron & Coal Co., 265 U. S. 59 (1924).

contracting as principal.[26] Nor is he relieved from liability by reason of the carrier's releasing the goods to the consignee without requiring payment, despite the fact that the bill of lading contains the provision "owner or consignee paying freight" and that the Interstate Commerce Act requires collection of the charges before delivery,[27] for these provisions are construed as intended for the benefit of the carrier only.[28]

Reconsignment. When the original consignee reconsigns the shipment to another destination, additional problems arise. The ultimate consignee accepting the goods is clearly liable for all the charges under the rule of the *York & Whitney* case unless he brings himself within the Newton Amendment, which provides that his notice of agency and lack of beneficial title must contain in addition the name and address of the beneficial owner.[7] The original shipper is also clearly liable as consignor for the charges up to the original destination or to the point of diversion, unless he has relieved himself from such liability by special contract.[29]

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26. Cincinnati, New Orleans & Texas Pacific Ry. Co. v. Vredenburgh Sawmill Co., 13 Ala. App. 442, 69 So. 228 (1915); T. S. Faulk & Co. v. Chicago, Indianapolis & Louisville Ry. Co., 21 Ala. App. 617, 111 So. 196 (1926), cert. denied, 215 Ala. 488, 111 So. 199 (1927); New York Central Rr. Co. v. Frank H. Buck Co., 2 Cal. (2d) 384, 41 P. (2d) 547 (1935); New York Central Rr. Co. v. Singer Manufacturing Co., 131 Atl. 111 (N. J. Sup. 1925); Central of Georgia Ry. Co. v. Lovell, 111 Misc. 735, 180 N. Y. Supp. 922 (Mun. Ct. 1919); Pennsylvania Rr. Co. v. General Crushed Stone Co., 76 Pa. Super. 186 (1921); Director General of Railroads v. Birdsboro Stone Co., 86 Pa. Super. 587 (1926); Delaware, Lackawanna & Western Rr. Co. v. Andrews Brothers Co., Inc., 90 Pa. Super. 574 (1927); Delaware, Lackawanna & Western Rr. Co. v. Ludwig, 94 Pa. Super. 289 (1928); Montpelier & Wells River Rr. v. Charles Bianchi & Sons, 95 Vt. 81, 113 Atl. 534 (1921), noted in (1922) 6 MINN. L. REV. 316; Coal & Coke Ry. Co. v. Backhannon River Coal & Coke Co., 77 W. Va. 309, 87 S. E. 376 (1915). But cf. Yazoo & M. V. R. Co. v. Zemurray, 238 Fed. 789 (C. C. A. 5th, 1917), noted in (1917) 17 COL. L. REV. 553, (1917) 30 HARV. L. REV. 760; Baltimore & Ohio Rr. Co. v. Johnson Battle Lumber Co., 37 Ga. App. 729, 141 S. E. 678 (1928).

27. 41 STAT. 479 (1920), 49 U. S. C. A. § 3(2) (1926).

28. Main Island Creek Coal Co. v. Chesapeake & Ohio Ry. Co., 23 F. (2d) 248 (C. C. A. 6th, 1928); Atchison, T. & S. F. Ry. Co. v. Hunt Bros. Fruit Co., 34 F. (2d) 582 (W. D. Mo. 1929); New York Central Rr. Co. v. Union Oil Co. of Pa., 53 F. (2d) 1056 (W. D. Pa. 1931); Moss Lumber Co. v. Michigan Central Rr. Co., 219 Ala. 593, 123 So. 90 (1929); Missouri Pacific Rr. Co. v. Pfeiffer Stone Co., 166 Ark. 226, 266 S. W. 82 (1924); Seaboard Air Line Ry. Co. v. Montgomery, 28 Ga. App. 639, 112 S. E. 652 (1922); New York Central Rr. Co. v. Philadelphia & Reading Coal & Iron Co., 286 Ill. 267, 121 N. E. 581 (1919), aff'g 210 Ill. App. 267 (1918), noted in (1920) 15 ILL. L. REV. 102; Chicago Junction Ry. Co. v. Duluth Log Co., 161 Minn. 466, 202 N. W. 24 (1925); Yazoo & Mississippi Valley Rr. Co. v. Picher Lead Co., 190 S. W. 387 (Mo. App. 1917); Davis, Director General of Railroads, v. Ford, 193 N. C. 444, 137 S. E. 328 (1927); Montpelier & Wells River Rr. v. Charles Bianchi & Sons, 95 Vt. 81, 113 Atl. 534 (1921), noted in (1922) 6 MINN. L. REV. 316; Coal & Coke Ry. Co. v. Backhannon River Coal & Coke Co., 77 W. Va. 309, 87 S. E. 376 (1915); Western Maryland Ry. Co. v. Cross, 96 W. Va. 666, 123 S. E. 572 (1924).

29. Cf. Pere Marquette Rr. Co. v. American Coal & Supply Co., 239 Ill. App. 139 (1925); S. A. Gerrard Co. v. New York, New Haven & Hartford Rr. Co., 39 Ohio App. 84, 176 N. E. 126 (1930).

It is the liability of the original consignee that has caused most of the difficulty. He should, of course, be considered as consignor of the reshipment and be held liable as such for the additional charges resulting from the reshipment unless he has contracted for an exemption from liability.[30] The real stumbling block is his liability for the charges which had accrued at the time of the reconsignment order. If he is the owner and has authorized the shipment, he should be held as the person receiving the benefit of the carrier's services.[31] But even in the absence of such a basis for holding him, there is substantial authority to the effect that simply making the reconsignment order is such an act of dominion over the goods as to amount to a constructive acceptance of the shipment and thus bring him within the rule of the *York & Whitney* case.[32] This result does not seem warranted by the rule, for the basis

30. Pere Marquette Rr. Co. v. American Coal & Supply Co., 239 Ill. App. 139 (1925); New York Central Rr. Co. v. Satuloff, 122 Misc. 119, 202 N. Y. Supp. 297 (Sup. Ct. 1923); S. A. Gerrard Co. v. New York, New Haven & Hartford Rr. Co., 39 Ohio App. 84, 176 N. E. 126 (1930); Delaware, Lackawanna & Western Rr. Co. v. Andrews Brothers Co., Inc., 90 Pa. Super. 574 (1927); Pennsylvania Rr. Co. v. Rothstein, 116 Pa. Super. 156, 176 Atl. 861 (1935); cf. Chesapeake & Ohio Rr. Co. v. Southern Coal, Coke & Mining Co., 254 Ill. App. 238 (1929), cert. denied, 282 U. S. 860 (1930) (terms of contract held to relieve consignee of liability).

31. Wabash Ry. Co. v. Horn, 40 F. (2d) 905 (C. C. A. 7th, 1930); New York Central Rr. Co. v. Satuloff, 122 Misc. 119, 202 N. Y. Supp. 297 (Sup. Ct. 1923).

32. New York Central Rr. Co. v. Platt & Brahm Coal Co., 236 Ill. App. 150 (1925); Andrew W. Mellon, Director General of Railroads, v. Landeck, 248 Ill. App. 353 (1928); Central Rr. Co. of New Jersey v. National Asbestos Mfg. Co., 127 Atl. 184 (N. J. Sup. Ct. 1925) (though reconsignment was return of goods to original consignor); C. L. Hils Co. v. Louisville & Nashville Rr. Co., 28 Ohio App. 459, 162 N. E. 761 (1928) (agency, if any, was undisclosed); West Jersey & Seashore Rr. Co. v. Whiting Lumber Co., 71 Pa. Super. 161 (1919); Pennsylvania Rr. Co. v. Rothstein & Sons, 109 Pa. Super. 96, 165 Atl. 752 (1933). *Contra:* Chicago, Indiana & Southern Rr. Co. v. D. E. McMillan & Brother Coal Co., 207 Ill. App. 58 (1917); Pere Marquette Rr. Co. v. American Coal & Supply Co., 239 Ill. App. 139 (1925); Chesapeake & Ohio Ry. Co. v. Southern Coal, Coke & Mining Co., 254 Ill. App. 238 (1929), cert. denied, 282 U. S. 860 (1930).

The same result has been reached as to the effect of making delivery orders. New York Central Rr. Co. v. Frank H. Buck Co., 2 Cal. (2d) 384, 41 P. (2d) 547 (1935); New York Central Rr. Co. v. Warren Ross Lumber Co., 234 N. Y. 261, 137 N. E. 324 (1922), noted in (1923) 36 HARV. L. REV. 751, (1923) 71 U. OF PA. L. REV. 390; New York Central Rr. Co. v. Maloney, 137 Misc. 751, 244 N. Y. Supp. 394 (Co. Ct. 1930). *Contra:* New York Central Rr. Co. v. Sharp, 124 Misc. 265, 206 N. Y. Supp. 755 (Sup. Ct. 1924), aff'd, 213 N. Y. Supp. 867 (4th Dep't, 1925), noted in (1925) 38 HARV. L. REV. 824 (defendant was notify-party).

Also as to assignment of bill of lading. New York Central Rr. Co. v. Stanzialc, 105 N. J. L. 593, 147 Atl. 457 (1929), rev'g 6 N. J. Misc. 1116, 143 Atl. 834 (1928), noted in Comment (1930) 28 MICH. L. REV. 910. *Contra:* Wallingford Bros. v. Bush, 255 Fed. 949 (C. C. A. 8th, 1918), noted in (1919) 19 COL. L. REV. 500; Davis, Director General, v. Richardson, 87 Pa. Super. 205 (1926).

See, also, Davis v. City Fuel Co., 157 Ark. 455, 248 S. W. 572 (1923) (goods were consigned by defendant's vendor to purchaser from defendant; defendant held not liable).

Probably the question is not necessarily involved in most of the cases discussing it, for the typical case is one in which the ultimate consignee has refused the goods and suit is brought by the carrier against the original consignee for the difference between the total

of the liability imposed by the rule is the release of the carrier's lien by delivery of the goods, and that basis is lacking in these cases, the carrier retaining its lien until delivery is made to the ultimate consignee.[33]

III

Thus it may be seen that in many cases both shipper and consignee may be liable to the carrier for undercharges, affording the carrier a choice of parties from whom to collect. Ultimate liability between shipper and consignee for the charges, however, is determined by a contract to which the carrier is not a party. So long as both remain solvent, there is no serious objection to allowing the carrier a choice of collecting from either, for if the carrier collects from the party not ultimately liable, the latter will be able to recover over against the party ultimately liable.[34] But if the party ultimately liable becomes insolvent before the undercharge is collected, it seems hard to hold the other party, leaving him without effective remedy to recover a loss which he will have suffered if he has sold the goods at a price reckoned on the basis of the amount orginally demanded by the carrier or has settled his account with the party ultimately liable on that basis.

Nor is such a result necessary to effectuate the policy of the Interstate Commerce Act against discrimination. Normally the only person receiving any advantage from a rebate is the one who as between shipper and consignee is ultimately liable for the charges. To exempt the other party from liability cannot, therefore, operate as a discrimination in his favor.[35] Indeed, if he is held liable at a time when he cannot recoup his loss against the other party, the result is a discrimination against him because he is forced to bear alone a loss to the carrier arising from insolvency, which in other fields is regarded as a cost of the business and distributed among all the customers.

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charges and the amount realized from a sale of the goods in satisfaction of the carrier's lien. This difference will ordinarily be not more than the additional charges accruing by reason of the reconsignment, for which the original consignee may be held as consignor of the reshipment.

33. In accord with this theory is the holding that the Newton Amendment, when it refers to a consignee accepting delivery, does not apply to a consignee making a reconsignment order. Pennsylvania Rr. v. Rothstein & Son, 109 Pa. Super. 96, 165 Atl. 752 (1933); cf. Pennsylvania Rr. Co. v. Rothstein, 116 Pa. Super. 156, 176 Atl. 861 (1935).

While it is true that the lien may become inadequate security by reason of the additional charges involved in the reconsignment, the appropriate method for the carrier to avoid this risk is to refuse to comply with the reconsignment order until the charges which it involves are paid.

34. There is, of course, the theoretical objection of circuity of action. But in practice collection will be made without litigation except in the insolvency cases. See Hook, J., dissenting, in Wallingford Bros. v. Bush, 256 Fed. 949, 951 (C. C. A. 8th, 1918), noted in (1919) 19 COL. L. REV. 500.

35. There is a possible theoretical exception to this statement. A manufacturer-shipper not ultimately liable for the charges may receive an indirect advantage from a rebate given to its distributors in the form of larger sales resulting from the lower prices to consumers made possible by the rebate. This advantage would be even more apparent in cases where the distributors are subsidiaries of the manufacturer. But the possibility seems too indirect and remote to deserve judicial recognition, especially since liability on the part of the shipper can be avoided by signing the "no recourse" blank.

This situation could be obviated by the courts' looking to the contract between shipper and consignee and holding that the rule refusing to allow an estoppel against the carrier to collect the undercharges was limited to cases against the party ultimately liable on that contract. Such a limitation on the rule would not open the way to additional devices for violation of the prohibition against rebating, and it would eliminate the cases of hardship resulting from the present inflexible application of the rule. Furthermore, while it may be true that such a rule would result in greater losses to carriers from failure to collect undercharges, nevertheless that objection would seem immaterial since the purpose of prohibiting rebating is not to relieve carriers of the burden of such losses and throw it instead on individual shippers, but rather to prevent discrimination between shippers. The result would be that where the consignee was an agent of the shipper or had purchased goods f. o. b. point of destination, he could raise an estoppel against the attempt of the carrier to collect undercharges; a shipper could do the same if he did not own the goods when shipped or if he had sold them f. o. b. point of shipment. It would be immaterial who paid the carrier the amount demanded before the mistake was discovered, for any payment made by the other party would be a payment on account of the party ultimately liable and not proof that the party paying was ultimately liable.