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INFANT STOCKHOLDERS

The purpose of the present article is to set forth a few of the general principles concerning the rights and liabilities of infant stockholders in corporations organized for profit, with particular attention to the Indiana cases upon the subject. Where the contract of a minor is involved, the questions which immediately present themselves are whether or not such contract is binding upon the infant, under what conditions may the minor disaffirm the same, and what will be the result of such disaffirmance. What is to follow in the succeeding pages will deal chiefly with these three questions.

An infant may subscribe for stock in a corporation, unless the charter of the corporation or a statute of the state provides otherwise.¹ We have no statute in Indiana preventing an infant from becoming a stockholder. But an infant cannot be an incorporator in this state, because our state statute requires at least three incorporators, all of whom must be of lawful age.² Prior to the enactment of this section, however, there was nothing in the laws of Indiana to prevent a minor from being one of the incorporators of a new corporation.

A subscription for corporate stock by an infant may, at his option, be disaffirmed and repudiated when the infant attains his majority and, upon such disaffirmance, he cannot be held liable either to the corporation or to its creditors or to an innocent purchaser of a note given by him for such subscription.³ All jurisdictions agree that a stock subscription contract made by a minor is voidable and not void. Consequently, it may become binding by ratification after the minor has reached his majority. Such ratification is valid even though, at the time of ratification, the infant was ignorant of his right to disaffirm.⁴

¹ 2 FLETCHER, ENCYCLOPEDIA OF CORPORATIONS, § 546.

² BURNS' ANN. IND. STAT. (SUPP. 1929) § 4835.

³ FLETCHER, *op. cit. supra* note 1; 31 C. J. 1098.

⁴ Clark v. Van Court, 100 Ind. 113 (1884).

The minor may avoid his stock subscription contract by disaffirmance upon reaching full age. The authorities are in harmony upon this point.⁵ But such disaffirmance must be made by the minor or by his legal representative. The plea of infancy is a personal privilege and is not available to others in privity of estate.⁶ This privilege remains purely personal during the lifetime of the minor, though the exercise of such privilege by the minor himself may inure to his privies in estate.⁷

We find, however, a lack of harmony in the decisions upon the question of what conditions are necessary to entitle the infant to disaffirm his contract. Here again all agree that he is entitled to the return of the purchase price upon a return of, or an offer to return, the stock which he has bought.⁸ Upon this point the Supreme Court of Indiana, in *Carpenter v. Carpenter*,⁹ said:

“If the minor, when avoiding his contract, have in his hands any of its fruits specifically, the act of avoiding the contract by which he acquired such property will divest him of all right to retain the same; and the other party may reclaim it. He cannot avoid in part only, but must make the contract wholly void if at all; so that it will no longer protect him in the retention of the consideration. *Badger v. Phinney*, 15 Mass. 359; *Bigelow v. Kinney*, 3 Verm. 353. Or, if he retain and use or dispose of such property after becoming of age, it may be held as an affirmation of the contract by which he acquired it, and thus deprive him of the right to avoid. *Boyden v. Boyden*, 9 Met. 519; *Robbins v. Eaton*, 10 N. H. 561. But if the consideration has passed from his hands, either wasted or expended during his minority, he is

⁵ *Wuller v. Chuse Groc. Co.*, 241 Ill. 398, 89 N. E. 796, 132 A. S. R. 216, 28 L. R. A. (N. S.) 128, 16 Ann. Cas. 522 (1909); *Carpenter v. Carpenter*, 45 Ind. 142 (1873); *White v. Branch*, 51 Ind. 210 (1875); *Indianapolis Chair Mfg. Co. v. Wilcox*, 59 Ind. 429 (1877); *Shirk v. Shultz*, 113 Ind. 571 (1887); *Seeley v. Seeley-Howe-LeVan Co.*, 128 Iowa 294, 103 N. W. 961 (1905); *Robinson v. Weeks*, 56 Me. 102 (1868); *White v. New Bedford Cotton Waste Corporation*, 178 Mass. 20, 59 N. E. 642 (1901); *Godfrey v. Mutual Finance Corporation*, 242 Mass. 197, 136 N. E. 178 (1922); *Danziger v. Iron Clad Realty & Trading Co.*, 141 N. Y. S. 593 (1913); *Gage v. Menczer*, 144 S. W. 717 (Tex. Civ. App. 1912).

⁶ *Harris v. Ross, Treas.*, 112 Ind. 314, 13 N. E. 873 (1887).

⁷ *Shrock v. Crowl*, 83 Ind. 243 (1882), citing *Pitcher v. Laycock*, 7 Ind. 398 (1856), and *Price v. Jennings*, 62 Ind. 111 (1878).

⁸ *Wuller v. Chuse Groc. Co.*, *op. cit. supra* note 5; *Seeley v. Seeley-Howe-LeVan Co.*, *op. cit. supra* note 5; *Crowley v. Mutual Finance Corporation*, 242 Mass. 259, 136 N. E. 179 (1922); *Gage v. Menczer*, *op. cit. supra* note 5.

⁹ *Op. cit. supra* note 5, at 146.

not thereby to be deprived of his right or capacity to avoid his deed, any more than he is to avoid his executory contracts. And the adult who deals with him must seek the return of the consideration paid or delivered to the minor in the same modes and with the same chances of loss in the one case as in the other. *Dana v. Stearns*, 3 Cush. 372. It is not necessary, in order to give effect to the disaffirmance of the deed or contract of a minor, that the other party should be placed *in statu quo*. *Tucker v. Moreland*, 10 Pet. 65-74; *Shaw v. Boyd*, 5 S. & R. 309.”

In establishing his right to a cancellation of the contract, the infant, of course, must show that his contract was with the defendant.¹⁰

The avoidance of such contract by the infant may be made either before or after the infant reaches his majority.¹¹ The fact of infancy at the time of the making of the contract is never presumed. Rather, the presumption is that the parties thereto were all of full age. The infant, therefore, must plead and prove such fact when asking for relief.¹²

As previously stated, the authorities disagree as to the conditions upon which the minor is entitled to a return of the consideration paid by him. Perhaps the greater weight of authority is that the minor, as a condition precedent to a recovery of the consideration paid by him, must return or tender a return of the property received under the contract, if it still remains in his hands.¹³ In Indiana, however, no such condition precedent is required. The infant may disaffirm his subscription contract without returning or tendering the return of the stock which he has purchased, even though he still has the same in his possession.¹⁴ Upon such

¹⁰ *White v. New Bedford Cotton Waste Corporation*, 52 N. E. 632 (Mass. 1899.)

¹¹ *Rice v. Boyer*, 108 Ind. 472, 9 N. E. 420, 58 Am. Rep. 53 (1886); *Shipley v. Smith*, 162 Ind. 526, 70 N. E. 803 (1904); *Childs v. Dobins*, 55 Iowa 205, 7 N. W. 498 (1880); *Robinson v. Weeks*, *op. cit. supra* note 5; *Chapin v. Shafer*, 49 N. Y. 407 (1872).

¹² *Pitcher v. Laycock*, *op. cit. supra* note 7.

¹³ See Note to *Wuller v. Chuse Groc. Co.*, in 16 Ann. Cas. 522.

¹⁴ *Pitcher v. Laycock*, *op. cit. supra* note 7; *Miles v. Lingerman*, 24 Ind. 385 (1865); *Briggs v. McCabe*, 27 Ind. 327 (1866); *Carpenter v. Carpenter*, *op. cit. supra* note 5; *State ex rel. Hutson v. Joest*, 46 Ind. 235 (1874); *Towell v. Pence*, 47 Ind. 304 (1874); *Dill v. Bowen*, 54 Ind. 204 (1876); *Clark v. Van Court*, *op. cit. supra* note 4; *Shirk v. Shultz*, *op. cit. supra* note 5; *Shipley v. Smith*, *op. cit. supra* note 11; *Story & Clark Piano Co. v. Davy*, 68 Ind. App. 150, 160 (1918).

disaffirmance, however, the title to such stock, if the same has not been alienated by the infant, reverts to the vendor and the vendor may thereupon bring an action for the cancellation of the stock or an action in replevin for its return.¹⁵

Whether or not the return of the stock or a tender thereof, when the same remains in the possession and ownership of the infant, should be a condition precedent to a recovery of the consideration paid by the infant might well be a matter for discussion. In one sense the result is the same, that is, the infant must eventually return any stock still remaining in his hands. The requirement of such a condition precedent, however, prevents a multiplicity of suits. All the rights of the parties are then determined in one action, because the infant must show, before he is entitled to a recovery, that he has returned or offered to return all of the stock remaining under his control. Where no such condition precedent is required, the vendor must commence a separate action against the infant to recover the stock which he still retains, the title to which has become revested in the vendor by the minor's act of disaffirmance. But even in Indiana, the minor must tender a return of the stock, if he seeks the aid of a court of equity to obtain the cancellation of his contract. Equity will not permit him to retain the benefits thereof and at the same time relieve him of all liability thereon.¹⁶ Here a distinction is made between the case where the minor invokes the equitable powers of the court to cancel his stock subscription contract and the case where the minor comes into court to seek the return of the consideration paid by him upon a stock subscription contract, which he has already avoided by a previous act of disaffirmance. In the latter case the contract is already rendered void and the minor merely seeks the return of the property to which he is given a legal right by his previous disaffirmance.

The right of an infant to avoid a contract for the purchase of corporate stock is an absolute and paramount right,

¹⁵ *Carpenter v. Carpenter*, *op. cit. supra* note 5; *White v. Branch*, *op. cit. supra* note 5; *Shirk v. Shultz*, *op. cit. supra* note 5.

¹⁶ *Pitcher v. Laycock*, *op. cit. supra* note 7; *Miles v. Lingerman*, *op. cit. supra* note 14.

superior to all equities of other persons.¹⁷ Neither will conditions arising after the purchase of the stock by the infant affect his right to disaffirm the contract upon reaching his majority. He may recover the price paid for the stock without any allowance for depreciation in the capital of the corporation.¹⁸

The disaffirmance of the contract by the infant renders it void from the beginning, and the parties thereto are thereby returned to the same relative positions which they occupied before the contract was made.¹⁹ As shown in the above quotation from *Carpenter v. Carpenter*, after disaffirmance, the parties are left to seek relief in the same modes and with the same changes of loss as in any other case where an owner seeks the return of property held by another. If the minor has sold or squandered the property which he received, no recovery can be had by the other party, and, if the corporation or vendor in the meantime has become bankrupt or insolvent, the infant has only a general claim against the bankrupt or insolvent estate for the return of the consideration paid by him, unless preference to such claim can be given without prejudice to the rights of creditors. In the words of the Supreme Court of Iowa:

"Whether a trust existed in favor of either of these parties as against the corporation is not decisive of the right to a preference in the distribution of the funds. There must be some showing that the estate has been augmented by the trust fund, or, at least, that the estate has been so benefited by the misappropriation of the trust fund that the removal of its equivalent from the estate will be without prejudice to creditors."²⁰

Ordinarily the infant cannot follow money, which he has paid for the purchase of stock, into the hands of a third person. In such case he has only a claim against a corporation or the vendor of the stock. Even the recovery of money was allowed in one case from a third person, a bank to which the

¹⁷ Gage v. Menczer, *op. cit. supra* note 5.

¹⁸ Godfrey v. Mutual Finance Corporation, *op. cit. supra* note 5.

¹⁹ Shrock v. Crowl, *op. cit. supra* note 7; Rice v. Boyer, *op. cit. supra* note 11.

²⁰ Seeley v. Seeley-Howe-LeVan Co., *op. cit. supra* note 5.

vendor had paid the money in satisfaction of his own debt to the bank, where it was shown that the bank had notice that the money was received from the sale of such stock to the minor.²¹ Where the infant transfers other personal property in consideration for the stock purchased, upon disaffirmance of his contract, he will be permitted to follow such property and recover the same from a third person to whom it has been transferred, even though such third person be an innocent purchaser for value.²² The act of disaffirmance makes void the title of the other contracting party to such property and the title of the third person is thereby also rendered void. The third person can receive no better title than was in his vendor.

Where corporate stock has been transferred to a minor, a question frequently arises as to whether or not the liabilities of a stockholder are thereby removed from the transferor and imposed upon the infant. Here we find the general rule to be that the transferor is not relieved from liability to creditors, even though the corporation was solvent when the transfer was made, unless, in the meantime, the infant has attained his majority and ratified the transfer. This rule is placed upon the ground that the transferor cannot relieve himself from liability unless the transfer is made to one capable of assuming the liabilities of a stockholder and to one who cannot subsequently repudiate such liabilities.²³ In the case of *Foster v. Lincoln et al.*,²⁴ the court held that a voluntary transfer of national bank stock to minors did not relieve the transferor of his statutory liability as a stockholder, since he knew at the time of the transfer that the bank was in a precarious condition. The acquiescence of the national bank in such a transfer is of no avail to the transferor, since the officers of the bank have no power or authority to waive the statutory liability placed upon stockholders of national banks.²⁵

²¹ Gage v. Menczer, *op. cit. supra* note 5.

²² Craig v. Van Bebber, 100 Mo. 584, 18 A. S. R. 569, note 661 (1890).

²³ 6 FLETCHER, ENCYCLOPEDIA OF CORPORATIONS, § 4203, and cases cited.

²⁴ 74 Fed. 382 (1896).

²⁵ Aldrich v. Bingham, 131 Fed. 363 (1904).

Another situation which frequently arises is the case where an adult purchases stock in the name of an infant. In such case the contract is really between the adult and the corporation. It is simply the case of a contract between two parties, capable of contracting, made for the benefit of a third person, who is an infant. In such case the infant has no right to avoid the contract.²⁶ A father buying stock in a national bank assumes the statutory liability as a shareholder, even though the stock is purchased in the names of his minor children, because the consent of such minors does not render them absolutely liable as stockholders. They may at any time, before or after reaching majority, repudiate such liability.²⁷ The liability of the father in such case will not be affected, even though, after the assessment is made, but before suit is brought thereon, the minor becomes of age and ratifies the purchase of the stock in his name.²⁸

A trustee, however, may hold stock in a national bank for the benefit of minors and, in such case, the trustee is not personally liable for the statutory assessment against stockholders.²⁹ This decision is based upon the express provisions of our Federal Act,³⁰ which expressly provides that in such case the trustee shall not be personally liable, but the liability shall attach to the trust fund or estate in his hands as such trustee. In such case, of course, there is no personal liability upon the minor.

There still remains the question of dividends upon stock held by minors. Where the corporation or the vendor has dealt with an adult, presuming to act in the name of a minor, there can be no question in this regard. The corporation must pay the dividends to whomsoever the adult designates, since there is no possibility of a subsequent disaffirmance by

²⁶ *Winkler v. Los Angeles Investment Co.*, 43 Cal. App. 408, 185 Pac. 312 (1919); *Stumpf v. Halstead Land, etc., Co.*, 59 Misc. 529, 110 N. Y. S. 838 (1908); *Stettheimer v. Wood Harmon Richmond Realty Co.*, 167 N. Y. S. 1059 (1918).

²⁷ *Foster v. Chase*, 75 Fed. 797 (1896).

²⁸ *Foster v. Wilson*, 75 Fed. 797 (1896).

²⁹ *McNair v. Darragh*, 31 Fed. (2d.) 906 (1929) (*Certiori* denied, *Gamble v. Darragh*, 50 S. Ct. 19).

³⁰ 12 U. S. C. A. § 66.

the minor for whose benefit the contract was made. Neither can the corporation refuse to pay dividends upon stock purchased by the minor in his own name. The infant may bring suit upon a contract entered into with him personally to enforce liability assumed therein by the party with whom the contract was made.³¹

"Whenever a party enters into a contract with a minor personally, or purchases property of him, or deals with him or on his account, such party must respond to him in an action the same as though he was an adult. So in all cases when an infant has the possession and control of his property he may bring his action for its conversion for any damage or injury to it the same as though he was of full age."³²

The disaffirmance of the contract for the purchase of stock, as stated above, relates back to the time of the purchase and renders the contract void from its inception. Theoretically, therefore, the corporation, which has sold stock direct to a minor, is revested with title to the dividends paid during the period between the time of purchase and the time of disaffirmance. Practically, however, this revesting of title is of little consequence, since dividends are nearly always paid in cash, which cannot be recovered. The decided cases afford little help in a discussion of this question. In fact, only a very few of the decisions refer to dividends at all. This is perhaps largely due to the fact that, in most instances, the minor repudiates his contract for the reason that no dividends have been received upon the stock. No one objects to assuming the responsibility of a stockholder so long as he receives dividends on the stock, which makes the ownership thereof profitable. It is only when the dividends cease and the liabilities become actual that an attempt is made to avoid the contract of purchase. In the case of *Indianapolis Chair Manufacturing Co. v. Wilcox*,³³ a dividend was declared while the stock was held by the infant,

³¹ TYLER, INFANCY AND COVERTURE (2nd. ed.), 200.

³² TYLER, *op. cit. supra* note 31, at 193.

³³ *Op. cit. supra* note 5.

but the right to retain such dividend was not considered. A dividend had also been paid to the minor on the stock involved in the case of *Godfrey v. Mutual Finance Corporation*,³⁴ but the plaintiff in that case offered to return the dividend received, so no issue on that score was raised or decided. The corporation, however, has a right to demand the return of a stock dividend which has been issued to the minor, if the stock received as such dividend has not been transferred by him. This is in accordance with the general rules regarding the rights of the parties upon disaffirmance.

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³⁴ *Op. cit. supra* note 5.