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PREFERRED STOCK.

A VERY important branch of modern corporation law, viz.: the law of Preferred Stock, naturally divides itself into two parts, which we shall treat in their order. (1.) The power of corporations to issue preferred stock. (2.) The rights of the holders ot preferred stock.

I. THE POWER OF CORPORATIONS TO ISSUE PREFERRED STOCK.

Preferred shares, are those the owners of which are entitled to profits to a certain extent in preference to other shareholders. The holders of such shares are not creditors of, but stockholders in, the company. They differ from other shareholders only in being entitled, as against them, to payment of dividends in priority to them. Preferred, preference, preferential or guaranteed shares, as they are indifferently called (*Henry* v. *Great Northern Railroad Co.*, 4 K. & J. 1), are usually issued by companies who have expended their original capital, for the purpose of obtaining further capital, and therefore where the authority to issue preference stock is given it is necessary that it shall be employed for that purpose alone, and the company cannot, for example, pay dividends with such stock: *Hoole* v. *Great Western Railroad Co.*, L. R., 3 Ch. 262. The issue of preferred stock cannot be justified except for the purpose of strengthening the company's standing or enlarging its business. The corporation has reached a crisis in its affairs; the stockholders are unable or unwilling to sink more money in the enterprise, but yet are ready to give to those who will do so a preference in any profits which the increased means may enable the concern to make. These considerations render the transaction fair and equitable; *Lockhart* v. *Van Alstyne*, 31 Mich. 76. A distinction, it should be observed, is made by the courts between dividends or interest upon preferred stock and upon common stock, and it is this: that, as to the latter, their declaration is discretionary with the directors, while, as to the former, the question of ability to pay will be decided by the court, and the decision of the directors is not conclusive: *Barnard* v. *Vermont, &c., Railroad Co.*, 7 Allen 512; *Bryant* v. *Ohio College*, 1 Cin. 67; *Dickinson* v. *Railroad Co.*, 7 W. Va. 390; *King* v. *Ohio, &c., Railroad Co.*, 9 Rep. 431; *Furness* v. *Caterham Railroad Co.*, 25 Beav. 614; *Chase* v. *Vanderbilt*, 37 N. Y., S. C. (5 J. & S.) 334.

If the power so to discriminate be reserved in the charter or by-laws, and so incorporated into the original contract, or if the discrimination be made with the first issue of stock by creating, *at that time*, two or more classes of stock, such procedure would, on familiar principles, be legal: *Kent* v. *Quicksilver Mining Co.*, 78 N. Y. 159. But where the company has been organized and the stock issued and taken up on a certain basis, it is obvious that rights which have thereby attached cannot be impaired except for good reasons and by virtue of proper authority. The shares of stock issued by a corporation are in the nature of *choses in action*, and give to the holder a fixed right to a proportion of the profits of the association while it is a going concern, and to a share of its assets after dissolution. They constitute a contract between the corporation and the subscriber. Therefore, where a corporation has issued the full amount of stock called for by its charter or by-laws, and such stock has all been taken up, the dividing the shareholders into classes, and giving some a preference over others in the earnings of the association without the consent of the deferred shareholders, is an impairment of the vested rights of the latter, a violation of the obligation of the original contract, and hence illegal: *Kent* v. *Quicksilver Mining Co.*, 78 N. Y. 159. In an English case (*Hutton* v. *Scarborough Cliff Hotel Co.*, 2 Dr. & Sm. 514; s. c. 4 DeG., J. & S. 672) where, without any authority, the directors had, by resolution at a general meeting, issued a number of preference shares, the vice-chancellor, in granting an injunction at the suit of these shareholders, who had notice of but did not attend the meeting, stated the law very clearly. "I think it is clear," he said, "that this is a case for an injunction. There is a memorandum of association which prescribes that the capital of the company shall be 120,000*l*., to be divided into 12,000 shares, of 10*l*. each. In the articles of association there are provisions in regard to the payment of the dividends, that they shall not be paid out of capital, and that when dividends are paid to the shareholders they are to be in proportion to the shares which they hold. So that when any person takes a number of shares in this company a contract is entered into between him and the general body of shareholders, to the effect that all those who have taken or shall take any of the 12,000 shares shall have a ratable dividend, whenever there is a dividend, in proportion to their respective shares. This is the contract between the parties. The question then really comes to this: can the majority of the shareholders, in order to induce persons to take some of these 12,000 shares, which are not yet issued, authorize the directors to make an arrangement for giving to them, not that which all the existing shareholders contracted should be given, viz.: a dividend in proportion to their shares, but a preferential dividend, so that every one who has contracted that he shall have a proportionate dividend with all those who take any of the 12,000 shares will no longer have a proportionate dividend, but his dividend will not be paid at all or at least suspended, until other persons who shall have been induced to take some of these 12,000 shares shall have been paid their dividend in full? That is a clear breach and violation of the contract which the parties entered into. It is not necessary that there should be a case of fraud in the moral sense of the term. It is a breach of contract, and that the directors have no right to commit."

Though it is sometimes said that the issue of preferred stock may derive validity from the power to borrow money, secured by a pledge of income, it has been distinctly held in a recent case that a scheme by which the holders of common stock might convert it into preferred stock by the payment of a specified sum could not be justified by virtue of this inherent power. "The idea of borrowing," said the court, "is not filled out unless there is in the agreement therefor a promise or understanding that what is borrowed will be repaid or returned: the thing itself, or something like it, of equal value, with or without compensation for the use of it in the meantime. To borrow is the reciprocal action with to lend; and to lend or to loan, say the dictionaries, is the parting with a thing of value to another for a time fixed or indefinite, yet to have sometime an ending, to be used or enjoyed by that other, the thing itself or the equivalent of it, to be given back at the time fixed or when lawfully asked for, with or without compensation for the use, as may be agreed upon. In this transaction with some stockholders that corporation had not the right nor was it under the liability to ever pay back the five dollars per share furnished by them to it; that was not named in the terms of the obligation given, nor was it contemplated in the negotiation and bargain. The stockholder had not by the scope of his bargain, nor by the terms of the written evidence of it, any right ever to ask for repayment of the money furnished by him. In short, there was not formed thereby the relations of debtor and creditor. The stockholder parted for ever with the money furnished, inasmuch as the charter of the company is perpetual, and the company made a perpetual charge upon its net earnings. Though there was a compensation fixed for the use of the money, and though it was to take the form of a yearly payment, and at a rate the same as the then lawful rate of interest, yet we cannot conceive that the transaction was a loan and borrowing of money with a compensation for the use of it. * * * The transaction is not to be looked upon as other than a preference of one class of stockholders to another; as giving to the first class a perpetual inextinguishable prior right to a portion of the earnings of the company before the other class might have anything therefrom:" *Kent* v. *Quicksilver Mining Co.*, 78 N. Y. 159. It will be seen that here was no actual borrowing of money, but the issue of preferred stock was not passed upon, and consequently we are prepared to find cases in which preference stock has been considered good under this power. Thus it has been held that where such stock was secured by bond and mortgage, the holders being expressly prohibited by statute from being members of the corporation (*Burt* v. *Rattle*, 31 Ohio St. 116), where the preferred stock was surrendered and a bond and mortgage taken in its stead, the preferential shareholders thereafter not being entered as members of the corporation (*Totten* v. *Tison*, 54 Ga. 139), where there was a provision for the redemption of the stock (*Westchester, &c., Railroad Co.* v. *Jackson*, 77 Penn. St. 321), and where there was a condition for payment of interest until the company should go into operation (*Richardson* v. *Vermont, &c., Railroad Co.*, 44 Vt. 613)—in all these cases the proceedings were adjudged not *ultra vires*, being looked upon as being in the nature of loans. And see *Rut-*

land, &c., Railroad Co. v. *Thrall*, 35 Vt. 536; *Hazlehurst* v. *Savannah, &c., Railroad Co.*, 43 Ga. 13.

As we have said, corporations cannot create preferred stock without power to do so. In England the judges look to the different statutes in which the powers and obligations of corporations are defined. The Act of 1845 (8 & 9 Vict. c. 16) gave no such authority, according to the better opinion (*Sturge* v. *Eastern Union Railroad Co.*, 7 DeG., M. & G. 158; *Fielden* v. *Lancashire, &c., Railroad Co.*, 2 DeG. & Sm. 531; *Matthews* v. *Great Northern Railroad Co.*, 28 L. J. (Ch.) 375; *In re National Patent Steam Fuel Co.*, 4 Drew. 529; Green's Brice's Ultra Vires 165–167; Lindley on Part. 621); neither did the Company's Acts of 1862 and 1867, nor the Company's Clauses Act of 1863 (26 & 27 Vict. c. 118). (See the act and Lindley on Part. 617.) Mr. Brice (Ultra Vires 170) states that by this act preference shares might be created, but this is evidently a mistake. Notwithstanding the large powers given by the Company's Act of 1862, corporations cannot issue preferred shares unless their articles as originally framed so authorized; *Hutton* v. *Scarborough Cliff Hotel Co.*, 2 Dr. & Sm. 514; *Moss* v. *Syers*, 32 L. J. (Ch.) 711. And power to issue a certain number cannot be extended to validate the issue of a greater number: *Melhado* v. *Hamilton*, 28 L. T. (N. S.) 578; 29 Id. 364.

The Railway Company's Act (1867, 30 & 31 Vict. c. 127, §§ 6–17) provides that where a company are unable to meet their engagements, the directors may prepare a "scheme or arrangement" with their creditors which must be assented to by three-fourths of the mortgagees and holders of bonds, debenture stock, &c., and confirmed by the Court of Chancery. Under the powers here conferred, as well as by direct application to Parliament, the following schemes, including the issue of preferred stock, have been adopted by derelict corporations: That each shareholder who had paid one-half the amount of his shares might convert each share into two half shares, the one-half fully paid up to be denominated "deferred half share," the other half to be denominated "guaranteed half share;" the whole of the dividends which would in each year have accrued to be applied towards the payment in the first place of interest or dividend at the rate of 6*l.* per cent. per annum upon the "guaranteed" half share, the remainder, if any, to be payable on the "deferred" half share; provided, the company should not pay any other or greater amount of interest or dividend upon the two half shares than was for the time being paid on each dividend share: *Matthews* v. *Great Northern Railroad Co.*, 28 L. J. (Ch.) 375. That the company's capital of 650,000*l.*, divided into 65,000 shares of 10*l.* each, should be increased by the issue of 25,000 new shares at 10*l.* each, such shares being preference shares, with such amount of preferential dividend, and with or without a power of redemption, and with or without the option within a specified time of turning the preference shares into ordinary stock: *Webb* v. *Earle*, L. R., 20 Eq. 556. That there should be five sorts of preference shares, some with a "preferential dividend" out of working profits, others with "preferential dividends," and others with a "preferential interest or dividend:" *Corry* v. *Londonderry, &c., Railroad Co.*, 29 Beav. 263. That the company should create certain amounts of debenture "A" stock and debenture "B" stock; debenture "A" stock to be applied first in payment of the mortgage debentures of the company, the stock applied to those purposes having priority in payment of interest over the residue of that stock, which residue was to be applied in paying unpaid vendors of land. Debenture "B" stock to be applied in paying off debentures, not mortgages, and other debts, and the income of the company to be applied in paying (1) rent charges; (2) interest on preferred debenture "A" stock; (3) interest on the residue of the stock; (4) interest on debenture "B" stock; (5) dividends to shareholders: *Stevens* v. *Midhants' Railroad Co.*, L. R., 8 Ch. 1064; and see *Re Bristol, &c., Railroad Co.*, L. R., 6 Eq. 448; *Re Devon, &c., Railroad Co.*, Id. 610–615; *London Financial Association* v. *Wrexham, &c., Railroad Co.*, L. R., 18 Eq. 566; *Munns* v. *Isle of Wight Railroad Co.*, L. R., 8 Eq. 655: *Re East & West Junction Railroad Co.*, Id. 87; *Re Potteries, &c., Railroad Co.*, L. R., 3 Ch. 67; *Re Cambrian Railroad Co.*, L. R., 3 Ch. 278.

Preference stock is frequently, as has been seen, authorized by statutory provisions or by the charter or articles of the corporation (*Matthews* v. *Great Northern Railroad Co.*, 28 L. J. (Ch.) 375; *Henry* v. *Great Northern Railroad Co.*, 1 DeG. & J. 606; *Taft* v. *Hartford, &c., Railroad Co.*, 8 R. I. 310; *St. John* v. *Erie Railroad Co.*, 10 Blatchf. 271; s. c. 22 Wall. 136; *Davis* v. *Proprietors*, 8 Metc. 321; *Re Anglo-Danubian Steam Navigation Co.*, L. R., 20 Eq. 339), and in such cases no question as to the *power* to issue it can be raised, and *a fortiori* where the issue was agreed to by all the shareholders: *Prouty* v. *Michigan, &c., Railroad Co.*, 1 Hun 655. The legislative authority may be given subsequent to the organization of the corporation (*Rutland, &c., Railroad Co.* v. *Thrall*, 35 Vt. 536; *City of Covington* v. *Covington, &c., Bridge Co.*, 10 Bush 69; *Midland Railroad Co.* v. *Gordon*, 16 M. & W. 804), and it has been held in a Georgia case, that preferred stock was valid where the amount of the authorized capital stock had not been reached and the preferential shares were issued from the remainder: *Hazlehurst* v. *Savannah, &c., Railroad Co.*, 43 Ga. 13. This is not a well-considered case; the judge who delivered the opinion, though admitting that the question was a new one and the doctrine not well established, declined to discuss them upon principle. It plainly conflicts with *Hutton* v. *Scarborough Cliff Hotel Co.*, 2 Dr. & Sm. 514, and lacks its authority. In England the issue of such stock is lawful where power is given in the articles of association to increase the capital stock by the issue of new shares, leaving to the discretion of the company the manner of raising and the amount and value of such stock: *Harrison* v. *Mexican Railroad Co.*, L. R., 19 Eq. 358.

Though the power must be clearly given it need not be in exact words, but it must be apparent; thus a right at a special meeting to increase the capital of the company by the issue of new shares, to be of such nominal value and subject to such conditions as to payment of calls or proportion of profits as may be determined, would not authorize the issue of preferred stock: *Moss* v. *Syers*, 32 L. J. (Ch.) 711. Therefore, in *Harrison* v. *Mexican Railroad Co.*, L. R., 19 Eq. 358, the power was implied from the use of words of wide signification. The company's memorandum of association declared that the capital was 2,700,000*l.*, divided into 135,000 shares of 20*l.* each, and provided that the directors might, with the sanction of a special resolution of the company, previously given in general meeting, increase the capital by the issue of new shares, each increase to be made in such manner, to such amount and to be with and subject to such rules, regulations and conditions, as the company in general meeting should think fit. It was held by the Master of the Rolls that a special resolution authorizing an increase of the capital by the issuing of preferred shares was not *ultra vires* the company. "Words of larger import," said he, "could hardly be imagined. Yet it is said that the language is not sufficient to convey the power to authorize the shares which are issued for the purpose of increasing the capital to be issued with the privilege of having attached to them a preferential dividend. The capital is to be raised or to be increased 'in such manner and with and subject to such rules, regulations, privileges and conditions,' as the company may think fit. I can find no such limit either in the term 'privilege' or in the term 'condition' as has been suggested. It seems to me that they are words of extensive meaning, and fully ample to cover all that is proposed to be done. * * * I think that there is no limit to the privilege that may be attached to the shares by the general meeting so far as regards participation in dividends, or any other right whatever."

The issue of preferred stock may be acquiesced in, so as to bar the other stockholders from objecting, from their recognising it at corporate meetings: *Lockhart* v. *Van Alstyne*, 31 Mich. 76, and especially where it has passed into the hands of innocent holders: *Kent* v. *Quicksilver Mining Co.*, 12 Hun 53; s. c. 78 N. Y. 159; *Hoyt* v. *Quicksilver Mining Co.*, 17 Hun 169.

Some of the cases fail to present the direct question as to the power to issue preferred stock, and are consequently of no particular weight in this discussion. In *McLaughlin* v. *Detroit, &c., Railroad*, 3 Mich. 100, the power of the corporation to issue such stock was not questioned, but it was denied to reside in the president and treasurer. The court held that the corporation had ratified the act of the president and treasurer, and, as the point as to the power of the corporation to make the issue was not raised by counsel, did not pass on that question. In *Evansville, &c., Railroad Co.* v. *City of Evansville*, 15 Ind. 395, the contract was more favorable to the defendant than to the other shareholders, and the court said it would be inequitable to allow the former to set up the latter's prejudice to avoid the issue. In *Williston* v. *M. S., &c., Railroad*, 13 Allen 400, this point was not necessarily involved in the decision of the cause. So in *Bates* v. *Androscoggin Railroad*, 49 Me. 491, the opinion as to this question was *obiter*.

II. The Rights of Holders of Preferred Stock.

A dividend when spoken of in reference to a going concern means "a fund which the corporation sets apart from its profits to be divided among its members." * * * "A dividend among preference stockholders exclusively is understood to imply that the sum divided has been realized as profits, though the earnings do not yield a dividend to the stockholders in general:" COOLEY, J., in *Lockhart* v. *Van Alstyne*, 31 Mich. 76; *Taft* v. *Hartford, &c., Railroad Co.*, 8 R. I. 310. Such dividends are equivalent to annual or semi-annual payments, and, under the general form of certificate in such cases, depend on no contingency except that the net profits of the association shall be sufficient to pay them: *Bates* v. *Androscoggin, &c., Railroad*, 49 Me. 491. Therefore an express guaranty to pay a certain dividend on preferred stock entitles the holders only to such dividends when there are profits out of which they can be paid: *Lockhart* v. *Van Alstyne*, 31 Mich. 76; *Taft* v. *Hartford, &c., Railroad Co.*, 8 R. I. 310.

The right of the holders of preferred stock extends only to a priority as to dividends; as to assets or capital they stand in the same position as ordinary shareholders (*Re London India Rubber Co.*, L. R., 5 Eq. 510). So, interest or dividends must be paid only out of the profits actually earned, and any agreement to pay them out of the capital would be *ultra vires: MacDougall* v. *Jersey Imperial Hotel Co.*, 2 H. & M. 528; *Pittsburgh, &c., Railroad Co.* v. *Allegheny Co.*, 63 Penn. St. 126; *Lockhart* v. *Van Alstyne*, 31 Mich. 76; *Curran* v. *Arkansas*, 15 How. 304. Where the power was express, preference capital was issued by an English corporation, and its validity sustained: *Re Bangor, &c., Slab Co.*, L. R., 20 Eq. 59. In *Lockhart* v. *Van Alstyne*, 31 Mich. 76, it was held that an agreement by a corporation to pay annual dividends to preferred stockholders without reference to its ability to pay them from earnings was void, Mr. Justice COOLEY maintaining in a vigorous opinion that such contracts were opposed to public policy. Such a guaranty is a preference with a perpetual promise to pay interest, profits or no profits; the holders having all the advantages of stockholders and creditors, while their associates are postponed as stockholders, and considered as representing the debtor corporation; they are deprived by the very terms of the contract of any reasonable probability of restoring its standing and strength, when once it shall have ceased to be prosperous. To agree to pay dividends from profits when there are any, and from capital when there are none, is like the promise of a debtor to pay from his gains, if his ship comes in, from his pound of flesh if it does not—every dividend from the capital being an attack on the life of the corporation which must eventually kill it. Another consideration arises from the relations of the stockholders, ordinary and preferred. Both have an equal right to participate in the management of the corporation, and from both classes the officers may be chosen—but the larger may by a combination obtain entire control. The earning of dividends by a corporation, depends on many circumstances both of internal management and public events, which even prudence cannot always foresee, but depends above all, on the fidelity and integrity of its officers. Therefore, such a contract is a guaranty that this fidelity and integrity shall produce dividends; but if the officers are preference stockholders, then we have the corporation guaranteeing to them their own integrity and fidelity, and undertaking to make up to them from its capital, whatever in expected results that management may fail to realize. Still other anomalous results follow. Harmony among the stockholders, preferential and common, is essential to success. If the preference extends only to a division of profits, their interests are the same; but if it extends beyond that, they become at once antagonistic. The preferred stockholder wishes to keep the failing concern in existence until his dividends have wholly exhausted its means; the common stockholders desire to hasten a dissolution, because then the dividends will cease and the assets be divided. The whole capital and assets will be at issue at every election; the one class anxious to dissolve the corporation, though its objects have not been realized; the other anxious to tie up its assets, so that its objects may not be accomplished. Legislation could never have intended the former result; public policy must be opposed to placing its capital where it cannot be productive, in order that debts may accrue to absorb it. "A contract," concludes Judge COOLEY, "the necessary construction of which would lead or tend to the consequences pointed out; which would require dividends, when honesty and good faith to the public would forbid, and public opinion condemn them; which would antagonize the positions of different classes of men engaged in the same joint undertaking, and preclude harmony of action and union of effort, precisely under those circumstances when harmony and union would be most essential; under which the corporation making it, must almost inevitably be destroyed unless it should enjoy continuous prosperity; and which, under some circumstances, would make one class of persons having a voice in the control and management of the corporation; interested in so controlling its means, as to keep them as long as possible in an unproductive condition, until, by a slow process, they can absorb them to the prejudice of their associates—must necessarily be opposed to public policy and void."

To what extent, if at all, arrears in one year must be made up from profits earned in subsequent years, has been discussed in *Henry* v. *Great Northern Railway Co.*, 1 DeG. & J. 606. By a special statute, the company were empowered "to guarantee the payment of dividends, not exceeding in any case seven per centum per annum, on any particular shares which the company may be authorized to issue, in preference to the payment thereof on the ordinary shares of the company, and upon such terms as shall be by the resolution of such meeting defined; provided always, that any preference shares which shall have been already issued by the company, shall have a preference or priority of dividend over the shares so guaranteed as aforesaid; and all preference shares shall have priority of dividend, according to the date at which such shares shall have been issued." At two meetings of the company preference shares were issued, the resolution providing, that they should bear "5*l.* per cent. interest or preference dividend in perpetuity." In the Court of Chancery, the question arose whether there attached to these preference shares, a right to be paid out of the profits of the company whenever the profits should accrue; and if the sum to be divided at any period of distribution was insufficient to pay in full the dividends on such shares, the holders were entitled on the next declaration of dividend, to receive the arrears unpaid as well as the new dividend. The vice-chancellor decided in the affirmative, and his judgment on appeal, was held correct. "The difficulty," said the chancellor, "arises from the want of a specific and distinct definition as to the extent of the rights conferred on each particular class of shareholders, by way of preference. The plaintiffs say that the right of a shareholder who is entitled to a dividend by way of preference, is to receive his dividend out of all profits from time to time accruing, and to carry over his demand for any unpaid arrears to all subsequent divisions of profit. The defendants say, that he has no right upon any fund save that actually under distribution; and that, if that fund is insufficient to satisfy him, he has no claim on any subsequent profits. The expression 'preference shareholder,' is equivocal. * * * All which the language fairly imports is, that some preference is given to the persons to whom the language applies. How far the preference is to extend, must be ascertained by other media than the mere expression itself. It was argued, that the word 'dividend' must be taken *ex vi termini*, to apply merely to the one fund to be divided, and that it could not in its true meaning, be extended to any fund afterward to be brought into division. But it must be observed, that the word 'dividend' as used in this and similar cases, is never used with strict accuracy, if strict accuracy depends upon its primary meaning. The word 'dividend,' if we look to its derivation, means obviously the fund to be divided, not the share of any particular partner or person in that fund; and strict language would require us to speak not of the dividend which any shareholder receives, but of his aliquot portion of the dividend. * * * We must construe the word 'dividend' in a secondary sense, and not according to its strict, original meaning. And acting on this view of the case, I have come to the conclusion, that what these statutes, in fact, guarantee to the favored stockholders is a charge on all accruing profits at the stipulated rate, before anything is divided among the ordinary shareholders." And KNIGHT BRUCE, L. J., said: "The word 'dividend' carries no spell with it. Applicable to various objects, it is not intelligible without knowing the matter to which it is meant as referring, and, of course, where there is a context, it is liable to be affected by that context. * * * The expression, where we have to consider it, seems to me correctly used in a large and general sense, as between or amongst the stockholders and shareholders, in respect of time and profits. A., B. and C. are partners in a trade, each having contributed an equal share of capital, but they agree that out of the profits, *5l.* per cent. per annum shall preferably, and in the first instance, be paid to A. on his portion of the capital. The division of the profits among them is agreed to be and is periodically made. At one of the periodical divisions, the profits fall short of a sufficiency to pay this amount to A., from the time to which, out of the profits his interest had previously been paid. Is the deficiency not afterwards to be made good to him from profits more than adequate to answer it? If, indeed, such a thing is prohibited by the terms of the contract, they must of course be abided by. Is there any such prohibition in the present instance. As it seems to me clearly not." The defendant's counsel having likened the right of a preference shareholder to the right to bring a cup of a certain measure to be filled at each dividend meeting, if there was enough to fill it, "I may be excused," said KNIGHT BRUCE, L. J., "for suggesting another case. Let us suppose a right to have a tun of wine from a vineyard. Is that the same merely as a right to have a tun of wine from a vintage? I do not think so. In the former case, the deficiency of an earlier would have to be supplied by a later vintage; not so possibly in the other. Here, as I apprehend, the plaintiffs have the vineyard, and not merely the chance of a particular vintage to look to."

In *Matthews* v. *Great NorthernRailway Company*, 28 L. J. Ch. 375, an act of Parliament provided that any shareholder who should have paid up one-half the amount of any share or shares of the company might convert each share into two half shares, whereof the one-half was fully paid up to be denominated "deferred half share," and the other half "guaranteed half share;" that thereafter the whole of the interest and dividends which would in each year have accrued, should be applied in the first place to the payment of interest or dividend at the rate of 6*l.* per cent. per annum on the amount paid upon the half share denominated "guaranteed," and the remainder, if any, should be applied to the half share denominated "deferred." Following *Henry's case*, WOOD, V.-C., held that the holders of the guaranteed half shares were entitled to be paid their 6*l.* per cent. in each year, not only out of the dividends accruing in that year, but out of all subsequent dividends, and therefore, that if in any year the dividends were more than sufficient to pay 6*l.* per cent. on the guaranteed half share, the surplus should be first applied to the payment of all arrears due on those half shares, before any dividend was declared on the deferred half shares. And see *Sturge* v. *Eastern, &c., Railroad Co.*, 7 DeG., M. & G. 158; *Webb* v. *Earle*, L. R., 20 Eq. 556; *Crawford* v. *North Eastern Railroad Co.*, 3 K. & J. 723; *Stevens* v. *South Devon Railroad Co.*, 9 Hare 313; *Corry* v. *Londonderry, &c., Railroad Co.*, 29 Beav. 263, where it was expressly provided as to some and not as to others that they should be so paid: *Coates* v. *Nottingham, &c., Railroad Co.*, 30 Beav. 86; *Smith* v. *Cork, &c., Railroad Co.*, Ir. L. R., 3 Eq. 356; 5 Id. 65; *Coey* v. *Belfast, &c., Railroad Co.*, Ir. Rep., 2 C. L. 112.

But by the Companies Clauses Act of 1863 (26 & 27 Vict. c. 16, § 14), it is provided that preference shares or stock shall be entitled to the preferential dividend or interest assigned thereto out of the profits of each year in priority to the ordinary shares and stock of the company; but if in any year there are not profits available for the payments of the full amount of the preferential dividend or interest for that year, no part of the deficiency shall be made good out of the profits of any subsequent year or out of any other funds of the company.

In this country the English rule, before the passage of the statute (26 & 27 Vict. c. 168 *ante*), is adhered to: *Lockhart* v. *Van Alstyne*, 31 Mich. 76; *Taft* v. *Hartford, &c., Railroad Co.*, 8 R. I. 310; *Prouty* v. *Michigan, &c., Railroad Co.*, 1 Hun 655.

Where each share in a company was converted into two half shares, one preferred, the other deferred, and the holders of the preferred half shares had, in a former year, acquiesced in the declaration of a dividend on the deferred half shares, while there was an arrear of dividends due on the guaranteed half shares, it was held, by WOOD, V.-C., that although they had precluded themselves from making any claim in respect to those particular arrears they had not waived their rights as to subsequent arrears: *Matthews* v. *Great Northern Railroad Co.*, 28 L. J. (Ch.) 375; *Smith* v. *Cork, &c., Railroad Co.*, Ir. L. R., 3 Eq. 356; 5 Id. 65.

Preferred stockholders have no control over the corporation which is not enjoyed by common stockholders, the difference between them is simply this, that the one class is to be first paid out of a certain fund to the exclusion of the other, if that fund be inadequate to pay both. The corporation is no more a trustee for the holders of preferred stock than for the holders of common stock, and consequently the former have no right to complain of acts of the directors, which simply make it less likely that the particular fund from which they expect to be paid will prove sufficient to satisfy their claims. Therefore the execution of a mortgage upon the whole line of a railroad for the purpose of raising funds for the company, and subsequent to the issuance by the corporation of preferred stock, is not in derogation of the rights of the preference shareholders, and an injunction will not issue to restrain the execution of such mortgage: *Garrett* v. *May*, 19 Md. 177; and so preferred stockholders who are entitled to receive interest in preference to the payment of dividends on the common stock, and after payment of the mortgage interest, are not to be considered prejudiced by the corporation issuing mortgage bonds consolidating prior and subsequent indebtedness: *Thompson* v. *Erie, &c., Railroad Co.*, 42 How. Pr. 68, 11 Abb. Pr. 188, s. c. 45 N. Y.

468. Where stockholders were allowed "interest on all sums paid by them," and some of the stockholders had paid the nominal value of the shares, while others had paid only part of such value, it was held, that under the language of the resolution, these latter should be allowed interest in proportion to the amounts paid in and not on the face value of their shares, and that the certificates of these shares should be reduced accordingly: *Richardson et. al.* v. *Railroad Co.*, 44 Vt. 613.

In *St. John* v. *Erie Railway Co.*, 10 Blatch. 271, 22 Wall. 137, preferred stock was entitled to preferred dividends "out of the net earnings of the road * * * after payment of mortgage interest and delayed coupons in full." Subsequent to the issue of this stock the company leased new roads, and borrowed money for the repair and equipment of the road, as it had power to do. The rent of the new road and the interest on this borrowed money, it was held in the Supreme Court of the United States, had priority over the preferred stock. Where the certificate of preferred stock provides, that after the payment of the guaranteed per cent., the preferred stockholders shall share in any surplus beyond a certain per cent., which may be divided upon the common stock, such preference shareholders are, after receiving their guaranteed per cent., to be deferred until the common shareholders have received their specified per cent., and then all stockholders are to be on the same footing as to any remaining surplus: *Bailey* v. *Railroad Co.*, 1 Dill. 174; s. c. 17 Wall. 96.

A preferential shareholder may file a bill to restrain the company from making a dividend prejudicial to his rights, without waiting until there are funds to make a dividend: *Sturge* v. *Eastern Union Railroad Co.*, 7 DeG., M. & G. 158.

Concerning the option which is often given to common stockholders to become preferential ones, on the surrender of a part of their shares or an additional payment, or the like, it is understood that any time limited is of the essence of the offer; and, therefore, where an option was given to registered shareholders to take a certain number of new shares before a specified time, it was held, that a shareholder who, living abroad, had no notice of the option until after the expiration of the time, could not then come in and demand to purchase any of the new shares: *Pearson* v. *London &c., Railroad Co.*, 14 Sim. 541. So also, where an option was given to convert loan notes into shares within a given time:

Campbell v. London, &c., Railroad Co., 5 Hare 519. And where, by the terms of a railroad bond, a time was fixed within which it might be converted into stock, if the holder so desired, an extension of the time of payment of the bond was held not to extend the time of the right of conversion: *Muhlenberg* v. *Philadelphia, &c., Railroad Co.*, 47 Penn. St. 16.

The decision of the court in *McGregor* v. *Home Ins. Co.*, 33 N. J. (Eq.) 181, concerning the *status* of the holders of preferred stock in the distribution of the capital on the winding up of the concern, in the absence of any statute designating how the assets are to be apportioned, is unquestionably the law. While the concern is going, if there be profits, the preference shareholders must be paid; if there be no profits, they get nothing, for they are not creditors but partners. On the dissolution of the corporation the profits cease; the only fund to which they have a right to go comes to an end. The capital remains, but as the preferred stockholders were prohibited from drawing on that while the corporation was in existence, so they are denied the privilege when it is defunct. *Re London India Rubber Co.*, L. R., 5 Eq. 519, in which this rule was first laid down by Vice-Chancellor MALINS is sufficiently set out in the opinion in the latest case, but we cannot refrain from quoting at more length from the admirable opinion of the Master of the Rolls in *Griffith* v. *Paget*, L. R., 6 Ch. Div. 511: "All these companies," said he, "are commercial partnerships, and are, in the absence of express provisions, statutory or otherwise, subject to the same considerations. If, in an ordinary commercial partnership, one or more of the partners has a larger share of the profits than is the proportion borne by his share of the capital to the capital of the others, whether on account of his services (which is the more frequent ground in cases of partnership for giving the larger share), or on account of the services of others formerly given to the partnership, which is sometimes done, especially in the case of a second or third generation, that privilege ceases when the partnership is dissolved. If you give an annuity out of profits to a widow during the continuance of the partnership, she having no share of the capital, of course that *ex vi termini* will come to an end at the dissolution of the partnership. If you give a managing partner a salary, or a larger share of profits than his proportion of the capital, of course, at the dissolution, the management comes to an end and his larger share of profits. But in the ordinary