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## The Problem of the Non-Exchanging Shareholder

### Cover Page Footnote

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# THE PROBLEM OF THE NON-EXCHANGING SHAREHOLDER

MARTIN E. GOLD\*

**T**HERE have been innumerable cases of corporate mergers, consolidations, and reorganizations requiring the holders of shares of predecessor corporations to exchange their certificates for ones of the successor or surviving corporation.<sup>1</sup> Most merger, consolidation, and reorganization agreements stipulate how the exchanges are to be accomplished, but many do not state how much time the shareholder has in which to make the exchange or what happens if no exchange is made. As a result, many corporations are forced to spend significant sums of money each year on these "lost" or "non-exchanging" shareholders,<sup>2</sup> maintaining records, paying transfer agents, sending out notices of meetings, and attempting to persuade such shareholders to exchange their shares and collect dividends that have accumulated. Problems are also likely to be found when the successor corporation wishes to merge or consolidate. Successor corporations, therefore, may have to spend substantial amounts on legal fees in attempts to determine how they can resolve problems concerning the non-exchanging shareholders.

It is clearly in the interest of the successor corporation to resolve the status of non-exchanging shareholders as soon as reasonably possible. Yet despite the costs, most firms maintain the non-exchanging shareholders' old "rights" and meet their claims whenever they are presented because the law is so uncertain in this area. In order to avoid

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1. Some of the reasons for having exchanges, including tax considerations and the desire to eliminate minority interests, are discussed in Fillman, *Cash and Property as Consideration in a Merger or Consolidation*, 62 Nw. U.L. Rev. 837, 838-44 (1968).

2. The term "lost" shareholders refers to any shareholders whom the corporation can no longer locate. In addition to problems they present in merger, consolidation, and reorganization situations, lost shareholders present particularly acute problems when the liquidation of the corporation is sought. A number of states have enacted dissolution legislation that provides for the placing of unclaimed property in general state funds or special school funds. Some states provide that the funds be deposited initially in a bank or with the state treasurer, but that they may be distributed after a certain time among the shareholders known at the time of dissolution. Other states give their courts almost complete freedom to determine what should be done with lost shareholder assets on liquidation. See Comment, *Unclaimed Dividends and Shares of Stock*, 46 Ill. L. Rev. 82, 85-86 (1951).

The term "non-exchanging" shareholders is adopted for the purposes of this Article to refer to those shareholders who, for whatever reasons, do not surrender their shares of stock when a corporate merger, consolidation, or reorganization calling for an exchange of these securities for new ones occurs, whether the corporation knows their whereabouts or not.

the risks of litigation and retain the shareholders' good will, many, perhaps most, firms make exchanges indefinitely and continue to incur the costs and the difficulties.<sup>3</sup>

Despite the continuing and obvious need for a solution, the problem has remained largely unsolved. This article will present the alternative approaches and problems that exist under present law, and offer a possible solution. Special attention will be paid to the relevant law of Delaware and New York, although cases addressing the problem of the non-exchanging shareholder in other jurisdictions will be considered.

### I. CORPORATION STATUTES

The state corporate law of Delaware and New York affords little specific assistance with the problem. Section 251 of Delaware's General Corporation Law, concerning mergers and consolidations, says:

The board of directors of each corporation which desires to merge or consolidate shall adopt a resolution approving an agreement of merger or consolidation. The agreement shall state: . . . (4) the manner of converting the shares of each of the constituent corporations into shares or other securities of the corporation surviving or resulting from the merger or consolidation . . . .<sup>4</sup>

The only other reference to exchanging certificates is made in section 260. That section gives the surviving corporation the power to "issue certificates of its capital stock and other securities to the stockholders of the constituent corporations in exchange or payment for the original shares . . . on the terms specified in the agreement."<sup>5</sup> Beyond this, Delaware's General Corporation Law is silent on the problem.

New York's provisions on the power<sup>6</sup> and requisite plan<sup>7</sup> of merger and consolidation are similarly inconclusive. The key paragraph simply says that the plan of merger or consolidation shall set forth:

The terms and conditions of the proposed merger or consolidation, including the manner and basis of converting the shares of each constituent corporation into shares, bonds or other securities of the surviving or consolidated corporation, or the cash or other consideration to be paid or delivered in exchange for shares of each constituent corporation, or a combination thereof.<sup>8</sup>

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3. Firms vary as to the amount of time and effort they expend in trying to communicate with lost or non-exchanging shareholders. Some simply mail material to the last known address, while others examine telephone directories, previously cashed checks, and bank records, or make inquiries with the public utilities. *See id.* at 83.

4. Del. Code tit. 8, § 251(b) (Supp. 1976).

5. *Id.* § 260 (1974).

6. N.Y. Bus. Corp. Law § 901 (McKinney 1963).

7. *Id.* § 902 (McKinney 1963 & Supp. 1976).

8. *Id.* § 902(3) (McKinney 1963).

We must, therefore, look elsewhere for guidance.

The only other corporate statute provisions that could be relevant are those that relate to so-called "dissenting shareholders." In both Delaware<sup>9</sup> and New York,<sup>10</sup> and virtually all other states, a record shareholder of a constituent corporation who objects in writing before the shareholders vote for a merger or consolidation has a statutory right to obtain the value of his shares from the resulting corporation.<sup>11</sup> The shareholder need not vote against the merger or consolidation to be considered a dissenting shareholder,<sup>12</sup> and if he was not given notice of the meeting, the written objection may not be required either.<sup>13</sup> The statutes of both Delaware<sup>14</sup> and New York<sup>15</sup> provide for court appraisal of the value of the shares.<sup>16</sup>

However, Delaware's dissenting shareholder statute is not applicable to a constituent corporation whose shares at the time of merger were listed on a national security exchange or held of record by more than 2,000 shareholders unless the certificate of incorporation provides

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9. Del. Code tit. 8, § 262 (1974 & Supp. 1976).

10. N.Y. Bus. Corp. Law § 623 (McKinney 1963 & Supp. 1976).

11. While virtually all states provide for a right of appraisal when a corporate merger or consolidation is accomplished pursuant to state statute, such a right is not uniformly conferred on shareholders who object to an exchange of the corporation's assets for the stock of another corporation, or when objection is made to other methods of combination. Whether or not a similar right of appraisal should be provided in sale-of-asset transactions and other nonstatutory combinations constituting de facto mergers is considered in Latty, *Some Miscellaneous Novelties in the New Corporation Statutes*, 23 Law & Contemp. Prob. 363, 389-90 (1958), and Note, *The Right of Shareholders Dissenting from Corporate Combinations To Demand Cash Payment for their Shares*, 72 Harv. L. Rev. 1132 (1959).

12. Del. Code tit. 8, § 262(a) (Supp. 1976); N.Y. Bus. Corp. Law § 623(b) (McKinney 1963).

13. This is explicit in the New York statute and implicit in the Delaware statute. Compare Del. Code tit. 8, § 262(b) (Supp. 1976) with N.Y. Bus. Corp. Law § 623(a) (McKinney 1963).

14. Del. Code tit. 8, § 262(f) (Supp. 1976).

15. N.Y. Bus. Corp. Law § 623(h) (McKinney 1963).

16. Whether dissenting shareholder statutes should permit a majority of shareholders to engage in a statutory merger or nonstatutory combinations constituting de facto mergers for the purpose of liquidating ("freezing out") minority interests by forcing them to take the appraised value of their shares is considered in Vorenberg, *Exclusiveness of the Dissenting Stockholder's Appraisal Right*, 77 Harv. L. Rev. 1189 (1964), and Note, *Freezing Out Minority Shareholders*, 74 Harv. L. Rev. 1630 (1961). Minority interests have received increasing protection under both state and federal laws. See Note, *The Developing Law of Corporate Freeze-outs and Going Private*, 7 Loy. Chi. L.J. 431 (1976). The Second Circuit has held that non-exchanging shareholders in a short-form merger may have a cause of action under rule 10b-5 of the Securities Exchange Commission, 17 C.F.R. § 240.10b-5 (1964). *Vine v. Beneficial Fin. Co.*, 374 F.2d 627 (2d Cir.), cert. denied, 389 U.S. 970 (1967). However, that holding has been significantly limited by the Supreme Court's most recent decision in this area: *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462 (1977) (where essence of complaint is that shareholders were treated unfairly by a fiduciary, rule 10b-5 not applicable).

otherwise.<sup>17</sup> Whether any of the shareholders of predecessor corporations could come within this statute, therefore, would depend upon these provisions and the relevant facts of listing and share ownership.

Dissenting shareholder statutes also have specified time periods within which a shareholder must exercise his appraisal rights. The Delaware statute provides for a statutory filing period that ends 120 days after the effective date of the merger.<sup>18</sup> The Delaware courts have strictly enforced the statutory cutoff.<sup>19</sup> New York requires the corporation to give notice of the merger to those who objected, or were not required to object,<sup>20</sup> within ten days,<sup>21</sup> and then the dissenter has twenty days to file a notice of election and a demand for payment.<sup>22</sup> Within one month thereafter, he must submit his shares to the corporation for notation.<sup>23</sup> While under certain circumstances the New York courts will excuse minor departures from the statutory periods,<sup>24</sup> delay by non-exchanging shareholders probably will present more than a minor departure from these relatively brief periods.<sup>25</sup> Those who have filed a notice of election to dissent within the time period of either state's law will lose their rights as shareholders, but these rights may be restored (including the right to payment of intervening dividends) if the dissenting shareholder withdraws his notice of election and obtains the written consent of the corporation.<sup>26</sup> But with respect to those who have not acted at all under these dissenting shareholder statutes, the search for a solution must continue elsewhere. They are not dissenting shareholders; they are simply lost or non-exchanging shareholders.

## II. COURT CASES

The status of a shareholder, whether assenting or dissenting, is generally clarified within a short time by the prompt exercise of rights accruing

17. Del. Code tit. 8, § 262(k) (Supp. 1976).

18. *Id.* § 262(c).

19. *See* Raab v. Villager Indus., Inc., 355 A.2d 888 (Del. 1976) (claimants have the burden of proving timely delivery of demand for payment); Schneyer v. Shenandoah Oil Corp., 316 A.2d 570 (Del. Ch. 1974) (court does not have power to extend statutory deadline).

20. *See* note 13 *supra* and accompanying text.

21. N.Y. Bus. Corp. Law § 623(b) (McKinney 1963).

22. *Id.* § 623(c).

23. *Id.* § 623(f).

24. Davis v. Adirondack Indus., Inc., 59 Misc. 2d 1098, 301 N.Y.S.2d 340 (Sup. Ct. 1969), *aff'd*, 33 App. Div. 2d 1100, 308 N.Y.S.2d 107 (1970).

25. *See* Weidersum v. Transvision Elec., Inc., 41 Misc. 2d 936, 246 N.Y.S.2d 638 (Sup. Ct. 1964).

26. A withdrawal of the notice of election by the shareholder, an abandonment or rescission of the proposed corporate action, or a judicial determination that the shareholder is not entitled to payment are among the methods by which the rights to appraisal can be lost. Del. Code tit. 8, § 262(f), (i) (Supp. 1976); N.Y. Bus. Corp. Law § 623(e) (McKinney 1963).

from the definite action required by the applicable statutes. The status of the lost or non-exchanging shareholder is, however, much less certain.<sup>27</sup> The few court cases that have arisen do not indicate any general rule with respect to such shareholders.

It has been said, in a number of court cases, that "[t]here is no underlying 'natural right' of a shareholder in a corporation to follow his investment into a consolidated corporation."<sup>28</sup> Resolutions calling for the exchange of a corporation's property for the stock of another corporation do not automatically convert individual shareholders of the exchanging corporation into shareholders of the issuing corporation.<sup>29</sup> Hence, it should not be entirely surprising that the status of these shareholders is uncertain. The courts have been free to decide these cases nearly as they choose, with the decisions dividing roughly into two groups: those that strain to find some provision in either a statute or the agreement of merger or consolidation which can be construed to make the person a shareholder in the new corporation, and those that hold that the shareholder can lose his rights under either contract theory or laches if he does not make the exchange within a certain period of time.

#### A. *Emphasis on Shareholder Protection*

Three early examples of courts finding that shareholders of consolidated or merged companies become shareholders of the new company are *Copeland v. Directors of Minong Mining Co.*,<sup>30</sup> which relied on a statu-

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27. One commentator has stated that "[i]mmediately on the filing of the certificate of merger, the stockholders of the absorbed corporation generally become stockholders of the surviving corporation." Fuld, *Some Practical Aspects of a Merger*, 60 Harv. L. Rev. 1092, 1104 (1947) (emphasis added). But see Note, *The Lost Shareholder*, 62 Harv. L. Rev. 295 (1948). "The general rule has been stated to be that [the non-exchanging shareholder] does not, merely by virtue of the reorganization, become a shareholder of the new corporation." *Id.* at 303. Fletcher's *Cyclopedia of the Law of Private Corporations* is in agreement with the latter statement. According to Fletcher, a shareholder who has not agreed to take stock in the surviving corporation is under no obligation to exchange his shares and he cannot, ordinarily, be compelled to do so. 15 W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 7135 (perm. ed. 1973).

Fletcher also says that unless there is a statute that automatically converts shareholders of the constituent companies into shareholders of the consolidated or absorbing company (*i.e.*, without action on their part), the "stockholders of the constituent corporations do not become stockholders in the new company merely by virtue of the consolidation." *Id.* The only citation Fletcher gives to such an automatic statutory conversion is one from a 19th-century Michigan case, indicating the paucity of examples, and suggesting that there are no such statutory provisions still in effect. *Id.* (citing *Copeland v. Directors of Minong Mining Co.*, 33 Mich. 2 (1875)).

28. *Beechwood Sec. Corp. v. Associated Oil Co.*, 104 F.2d 537, 540 (9th Cir. 1939); *accord*, *May v. Midwest Ref. Co.*, 25 F. Supp. 560, 564 (D. Me. 1938); *Johnson v. Baldwin*, 221 S.C. 141, 69 S.E.2d 585, 591 (1952).

29. 15 W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 7135 (perm. ed. 1973).

30. 33 Mich. 2 (1875).

tory provision for the automatic cancellation of old shares and the issuance of new shares in a mining company, *Fee v. New Orleans Gas & Light Co.*,<sup>31</sup> where the court looked to a provision in the agreement for cancellation of old shares and issuance of new ones, and *Ridgway v. Griswold*,<sup>32</sup> which does not appear to have relied on any particular statutory or contractual provision in holding that a shareholder in a constituent corporation becomes a shareholder in the new company upon the perfection of the consolidation.

Another interesting example of a court straining to provide protection for the shareholder appears in the New Hampshire case of *Douglas v. Concord & Montreal Railroad*.<sup>33</sup> In 1865 the plaintiff purchased five shares of the Boston, Concord & Montreal Railroad, and in 1871 she placed them with an agent. When the shareholder reexamined the shares in 1898, she discovered that the original issuer had merged with a second railroad corporation nine years earlier to form a new corporation, the Concord & Montreal Railroad. The merger agreement provided that shares in the old corporation were to be exchanged for shares in the new corporation in the ratio of one for one. However, the new shares corresponding to the plaintiff's five old shares had been sold under a further provision of the merger agreement which specifically stated that "[i]f any stockholder [did] not accept the stock apportioned to him in exchange for his old stock," the directors could sell the new shares and apply the proceeds to the needs of the corporation.<sup>34</sup>

The Supreme Court of New Hampshire looked to a local statute on railroad mergers which provided that if a shareholder dissented the corporation might apply to a state supreme court justice for a valuation of the shares. The statute said that "[w]hen notice [had] been given," the court would determine the value of the shares.<sup>35</sup> Although the shareholder in this case had not given the corporation any notice of her "dissent," and was thus not expressly a dissenting shareholder, the court nonetheless read the merger agreement as operative only within the statute. The court found that the plaintiff's failure to exchange should have been understood by the company as either an assent or a dissent to the merger, and then reasoned:

If they understood she assented to the contract, they understood she did not refuse to accept the stock, and that they had no right to sell it. If they understood she dissented, under the law they had no title to her corporate interest without paying its value. . . . There is no suggestion of any method, either in the statute or the contract of union, if

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31. 35 La. Ann. 413 (1883).

32. 20 F. Cas. 772 (C.C.D. Kan. 1878) (No. 11,819).

33. 72 N.H. 26, 54 A. 883 (1903).

34. *Id.* at 29, 54 A. at 885.

35. *Id.* at 28, 54 A. at 884.



either could be upheld, by which any stockholder could be or was to be deprived of his corporate interest without payment in stock or money. If a provision, in the contract of union, that all stockholders who did not present their stock for exchange within a time named, or a time denominated reasonable, should forfeit their right to stock in the new corporation and to compensation for its value, would have been valid and binding upon the plaintiff, in actual ignorance of the provision, no such provision was attempted to be inserted.<sup>36</sup>

The court avoided the agreement provision by claiming that "non-presentation for exchange" is not equal to the required showing of a "refusal" to accept the new stock, although the merger agreement did not use the word "refusal." The court then held that the new corporation had to account for the proceeds of the sale and that, although laches or estoppel might be relevant, they would not apply here because the plaintiff did not "lie by with knowledge of her rights, and no one has rightfully acquired rights, or invested money, or changed his position, upon the strength of her silence."<sup>37</sup>

A more recent example of a court straining to protect the non-exchanging shareholder is *In re Interborough Consolidated Corp.*<sup>38</sup> In that case Judge Mayer of the Southern District of New York was confronted with a successor corporation which had entered into bankruptcy proceedings after a consolidation. During the bankruptcy proceedings, some of the owners of 3,085 unexchanged shares of preferred stock of a predecessor company sought to exchange their shares for preferred shares of the new corporation. Judge Mayer cited pertinent sections of New York's statute governing corporate consolidations and the consolidation agreement itself, which contained no cutoff date, in holding that plaintiffs could not be deprived of the right or privilege of exchanging except by the statutory procedure of appraisal.<sup>39</sup>

The statute, however, was a dissenting shareholder's law, clearly requiring either that shareholders seeking an appraisal *affirmatively object* and make a demand for payment or that the new corporation initiate an action within a stipulated time period.<sup>40</sup> Since neither had taken place, the statute should have been considered irrelevant. Nevertheless, Judge Mayer held that under the circumstances there was "probably" a continuing right to exchange unless the stock had been valued as provided by the statute.<sup>41</sup> He argued that

the theory of the New York statute providing for consolidation is that the stockholder

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36. *Id.* at 30, 54 A. at 885.

37. *Id.* at 31, 54 A. at 885-86.

38. 267 F. 914 (S.D.N.Y. 1920).

39. *Id.* at 917.

40. The text of the relevant statute then in effect is set forth in *id.* at 920.

41. *Id.* at 917.

of the old company cannot be deprived of his stock by a consolidation. . . . If he concludes, as in the case at bar, to remain quiescent, then the *only way* in which the new consolidation corporation could wipe out the stock of the old corporations, and remove whatever embarrassment might be connected therewith, was to pay the owner of the old stock the value thereof in the circumstances, and after the procedure provided by the statute.<sup>42</sup>

The *Douglas* and *Interborough* cases, although somewhat aged, remain important because they show how far judges will go to give non-exchanging shareholders a perpetual right to exchange. They also show how the courts can and will use dissenting shareholder statutes to protect non-exchanging shareholders even though those statutes are actually inapplicable.

But the *Interborough* case also suggests that these statutes, with some alteration, could provide corporations with a solution to the non-exchanging shareholder problem. If the wording in the statutes clearly allowed the surviving corporation to initiate court action for appraisal and payment, it would become possible for corporations to bring actions on their own to end the uncertainty. However, the existing laws are not designed for this purpose, and the relevant statutory time periods most probably will have expired. Even so, a corporation might institute an action at any time to give non-exchanging shareholders the value of their shares, in trust if necessary, and to remove them from the corporation's records, arguing "the theory" of the statute, as did Judge Mayer.

#### B. *Contract Theory and Laches Cases*

Some courts have chosen to consider the problem of non-exchanging shareholders as a part of the law of contracts. Under contract theory, the offer by the new corporation to exchange shares is viewed as a contractual offer and the time period for acceptance is governed by contract law principles. A major case utilizing this approach is *McKay v. Rochester & Lake Ontario Water Service Corp.*<sup>43</sup> In *McKay*, a certificate dated January 26, 1928, consolidating the Rochester & Lake Ontario Water Company and the Clyde Water Supply Company into the Lake Ontario Water Service Corporation stated:

The stockholders of Rochester & Lake Ontario Water Company shall surrender for cancellation their certificates and shall be entitled to receive for each share of such

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42. *Id.* at 918 (emphasis added). Judge Mayer in the *Interborough* case also considered the dividends that had been declared. He said that since they were declared and deposited in a fund, they constituted a trust fund held by the corporation for the shareholders who had not exchanged their shares, but that the shareholders were not entitled to any interest on the amounts so held. *Id.* at 919-20.

43. 247 App. Div. 499, 286 N.Y.S. 801, *aff'd*, 272 N.Y. 528, 4 N.E.2d 432 (1936). See also *Spratt v. Paramount Pictures, Inc.*, 178 Misc. 682, 35 N.Y.S.2d 815 (Sup. Ct. 1942).

stock so surrendered a certificate for one-third of a share of the preferred stock of the par value of \$100 each of the Consolidated Corporation. . . .

Until surrendered and exchanged for certificates issued by it, the Consolidated Corporation shall recognize the now outstanding certificates of stock of the respective Constituent Corporations as evidencing the rights and interests of the several holders thereof as stockholders of the Consolidated Corporation to the same extent and in the same manner as those rights and interests would be evidenced by certificates issued by it, had such outstanding certificates been exchanged therefor.<sup>44</sup>

More than six years after the consolidation the plaintiff sought to exchange the stock. The defendant corporation refused, claiming simply that it was too late. The court found that there was no prescribed time within which the stock had to be surrendered, or the new preferred stock issued, in either the certificate of consolidation or the resolution of the successor company which called for the redemption in accordance with the certificate. Further, the exchange provisions in the certificate of consolidation and the subsequent resolution were found to constitute an "offer" to exchange. Citing the Restatement of Contracts, the court said: "An offer until terminated gives to the offeree a continuing power to create a contract by acceptance of the offer . . . . The power to create a contract by acceptance of an offer terminates at the time specified in the offer, or, if no time is specified, at the end of a reasonable time."<sup>45</sup> The court found that while the plaintiff could have presented his stocks for exchange at any time following the January 26, 1928, offer, he did not do so until May 15, 1934. It was therefore a triable question of fact, turning on the nature of the contract proposed, the usages of business, and all other circumstances, whether the surrender and demand was made within a "reasonable time."<sup>46</sup> The court affirmed the lower court's denial of defendant's motions for dismissal of plaintiff's complaint and for summary judgment.

The *McKay* case fits quite well into the wider pattern developed in stock offer cases, particularly those concerning stock subscriptions from new companies.<sup>47</sup> Sometimes, a subscription for shares is considered an offer which is accepted by the corporation by the act of incorporation. The subscriber's offer in these cases can be withdrawn at any time up to the completion of the acts needed to effect incorporation.<sup>48</sup> However, when the solicitation of subscriptions is made by a corporation (for example, through a vote to open subscriptions and the appointment of a committee to solicit), it is the corporation that is viewed as making the

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44. 247 App. Div. at 500-01, 286 N.Y.S. at 803.

45. *Id.* at 501-02, 286 N.Y.S. at 804 (quoting Restatement of Contracts §§ 34, 40 (1932)). See also Restatement (Second) of Contracts § 40(1) (Tent. Drafts Nos. 1-7 1973).

46. 247 App. Div. at 502, 286 N.Y.S. at 804-05.

47. See 1 S. Williston, *A Treatise on the Law of Contracts* § 69B (3d ed. 1957).

48. See, e.g., *Collins v. Morgan Grain Co.*, 16 F.2d 253 (9th Cir. 1926); *Planters' & Merchants' Indep. Packet Co. v. Webb*, 156 Ala. 551, 46 So. 977 (1908).

offer and the subscriber who communicates his acceptance to the corporation.<sup>49</sup> This parallels the approach used in *McKay*. Similarly, in *Spratt v. Paramount Pictures*,<sup>50</sup> the plaintiff sought to compel the issuance of common stock in exchange for his preferred stock based on a provision for such conversion in the certificate of incorporation "only up to and including the day which shall be two weeks prior to the redemption" of the preferred stock.<sup>51</sup> The court analyzed this provision in terms of an offer which had to be accepted according to the time and mode requirements of the offer and found that the plaintiff had acted too late.

Sometimes the courts resort to the theory of laches to decide these cases. In *Auten v. St. Louis, Iron Mountain & Southern Railway*,<sup>52</sup> the plaintiff, who owned twenty shares in a company which consolidated into a new one, sued for twelve shares in the new company, arguing that he was never given notice of the consolidation. The court said that while knowledge was necessary before laches would apply, circumstances in a particular case could constitute *constructive* knowledge.<sup>53</sup> The plaintiff was charged with constructive knowledge and laches was applied because he knew he was a shareholder and was not being paid any dividends. Moreover, the "slightest inquiry would have disclosed the facts to him."<sup>54</sup>

Two related Delaware cases, *Frank v. Wilson & Co.*<sup>55</sup> and *Bay Newfoundland Co. v. Wilson & Co.*,<sup>56</sup> used laches in a closely connected context. In 1935, Wilson & Co., using a charter amendment, reorganized itself: old class A stock was to be exchanged for new common on a five-for-one basis.<sup>57</sup> The company subsequently made several requests to those shareholders who had not exchanged their shares.<sup>58</sup> In one of the cases arising from that reorganization, the plaintiff requested a rescission,<sup>59</sup> in the other, the plaintiff sought rescission, and either an injunction against the payment of dividends on new common stock until accrued dividends were paid on the stock owned by the complainant or payment of the redemption price for complainant's stock.<sup>60</sup> In both cases, the courts found that the plain-

49. See, e.g., *Kennebec Hous. Co. v. Barton*, 123 Me. 293, 122 A. 852 (1923); *Red River Furnace Co. v. Tennessee Cent. Ry.*, 113 Tenn. 697, 87 S.W. 1016 (1905).

50. 178 Misc. 682, 35 N.Y.S.2d 815 (Sup. Ct. 1942).

51. *Id.* at 683, 35 N.Y.S.2d at 816.

52. 110 Ark. 24, 160 S.W. 873 (1913).

53. "While knowledge is necessary to ground the defense of laches, yet, where the circumstances were such as to have induced inquiry and the means of ascertaining the truth were available, the party is chargeable with knowledge of the truth . . ." *Id.* at 30, 160 S.W. at 874.

54. *Id.* at 31, 160 S.W. at 874.

55. 27 Del. Ch. 292, 32 A.2d 277 (1943).

56. 27 Del. Ch. 344, 37 A.2d 59 (1944).

57. *Frank v. Wilson & Co.*, 27 Del. Ch. at 295, 32 A.2d at 278-79.

58. *Id.* at 296-97, 32 A.2d at 279.

59. *Id.* at 298, 32 A.2d at 279.

60. *Bay Newfoundland Co. v. Wilson & Co.*, 27 Del. Ch. at 345, 37 A.2d at 59.

tiffs were barred because they had waited almost three years after the charter amendment to bring suit.<sup>61</sup>

In another Delaware case, *Federal United Corp. v. Havender*,<sup>62</sup> defendant corporation voted to merge with a subsidiary and to have old preferred stock of the parent corporation converted into new preferred stock of the successor corporation without paying the accrued dividends on the old preferred stock. More than two years later, plaintiffs sued for money payments, including the dividends that had accrued on their old preferred stock. Their claim was that a dissenting shareholders' statute, which provided that "all debts, liabilities and duties of the respective constituent corporations shall thenceforth attach to said resulting or surviving corporation,"<sup>63</sup> protected them. In contrast to the *Interborough* case, the court here refused to apply the dissenting shareholder statute to protect the shareholders' request.<sup>64</sup> No specific time requirements seem to have been violated. In denying the shareholders' petition, the court said the holder of

preference stock as to which dividends have accumulated may not insist that his right to the dividends is a fixed contractual right in the nature of a debt, in that sense vested and, therefore, secure against attack. Looking to the law which is a part of the corporate charter, and, therefore, a part of the shareholder's contract, he has not been deceived nor lulled into the belief that the right to such dividends is firm and stable. On the contrary, his contract has informed him that the right is defeasible; and with that knowledge the stock was acquired.<sup>65</sup>

Since the plaintiffs had not acted under the dissenting shareholder statute, they were held to have lost the right to sue for the accrued dividends.<sup>66</sup>

The *McKay* case, probably the leading case suggesting that non-exchanging shareholders' rights may be cut off when they are not exercised within a reasonable time, was decided in 1936, and has never been overruled. The holding is probably still good law, at least in New York.<sup>67</sup>

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61. *Id.* at 348-55, 37 A.2d at 60-64; *Frank v. Wilson & Co.*, 27 Del. Ch. at 295-306, 32 A.2d at 279-83.

62. 24 Del. Ch. 318, 11 A.2d 331 (1940).

63. *Id.* at 327, 11 A.2d at 335-36.

64. Compare *id.* at 344, 11 A.2d at 343, with *In re Interborough Consol. Corp.*, 267 F. 914, 917-18 (S.D.N.Y. 1920).

65. 24 Del. Ch. at 335, 11 A.2d at 339.

66. *Id.* at 344, 11 A.2d at 343.

67. In fact, the case was cited and discussed at length in *New York Laws Affecting Business Corporations* 168-69 (57th ed. United States Corp. Co. pub. 1976) (annotating § 902 of the New York Business Corporation Law on plans of merger or consolidation) under the head note "Reasonable time in which to surrender certificates for exchange." Curiously enough, the *Interborough* case was not mentioned.

### III. ABANDONED PROPERTY STATUTES

Lost shareholders and unclaimed dividends have long created problems of uncertainty.<sup>68</sup> In recent years, a number of states, including New York and Delaware, have modified their "abandoned" or "unclaimed" property laws to make them applicable to dividends and securities.

#### A. *Application to Securities*

Paragraph 2 of section 501 of New York's Abandoned Property Law provides:

Any security issued by a domestic or foreign corporation and held for a resident by such issuing corporation . . . shall be deemed to be abandoned property where, for three successive years:

(a) All amounts, if any, payable thereon or with respect thereto have remained unpaid to such resident, and

(b) No written communication has been received from such resident by the holder, and

(c) Where the security is held by the issuing corporation, all regular corporate notices required by law to be given to security holders which have been sent, via first class mail, to such resident at his last known address have been returned to the corporation by the postal authorities for inability to locate such resident.<sup>69</sup>

Paragraph 4 of section 501 defines a resident of the state for the purposes of this statute. Paragraph 5 states: "Any . . . security with respect to which such domestic or foreign corporation or fiduciary has on file written evidence received within three years that the person . . .

68. The lack of certainty produced the following statement nearly 30 years ago: "The situation would, therefore, seem to be one calling for legislative clarification. . . . It would seem desirable . . . to make such shares and dividends, or funds for payment of the value of shares, subject to abandoned property statutes. These statutes . . . come closest to reconciling the conflicting objectives of reasonable protection of the shareholder's interests and alleviation of the annoying burdens on the corporation without embarrassing the good will between the company and its shareholder." Note, *The Lost Shareholder*, 62 Harv. L. Rev. 295, 304-05 (1948).

In the absence of such legislative clarification, a number of problems arise. For example, if the corporation sets aside dividends accruing on unclaimed shares, the question of when, if ever, claims for these dividends would become barred by the statute of limitations has generated more questions than answers: "Even after time-consuming research, it will not often be easy in any particular jurisdiction to determine whether the statute of limitations has run against declared but unpaid dividends. Does the statute start running when the dividend becomes payable, or only upon demand and refusal? Is the answer to be reached by sheer logical deduction from the rule (or fiction?) that declaration of the dividend creates a debtor-creditor relationship? Or is it a 'trust' relation? Which statute applies—that relating to trusts, implied contracts, obligations in writing for the payment of money, or some other?" Latty, *Some Miscellaneous Novelties in the New Corporation Statutes*, 23 Law & Contemp. Prob. 363, 376 (1958) (footnotes omitted). For a discussion of unclaimed dividends under current law, see notes 100-05 *infra* and accompanying text.

69. N.Y. Aband. Prop. Law § 501(2) (McKinney Supp. 1976).

for whom such security is held had knowledge thereof shall not be deemed abandoned property."<sup>70</sup>

It appears from the language of the statute that the law is aimed at situations involving an "issuee" of a security who has had no communication with the corporate holder of the security, who has no knowledge that the security is being held for him, and whose whereabouts are unknown to the corporate holder. This is probably not the case with respect to most non-exchanging holders of predecessor securities.<sup>71</sup> The New York statute is really addressed only to clear cases of ownership of unclaimed and abandoned property. Non-exchanging holders of predecessor shares will not necessarily meet all three tests in paragraph 2 plus the test in paragraph 5. Even where they do meet these tests, they still are probably not covered by the statute because they cannot be considered to be the actual owners of the shares of the successor corporation since they never made the exchange that would establish such ownership. If they were never the owners of the shares, they could not have "abandoned" them, and the statute is inapplicable on its face.

One might attempt to refute this argument in those cases where there is language in the corporation merger agreement to the effect that the shares of the predecessor companies shall be deemed to represent the number of full shares of common stock of the surviving corporation. But it is questionable whether merger agreement provisions of this sort<sup>72</sup> will satisfy the requirements of ownership implicit in the Abandoned Property Law.<sup>73</sup>

It may, in fact, not even be necessary to go as far as the question of ownership and abandonment to conclude that the statute does not apply. Paragraph 2 refers to "issued" securities that are "held" by the issuing corporation.<sup>74</sup> Are the shares of a successor company "issued" before there is a presentation for exchange, or are they authorized shares that are as yet unissued? It seems that, unless the merger agreement provides otherwise, the shares are not yet issued.<sup>75</sup> Section

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70. *Id.* § 501(5).

71. See note 2 *supra*. Clearly, if it is the case, an immediate and thorough effort should be made to locate the non-exchanging shareholder. See Ely, *Escheats: Perils and Precautions*, 15 Bus. Law. 791, 800 (1960).

72. A shareholder's ownership interest in a corporation does not necessarily continue in a successor corporation, and a unilateral corporate act does not necessarily change this. See notes 28-29 *supra* and accompanying text.

73. All of the policies underlying the Abandoned Property Law are set forth in relation to the interests of an "owner." See N.Y. Aband. Prop. Law § 102 (McKinney 1944).

74. *Id.* § 501(2) (McKinney Supp. 1976).

75. Some merger agreements provide that new shares are to be issued at the closing. However, these new shares are often held in escrow for an exchange, and not by the successor corporation.

262 of Delaware's General Corporation Law on dissenting shareholders<sup>76</sup> supports this conclusion. Paragraph (j) of that section refers to the new shares of a surviving or resulting corporation into which the old shares held by dissenters would have been converted as having "the status of authorized and unissued shares."<sup>77</sup> If the shares are not "issued," how can they be "held" by the corporation? They cannot. And it seems logical that the result is likely to be the same within other abandoned property statutes.

To solve the problem of out-of-state shareholders of local corporations, Delaware has enacted escheat laws<sup>78</sup> that adopt the Supreme Court's rules in *Texas v. New Jersey*<sup>79</sup> governing conflicting claims to abandoned property.<sup>80</sup> These laws provide that if the specific property is held for, or owed to, an owner whose last known address is in another state, and the property is subject to the escheat laws of that other state, Delaware will not assert any escheat right simply because the company is incorporated in Delaware. Delaware will assert its right to escheat only if (1) the record owner's last known address is in Delaware, or (2) a corporation doing business or incorporated in Delaware is involved and either there is no record of any address for the shareholder or the shareholder's last known address is in a state that does not have an applicable escheat law.<sup>81</sup> Hence, a Delaware corporation would have to check the laws of each of the states in which owners of abandoned or unclaimed securities maintained their last known addresses. If the escheat law of the other state governs, then the Delaware corporation can hold on to the relevant securities up to the statutory period provided for in that state's law.

Delaware's escheat law states:

All property, as hereinafter defined and not otherwise subject to escheat in accordance with this chapter, the title to which has failed and the power of alienation suspended by reason of, (a) the death of the owner thereof, intestate, leaving no known heirs-at-law; (b) the owner thereof having disappeared or being missing from his last

76. Del. Code tit. 8, § 262 (1974).

77. *Id.* § 262(j).

78. *Id.* tit. 12, §§ 1197-1211 (1974 & Supp. 1976).

79. 379 U.S. 674 (1965).

80. A good descriptive history of the entire problem of conflicting claims by states to abandoned property and the Supreme Court's attempts to develop a solution can be found in Sentell, *Escheat, Unclaimed Property, and the Supreme Court*, 17 W. Res. L. Rev. 50 (1965). The problem of conflicting state claims to intangible property is not simply a problem of adequate contacts. Rather, it is a problem of determining which state should be given a clear and ultimately superior right to escheat when there is more than one state with adequate contacts. In *Texas v. New Jersey*, the Supreme Court established the rule that the state of the creditor's last known address, according to the debtor's records, would have the first right of escheat. If there is no such record, or the address is in a state that has no applicable escheat law, the state of corporate domicile has the right of escheat. 379 U.S. at 682.

81. Del. Code tit. 12, §§ 1197-1198, 1211 (1974 & Supp. 1976).



known place of residence for a continuous period of 7 years or more, leaving no known heirs-at-law; or (c) the same having been abandoned by the owner thereof, as hereinafter defined, shall descend to the State as an escheat in accordance with the Constitution, the general laws of this State or this subchapter.<sup>82</sup>

“Property” is defined to include “stocks, bonds and other securities . . . dividends, cash or stock.”<sup>83</sup> The property must be in the possession of a “holder,” which is defined as “any person having possession, custody or control of the property of another person and includes . . . every other legal entity . . . doing business in this State.”<sup>84</sup> But the question of whether the successor corporation is the “holder” of the successor shares persists. If all that exists is a registry and the new shares are not yet issued, can they be considered “property” that is “held” by the successor corporation? Probably not.

Property under the Delaware statute will only be considered “abandoned” if the full “period of dormancy”<sup>85</sup> has run. The latter is defined as

the full and continuous period of 7 years . . . during which an owner has ceased, failed or neglected to exercise dominion or control over his property or to assert a right of ownership or possession or to make presentment and demand for payment and satisfaction or to do any other act in relation to or concerning such property.<sup>86</sup>

The statute says that “‘Owner,’ in addition to its commonly accepted meaning, shall be construed to particularly mean and include any person . . . having the legal or equitable title to property coming within the purview of this subchapter.”<sup>87</sup> Hence, we also face the problem here of whether the holders of predecessor shares can be considered as the “owners” of shares of the successor corporation. The wording of the Delaware statute presents the question somewhat more squarely than does that of the New York statute because it actually uses the term “owner,” but it seems that the New York statute includes, at least implicitly, the same requirement of past ownership.<sup>88</sup>

The Delaware statute goes on to set out requirements for reporting of property deemed abandoned by holders<sup>89</sup> and publication of lists of abandoned property by the state escheator<sup>90</sup> before the property is turned over to him.<sup>91</sup> Failure to report abandoned property can be punishable by daily fines.<sup>92</sup>

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82. *Id.* § 1197 (1974).

83. *Id.* § 1198(10) (Supp. 1976).

84. *Id.* § 1198(6) (1974).

85. *Id.* § 1198(8).

86. *Id.*

87. *Id.* § 1198(7).

88. See note 73 *supra* and accompanying text.

89. Del. Code tit. 12, § 1199 (1974).

90. *Id.* § 1200.

91. *Id.* § 1201.

92. *Id.* § 1207.

If an escheat law governed, the successor corporation would simply hold the unclaimed "shares" until they become "abandoned" and then would have to turn them over to the state. Escheat laws generally make the state the custodian of the property, or its equivalent value, even if transfer of sale of the specific property is provided for after some period of time. The rightful owner, therefore, can generally make a claim for the value of his property against the state after it has escheated.<sup>93</sup> For example, section 1206 of Delaware's law on abandoned and unclaimed property says in paragraph (a): "Any person claiming an interest in any property paid or delivered to the State Escheator under this subchapter may file a claim thereto or to the proceeds from the sale thereof with the State Escheator."<sup>94</sup> Paragraphs (b) and (c) say the owner is not entitled to receive income or other increments accruing after the property was delivered to the state escheator<sup>95</sup> and the procedure for making a claim is set out in another section.<sup>96</sup>

Similarly, New York's Abandoned Property Law provides:

A domestic or foreign corporation or a fiduciary which has paid or delivered to the state comptroller abandoned property pursuant to section five hundred two may make payment to the person entitled thereto, and may file claim for reimbursement for such payment by the state comptroller, who shall, upon satisfactory proof of such payment and after audit, reimburse such domestic or foreign corporation or fiduciary.<sup>97</sup>

The successor corporation, therefore, need not feel that an injustice will be done in states such as New York or Delaware that act as continuing custodians if the securities are given to the state escheator or comptroller after the statutory waiting period for escheating has run.

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93. See Comment, *A Survey of State Abandoned or Unclaimed Property Statutes*, 9 St. Louis Univ. L.J. 85 (1964). Laws governing the disposition of abandoned or unclaimed property can be categorized into three groups: those that make the state a continuing custodian of the property, with an unlimited right in the owner to reclaim the property or its equivalent value; those that provide for "true escheat" of the property, with title vesting indefeasibly in the state after an escheat proceeding; and those that provide for a hybrid of the two methods, with the owner's right to reclaim the property terminating at some time after the property escheats. See McBride, *Unclaimed Dividends, Escheat Statutes and the Corporation Lawyer*, 14 Bus. Law. 1062, 1063-65 (1959). The laws of Delaware and New York, like those of an overwhelming majority of states, are custodial in nature. See notes 94-97 *infra* and accompanying text. An example of a true escheat statute is Conn. Gen. Stat. § 3-72a (1972) (escheat proceeding vests absolute title in state). An example of a hybrid statute is Ark. Stat. Ann. § 50-612 (1971) (claim may be made within two years of escheat proceeding).

94. Del. Code tit. 12, § 1206(a) (1974).

95. *Id.* § 1206(b)-(c).

96. *Id.* § 1146.

97. N.Y. Aband. Prop. Law § 504 (McKinney Supp. 1976). The amount of the reimbursement, however, cannot exceed the amount received by the state comptroller in a sale of such property pursuant to N.Y. Aband. Prop. Law § 1403 (McKinney Supp. 1976).

Generally under escheat statutes, the successor corporation is also protected if it mistakenly decides that escheat law applies. Delaware's law, for instance, says:

The payment or delivery of property to the State Escheator by any holder shall terminate any legal relationship between the holder and the owner and shall release and discharge such holder from any and all liability to the owner, his heirs, personal representatives, successors and assigns by reason of such delivery or payment, regardless of whether such property . . . and such delivery and payment may be pleaded as a bar to recovery and shall be a conclusive defense . . . .<sup>98</sup>

New York and other states provide similar protection to the holder with respect to liability to other persons for the transfer of securities to the state comptroller.<sup>99</sup>

### B. *Application to Dividends, Meetings, and Voting*

The question of what is to be done with dividends, the calling of meetings, and the counting of votes is as uncertain as the right to exchange shares.<sup>100</sup> One leading commentator says that preferred shareholders of a corporation which has been consolidated with another have a right to money deposited to pay dividends (since a deposit constitutes a trust) if they have the right to exchange their stock, but that they have no lien for accumulated dividends not set apart.<sup>101</sup> This would be in accord with the *Interborough* case. But it begs the question of whether shareholders retain the right to exchange and therefore the right to claim segregated dividend assets. If dividend funds are not segregated, preferred shareholders would appear to have no rights to them.<sup>102</sup>

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98. Del. Code tit. 12, § 1203 (1974).

99. See, e.g., N.Y. Aband. Prop. Law § 502(2) (McKinney Supp. 1976).

100. For example, one commentator observed that certificates of merger sometimes provide that no dividends shall be paid on new stock until the old shares are surrendered, but suggested that it is not certain that such provisions would be sustained in a court test. Fuld, *Some Practical Aspects of a Merger*, 60 Harv. L. Rev. 1092, 1104 (1947). The article went on to say: "It is certainly necessary to give [the owner of a certificate which has been temporarily mislaid or is inaccessible] notice of, and to count his vote at, all stockholders' meetings, whether or not the new stock certificate has actually been issued." *Id.* at 1105. But a Note in a later volume of the same publication said, simply, that the situation was ambiguous, unlitigated, and in vast need of legislative clarification. Note, *The Lost Shareholder*, 62 Harv. L. Rev. 295, 304 (1948).

Statutes allowing a corporation to set a record date to determine which shareholders are entitled to vote at a meeting do not address the problem of whether the non-exchanging shareholders should be considered record shareholders in the successor corporation on the chosen record date. See Del. Code tit. 8, § 213 (1974); N.Y. Bus. Corp. Law § 604 (McKinney 1963).

101. 15 W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 7140 (perm. ed. 1973).

102. There is also the question of whether the running of the statute of limitations on claiming a dividend (see note 70 *supra*) can prevent the application of an escheat statute. The Supreme Court of New Jersey in *State v. Standard Oil Co.*, 5 N.J. 281, 74 A.2d 565 (1950), *aff'd*, 341 U.S.

However, it should be noted that, unlike the Delaware statute,<sup>103</sup> the New York Abandoned Property Law has a provision for dividends separate from that applicable to the underlying security:

Any amount which, on or after January first, nineteen hundred forty-seven, shall have become payable by a domestic or foreign corporation or by a fiduciary to a resident shall be deemed abandoned property when the security with respect to which such amount is payable has been deemed abandoned or when such amount:

- (a) Is payable to such resident as a holder or owner of a security; and
- (b) Has, on the thirty-first day of December in any year, remained unpaid to such resident for three years.<sup>104</sup>

Thus, an unclaimed dividend may arguably escheat under New York law after three years, even where the underlying security does not meet the four tests separately applicable to it.<sup>105</sup>

#### IV. THE PRESENT ALTERNATIVES

Although the law is admittedly unclear, a successor corporation should first collect all the data it has relating to the shareholders of the predecessor corporations who might still demand that their old shares be exchanged for the shares of the successor corporation. The collected data should include the number of shares, either the residence or the last known address of the record owner (or both), and whether or not there have been any communications from that person. It would also be useful to include any evidence indicating whether that person is aware of the possibility of exchange. It may then be possible to group people into two basic categories. The first would include those who, aside

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428 (1951), said that the running of a statute of limitations on a debt would mean that there was nothing left to escheat, but held that this did not apply to unclaimed dividends because dividends are not a debt. Rather, they are funds held in trust by the corporation for lost shareholders. *Id.* at 302, 74 A.2d at 573-74. It should be noted, however, that a segregated fund for unclaimed dividends was kept by the Standard Oil Company. It is not certain that the same analysis would apply where the unclaimed dividends were not segregated. *See* Comment, *Unclaimed Dividends and Shares of Stock*, 46 Ill. L. Rev. 82, 90-91 (1951). If the running of statutes of limitations barred the escheat of dividends, most unclaimed property laws would become inapplicable because the time periods in the statute of limitations are generally shorter than those for escheating. *Id.* at 91.

The Delaware statute avoids this problem by providing that a statute of limitation will usually not bar application of its escheat law: "The expiration of any period of time specified by statute or court order, during which an action or proceeding may be commenced or enforced to obtain payment of a claim for money or recovery of property, shall not prevent the money or property from being deemed abandoned property nor affect any duty to file a report required by this subchapter or to pay or deliver abandoned property to the State Escheator." Del. Code tit. 12, § 1202 (1974).

103. Del. Code tit. 12, §§ 1210-1211 (1974).

104. N.Y. Aband. Prop. Law § 501(1) (McKinney Supp. 1976).

105. *See* note 69 *supra* and accompanying text. Whether the dividends should be considered payable when there has been no exchange of shares is not completely clear, however.

from the question of whether they can be considered "owners" of the successor shares, or whether the new securities are "issued" and "held" by the successor corporation, seem to satisfy the requirements of an applicable escheat law, whether it be the state of their last known address or the state of incorporation. The second would include those who definitely cannot come within *any* escheat law. With respect to the first group, the successor corporation can then concentrate on the question of ownership, perhaps requesting an opinion from the state escheator or comptroller as to whether the escheat law applies. These shareholders would hopefully then remain separable according to whether unclaimed or abandoned property laws are applicable to them or not.

But even where such data are diligently collected, it is likely that a substantial number of non-exchanging shareholders will remain as to whom the successor corporation will have to decide among the following choices: (1) to make exchanges indefinitely, (2) to act under escheat law notwithstanding its apparent inapplicability, (3) to initiate an action using dissenting shareholder law to pay the value of the shares, or (4) to deny the right to make exchanges after a requisite period of time has run.

#### A. *Making Exchanges Indefinitely*

Making exchanges indefinitely has several obvious disadvantages. The corporation must maintain all the old shareholders on its record books and continually decide what to do in connection with invitations to meetings, voting rights, and rights to dividends. It is likely that each of these problems will exist indefinitely since the successors-in-interest to the non-exchanging shareholder might also remain silent or seek to exchange their shares at some indefinite future date. There is, therefore, a high administrative cost in making this choice.

But there are advantages to this alternative as well. Since it is not clear what law applies to the situation, making any of the other choices will run some risk of litigation, failure, and embarrassment. Making exchanges indefinitely is also the choice most likely to maintain the shareholders' good will.

#### B. *Acting Under Escheat Law*

The utilization of an applicable escheat law offers three distinct advantages: (1) the corporation can be rid of the expense of sending notices such as those for meetings, votes, or dividends by removing the securities from its records; (2) the corporation would be protected from any liability to the owner; and (3) the shareholder can generally still obtain a payment for the value of his shares after the shares are escheated.

The main problem with escheat laws, however, is the likelihood that they do not apply. A review of all relevant escheat laws and the opinion of state escheators or comptrollers would be useful in determining applicability. But even if an escheat law is mistakenly applied, the successor corporation should find comfort in the fact that it will most probably be protected from any liability. This makes the use of escheat law much more palatable.

### C. Utilizing Dissenting Shareholder Law

Although New York's dissenting shareholder statute has been altered since the *Interborough* case, the state's Business Corporation Law contains the following sentence:

If a notice of election is withdrawn, or the proposed corporate action is abandoned or rescinded, or a court shall determine that the shareholder is not entitled to receive payment for his shares, or the shareholder shall otherwise lose his dissenter's rights, *he shall not have the right to receive payment for his shares* and he shall be reinstated to all his rights as a shareholder as of the filing of his notice of election, including any intervening preemptive rights and the right to payment of any intervening dividend or other distribution or, *if any such rights have expired* or any such dividend or distribution other than in cash has been completed, in lieu thereof, *at the election of the corporation*, the fair value thereof in cash as determined by the board as of the time of such expiration or completion, but without prejudice otherwise to any corporate proceedings that may have been taken in the interim.<sup>106</sup>

The statute also says: "*The court shall determine whether each dissenting shareholder, as to whom the corporation requests the court to make such determination, is entitled to receive payment for his shares.*"<sup>107</sup>

Similarly Delaware's law says that if there is a failure to agree on the shares' value, the corporation may petition the Court of Chancery to determine the value.<sup>108</sup> Hence, while dissenting shareholder statutes may not have been intended to apply to non-exchanging shareholders, courts may find, as did Judge Mayer in the *Interborough* case, that if a shareholder remains "quiescent, then the only way in which the new consolidation corporation could wipe out the stock of the old corporations . . . [is] to pay the owner of the old stock the value thereof" through the procedure of the dissenting shareholder statute.<sup>109</sup> A successor corporation, under this doctrine, could attempt to use a dissenting shareholder statute to resolve its problem. And, although the statutory time periods may have run (which seems to have been so in the *Interborough* case), the judge may simply ignore the question as Judge Mayer did in *Interborough*.

A successful utilization of a dissenting shareholder statute would have

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106. N.Y. Bus. Corp. Law § 623(e) (McKinney 1963) (emphasis added).

107. *Id.* § 623(h)(4) (emphasis added).

108. Del. Code tit. 8, § 262(c) (Supp. 1976).

109. 267 F. 914, 918 (S.D.N.Y. 1920).

the great advantage of settling the whole problem through a single payment. But there could be the problem of where to send the payments if the addresses of the shareholders are unknown. This problem is a manifestation of the basic fact that non-exchanging shareholders do not follow the statutory procedures for registering their "dissent,"<sup>110</sup> and indicates the difficulties inherent in applying dissenting shareholder laws to their situation. It also suggests that the courts may be very reluctant to apply these laws to non-exchanging shareholders, the *Interborough* case notwithstanding.

#### D. *Applying Contract Law*

Under contract law theory, the "ownership" of successor shares is held to be in the successor corporation until the offer to exchange is accepted. If the offer is not accepted after having been in existence for a "reasonable time," the offer would no longer be open to acceptance and ownership would continue in the successor corporation, which presumably could do as it pleases with the shares. The successor corporation might thereafter treat the shares as authorized but unissued.<sup>111</sup>

If contract law theory is applicable, it may not, in fact, be necessary to wait until a "reasonable" period of time has run. Offerors have full power over the terms of their offers. Unless an offer is irrevocable by its terms, or by statute, it can be revoked or altered<sup>112</sup> by setting a cut-off for acceptance. The possibility that the offer to exchange may be revoked, however, is not easy to accept. It would mean that those who failed to accept at any arbitrary point at which the offer is revoked would have no recourse. This potential result raises some doubt as to whether the *McKay* case reasoning<sup>113</sup> would be followed. However, it is possible that the courts will find that an offer to exchange is irrevocable for the original period of time stated or for a "reasonable" period of time if no time period is stated. With the exception of this limitation, the principle of freedom to alter an offer would apply as in *McKay*. The successor corporation could specify a date after which the offer to exchange would terminate. After being communicated to those shareholders who had not already accepted the offer, the specified date would then determine a period within which the shareholder-offerees must act to make the exchange or lose the right to exchange forever. Even without an address to which such communication could be sent, it might be possible to provide the necessary notice through publication.<sup>114</sup> After the cut-off date, the

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110. See notes 9-26 *supra* and accompanying text.

111. See text accompanying note 75 *supra*.

112. 1 A. Corbin, Contracts § 39 (1963).

113. See notes 43-46 *supra* and accompanying text.

114. 1 A. Corbin, Contracts § 41 (1963).

corporation would be freed from all obligations to list the former shareholders in its records and documents. The successor shares, and the dividends relating to those shares, would no longer be subject to a demand for payment. The predecessor shares would then be void. However, the firm would still be able to make voluntary payments to claimants if it chose to do so.

Yet there still is a basic problem of uncertainty in following the contract theory approach. If this approach were relied upon by the corporation, a shareholder might nevertheless sue to force an exchange, and the courts could simply find that contract law is inapplicable.

## V. CONCLUSION

The problems and uncertainties inherent in any of the alternatives just described should impress upon anyone handling the merger of two or more corporations the existence of a need to resolve, to the extent possible, the problem of the non-exchanging shareholder in the merger agreement documents. If possible, the final date for making an exchange should be stipulated and adequate communication of the date should be made to shareholders. In addition, provisions should be included to handle shareholders who wish to make exchanges after the cut-off date has passed. The monetary equivalent of the shares, for example, might be held in trust for such claimants.

Yet, because it may be difficult or impossible to include such provisions in merger agreements, and because many merger agreements will inevitably fail to contain a complete solution, state legislatures should enact legislation to solve the problem of the non-exchanging shareholder. It is this writer's view that the best legislative solution would be one in which the abandoned property laws are amended so they specifically apply to non-exchanging shareholders, even if this is perceived to be somewhat beyond the traditional reach of these statutes. These laws offer the best solution because they establish precise and reasonable periods of time before the property is considered "unclaimed" or "abandoned" and because there would be no doubt as to when the time period has run. After the stipulated period, the corporation could transfer the property to the state and strike the non-exchanging shareholder's name from its record books. The corporation would be protected from any liability to claimants for transferring the shares to the state, and the shareholder might still obtain the value of his shares from the state upon a proper application.