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## Corporations – Cumulative Voting – Stagger System – Unconstitutional

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to show the maintenance of a liquor nuisance.<sup>15</sup> The probative value of such evidence is to be determined in connection with all the other evidence in the case,<sup>16</sup> and, in the absence of a statute making possession of a license prima facie evidence of guilt,<sup>17</sup> the mere issuance of such a license is not sufficient to sustain a conviction.<sup>18</sup>

At the time the instant case was decided, there was a statute<sup>19</sup> which made the purchase and possession of the gambling stamp prima facie evidence of violation of the gambling laws. It is interesting to note that this statute was not even mentioned in this case, although there was an excellent opportunity to do so, and its logical application would have resulted in an opposite decision. However, it is probable that the court refrained from mentioning the statute in anticipation of the case,<sup>20</sup> which only a few months later, held the statute unconstitutional. Thus the court appears to have followed the law with regard to liquor licenses.

JOAN M. FRANKS

### CORPORATIONS—CUMULATIVE VOTING—STAGGER SYSTEM—UNCONSTITUTIONAL

A stockholder sought to have declared unconstitutional an Illinois statute<sup>1</sup> which provided that a corporation could stagger the terms of office of its directors by designating different classes of directors who are elected at different intervals. *Held*, that although the Illinois Constitution,<sup>2</sup> providing for cumulative voting, did not expressly prohibit director classification, the statute could not be upheld since it defeated the purpose of cumulative voting. *Wolfson v. Avery*, Illinois Supreme Court, No. 33563, April 15, 1955.\*

Cumulative voting is a method by which a stockholder, instead of voting his shares for each of the directors to be elected, is allowed to cast the whole number of his votes for one director or to concentrate or distribute

15. *State v. Kallas*, see note 14 *supra*.

16. *Bishop v. State*, 90 Okla. Cr. 410, 214 P.2d 971 (1950); *White v. Comm.*, 107 Va. 901, 59 S.E. 1101 (1907).

17. For example, ARK. STAT. § 48-49 (1947).

18. *Appling v. State*, 88 Ark. 393, 114 S.W. 927 (1908); *Peyton v. State*, 83 Ark. 102, 102 S.W. 1110 (1907); *Liles v. State*, 43 Ark. 95 (1884).

19. FLA. STAT. § 849.051 (1953).

20. *Jefferson v. Sweat*, 76 So.2d 494 (Fla. 1954) (held statute unconstitutional on ground that mere possession of the stamp cannot be prima facie evidence that defendant has been guilty of a crime when there is no evidence of any kind that a crime has been committed).

1. ILL. CODE ANN. § 157.35 (1951): Providing that when a corporation shall have nine or more directors they may be divided into classes.

2. ILL. CONST. ART. XI, sec. 3 (1870): Every stockholder shall have the right to cumulate his vote. ILL. CODE ANN. § 157.28 (1951).

\*A rehearing of this case is anticipated.

such votes as he sees fit.<sup>3</sup> Under this system, the stockholder multiplies the number of his shares by the number of directors to be elected. The product represents the number of votes the stockholder may cast as he pleases. The purpose of this device is to give a sufficient minority an opportunity to secure representation on the board of directors.<sup>4</sup> Cumulative voting is a potent weapon against corporate mismanagement since the minority directors can inform stockholders of misdealings.<sup>5</sup> It makes management by secrecy an impossibility.<sup>6</sup> Those opposed to cumulative voting have two major objections. First, it permits corporate raids by minority stockholders.<sup>7</sup> Second, it is detrimental to smooth and efficient management.<sup>8</sup>

Generally speaking, there are three ways that the right to cumulative voting in the election of directors is provided:

- (I) Required by the state constitution.<sup>9</sup>
- (II) Required by a state statute.<sup>10</sup>
- (III) Optional, by state statute, if provided for in the corporate charter.<sup>11</sup>

If cumulative voting is required by constitutional or statutory provisions, it can not be circumvented by contrary provisions in the corporate charter or by-laws.<sup>12</sup> If it is permitted by statute, then the corporation charter or by-laws must expressly provide for cumulative voting.<sup>13</sup> Florida has no statutory or constitutional provisions governing cumulative voting in general

3. 13 AM. JUR., *Corporations*, § 508: State statutes always provide for the election of directors by stockholders. See the UNIFORM BUS. CORP. ACT. § 31, which provides that except as in the case of vacancies, directors other than those constituting the first board shall be elected by the stockholders.

4. 5 FLETCHER, *CYCLOPEDIA CORPORATIONS, Cumulative Voting*, § 2048 (1952).

5. Note, 56 DICK. L. REV. 330 (1951).

6. *Id.*

7. *Id.*

8. *Id.*

9. ILL. CONST. ART. XI, § 3 (1870); PA. CONST. ART. XVI, § 4 (1874); S. DAK. CONST. ART. XVII, § 5 (1898).

10. CAL. LAW OF CORP. C. I, § 2235 (*Deering* 1947); OHIO STAT. ANN. § 1701.58 (1951); WASH. REV. CODE 23:32:070 (1951).

11. 8 DEL. CODE ANN. § 214 (1953); N. Y. LAWS, c. 653, § 49 (1935); N.J. REV. STAT. 14:10-15 (1937); GEN. LAWS R.I. c. 116, § 23 (1938); TENN. CODE ANN. § 3744 (1942); VA. CODE § 13-203 (1950).

12. *Wright v. Cent. Cal. Water Co.* 67 Cal. 532, 8 Pac. 70 (1885); *Chicago Macaroni Co. v. Boggiano*, 202 Ill. 312, 67 N.E. 17 (1903); *Zachary v. Milin*, 294 Mich. 622, 293 N.W. 770 (1940); *Commonwealth v. Green*, 351 Pa. 170, 40 A.2d 492 (1945); *State v. Perham*, 30 Wash.2d 368, 191 P.2d 689 (1948); *Cross v. W. Va. Cent. Ry.* 35 W. Va. 174, 12 S.E. 1071 (1891).

13. *Chappel v. Standard Supply Co.* 15 Del. Ch. 333, 138 Atl. 74 (1927); *In re Brophy*, 13 N.J. Misc. 462, 179 Atl. 128 (1935); *In re American Fibre Seat Corp.*, 265 N.Y. 416, 193 N.E. 253 (1934); *In re Jamaica Consumers' Ice Co.* 190 App. Div. 739, 180 N.Y. Supp. 384 (1920).

business corporations,<sup>14</sup> therefore, it is probably necessary to provide for the right in the certificate of incorporation.<sup>15</sup>

Classification of directors is a device to counter the effect of cumulative voting.<sup>16</sup> Under this system, a corporation may place its directors into classes who hold staggered terms, each class being elected at different intervals. Many states<sup>17</sup> have statutes which permit this practice in corporate business, if provided for in the charter. The result of its application is tantamount to nullifying the right of cumulative voting, as illustrated below.

The Montgomery Ward Company has a board of nine directors. There are approximately six and one-half million shares outstanding. Assume that five and one-half million votes will be cast, and of these the majority has three million and the minority two and one-half million. By multiplication, the majority has twenty-seven million votes (9 x 3,000,000) and the minority has twenty-two and one-half million votes, (9 x 2,500,000) respectively. By the proper concentration of votes, the majority may elect five directors and the minority four directors, leaving management control with the majority. The minority, however, has substantial representation.

Majority slate of directors	A	B	C	D	E	F	G	H	I	Total votes cast
Majority Votes (in millions)	5.4	5.4	5.4	5.4	5.4					Majority 27,000,000
Minority slate of directors	R	S	T	U	V	W	X	Y	Z	
Minority votes (in millions)						5.7	5.6	5.6	5.6	Minority 22,500,000

Now assume the directors are divided into three classes, and at the time of the election all nine directorships are held by the majority. Only three directors are to be elected.<sup>18</sup> Therefore, the number of votes to be cast decreases. The majority will have nine million votes (3 x 3,000,000). The minority will have seven and one-half million votes (3 x 2,500,000). Again there is a proper concentration of votes, inasmuch as both the majority and minority know they can not capture all three of the directorships.

14. FLA. STAT. c. 608 (1953).

15. In the absence of an express provision in the charter, a Florida corporation stockholder would not have the cumulative voting right.

16. Note, 56 DICK. L. REV. 530 (1951).

17. Connecticut, Delaware, Florida, Massachusetts, Michigan, New Jersey, New York, Ohio, Oklahoma, Pennsylvania, Rhode Island and Tennessee.

18. ILL. CODE. ANN. § 157.35 (1951): Provided maximum of three classes of directors to hold office for no longer than three years each.

Majority slate of directors	A	B	C	Total votes cast
Majority votes (in millions)	4.5	4.5		Majority 9,000,000
Minority slate of directors	R	S	T	
Minority votes (in millions)			7.5	Minority 7,500,000

Here, even though cumulative voting is utilized, the best the minority can do is to capture one directorship.<sup>19</sup> In succeeding years the result would be the same, and the minority as such, could never capture more than three seats in any three-year period. For, in the fourth year, the director elected in the first year will have completed his term and would be up for re-election.<sup>20</sup>

In the instant case, the court believed the stagger system was contrary to the purpose and intent of the Illinois Constitution which guarantees the right to cumulative voting. The decision rested upon the court's conclusion that by use of director classification, the cumulative voting right was watered down to the point, that in reality, it was of no effect. There is room for argument however, since cumulative voting is a guarantee of minority representation on the board of directors and not necessarily of "fair" representation. Even under the classification system, the minority stockholders of the Montgomery Ward Company would have secured at least one chair, if they were a sufficient minority. The decision was solely one of constitutional interpretation.

Florida has a statute<sup>21</sup> providing for the classification of directors. The same is true of Delaware,<sup>22</sup> New York,<sup>23</sup> New Jersey<sup>24</sup> and Massachusetts<sup>25</sup> However, it is not likely that those states will be affected by this decision as there exists no constitutional or statutory right to cumulative voting.<sup>26</sup> Other states, such as California,<sup>27</sup> South Carolina,<sup>28</sup> South Dakota,<sup>29</sup> Ohio,<sup>30</sup> Washington<sup>31</sup> and Pennsylvania<sup>32</sup> give the right

19. *Id.*

20. Under the Illinois law no more than three directorships could be acquired at any election, and that would take almost a unanimous vote of the stockholders.

21. FLA. STAT. § 608.08 (1953).

22. 8 DEL. CODE ANN. § 141 (1953).

23. N. Y. LAWS c. 717, § 6 (1951).

24. N. J. REV. STAT. 14: 7-3 (1937).

25. MASS. GEN. LAWS c. 156, § 22 (1932).

26. Inasmuch as some states do not require cumulative voting, it follows that there should be no objection to a statute providing for classification of directors.

27. CAL. LAW OF CORP. c. 1, § 2235 (*Deering* 1947).

28. S.C. CONST. ART. IX, § 11 (1895); S.C. STAT. ANN. § 12-253 (1952).

29. S. DAK. CONST. ART. XVII, § 5 (1898).

30. OHIO STAT. ANN. § 1701.58 (1953).

31. REV. CODE WASH. 23:32:070 (1951).

32. PA. CONST. ART. XVI, § 4 (1874).

to cumulative voting by constitutional or statutory provision. Of these, only Ohio<sup>33</sup> and Pennsylvania<sup>34</sup> have statutes expressly authorizing director classification. It seems that those states requiring cumulative voting generally do not authorize the classification of directors. It is probable therefore, that the laws of those states such as Ohio and Pennsylvania which ensure the cumulative voting right and at the same time authorize director classification may come under fire. The instant case may be persuasive in those jurisdictions, but, in all probability, will have no effect in jurisdictions without constitutional or statutory cumulative voting requirements.

PAUL LOW

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33. OHIO STAT. ANN. § 1701.64 (1953).

34. 15 PA. STAT. § 48 (*Purdon* 1938).