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Contracts--Specific Performance--Creation of a Constructive Trust [*Butler v. Attwood*, 369 F.2d 811 (6th Cir. 1966)]

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CONTRACTS — SPECIFIC PERFORMANCE — CREATION
OF A CONSTRUCTIVE TRUST

Butler v. Attwood, 369 F.2d 811 (6th Cir. 1966).

Although a corporate shareholder is normally free to buy or sell shares as he wishes,¹ certain restrictions on the transfer of shares may be imposed by charter or by shareholder agreements.² In *Butler v. Attwood*³ plaintiff Butler sought a court decree requiring the defendants — Attwood, the original buyer, and the Finzels, the original sellers — to transfer to him certain corporate shares which had become the subject of a buy-and-sell agreement between Attwood and the Finzels (hereinafter referred to as the Attwood-Finzel contract). Plaintiff Butler based his claim upon an antecedent contract (hereinafter referred to as the Butler-Attwood contract) he had negotiated with the buyer, Attwood, which entitled the plaintiff to purchase one half of any stock in the corporation that became available for purchase by Attwood.⁴ The federal district court held that the plaintiff was entitled to specific performance against the buyer since the latter had breached his earlier agreement with the plaintiff when he refused to sell the shares to him, but the court denied such relief against the sellers, the Finzels, because the buyer had not entered into the Attwood-Finzel contract as an agent or fiduciary of the plaintiff.⁵

The plaintiff appealed, arguing that the relief granted by the district court was "worthless" to him because the buyer, Attwood, and the sellers had failed to close the sale of the shares to the buyer. In remanding, the Sixth Circuit held that the plaintiff was entitled to specific performance against both the buyer and the sellers.⁶

¹ Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505 (1965).

² BALLANTINE, CORPORATIONS § 336 (rev. ed. 1947).

³ 369 F.2d 811 (6th Cir. 1966).

⁴ The agreement provided that "any future purchases of stock shall be made on a 50-50 basis between the two parties and that at some future time an agreement for all contingencies will be drawn between the parties." *Id.* at 813.

⁵ *Id.* at 812. The lower court granted specific performance of the Butler-Attwood contract because the stock was unique and not available on the market. *Butler v. Attwood*, Civil No. 25165, E.D. Mich., Aug. 2, 1965. In recent years the courts have increased the availability of specific performance of contracts other than those for the sale of land. Generally, courts have granted specific performance of a contract for the sale of any stock which is unique. See *Baltimore Realty Corp. v. Alman*, 282 App. Div. 714, 122 N.Y.S.2d 224 (1953); *Kurth v. Hauser*, 262 Wis. 325, 55 N.W.2d 367 (1952); *Van Hecke*, *Changing Emphasis in Specific Performance*, 40 N.C.L. REV. 1 (1961); Comment, 51 MICH. L. REV. 408 (1953).

⁶ 369 F.2d at 821.

The court of appeals in *Butler* decided that the lower court's finding that the buyer had not entered into the Attwood-Finzel contract as a fiduciary of the plaintiff was a conclusion of law inconsistent with the findings of fact.⁷ Having found that a fiduciary relationship existed between the plaintiff and the buyer, the appellate court manifested its desire to be equitable by creating a constructive trust.⁸ It was reasoned that Attwood obtained a vested right to acquire the sellers' shares and to the extent of one half of these shares held such right as a constructive trustee for the plaintiff.⁹ In addition, the court held that in order to fulfill the constructive trust, there was no impediment in employing as a remedial device a decree which directed the carrying out of the Attwood-Finzel contract, particularly since the sellers knew of the plaintiff's rights acquired under the Butler-Attwood contract.¹⁰

The court of appeals overruled the district court on the issue of whether the buyer entered into the Attwood-Finzel contract as a fiduciary of the plaintiff.¹¹ The term fiduciary in its broadest meaning includes both technical fiduciary relationships and those informal relations which exist whenever one person trusts and relies upon another.¹²

The lower court found that the conduct of the parties demonstrated that the Butler-Attwood agreement simply required that one party communicate the existence of opportunities to purchase stock in the corporation to the other party who would then be privileged to purchase one half of the amount offered for sale.¹³ The lower court also found that the conduct of the parties demonstrated that neither of them was required to purchase the stock with a resale of

⁷ *Id.* at 819.

⁸ *Ibid.* A constructive trust is a remedial device of a court of equity, arising when a person in a fiduciary relation acquires or retains property in violation of his fiduciary duty. 4 SCOTT, TRUSTS § 499, at 3225 (2d ed. 1956). The fiduciary under these circumstances holds the property as a constructive trustee and is subject to an equitable duty to convey the property to the beneficiary of the trust on the ground that the trustee would be unjustly enriched if he were permitted to retain it. *Id.* at 462.1, at 3104.

⁹ 369 F.2d at 818. The court stated that the right of the buyer to purchase and the obligation of the sellers to sell the shares created a res upon which to impose a trust for the benefit of the plaintiff. *Ibid.*

¹⁰ *Ibid.*

¹¹ *Ibid.*

¹² *E.g.*, trustee-beneficiary, guardian-ward, agent-principal, and attorney-client. See *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 571, 160 S.W.2d 509, 512 (1942); *Cartwright v. Minton*, 318 S.W.2d (Tex. Civ. App. 1958). A fiduciary is under a duty to act for the benefit of the other party as to matters within the scope of the relationship. 1 SCOTT, *op. cit. supra* note 8, § 2.5, at 38.

¹³ 369 F.2d at 815.

one half to the other party, concluding from these facts that the buyer did not enter into the Attwood-Finzel contract as an agent or fiduciary of the plaintiff.¹⁴

The Sixth Circuit, in reaching a different conclusion,¹⁵ reasoned that the buyer entered into the Finzel-Attwood contract as an agent, with a corresponding fiduciary duty,¹⁶ for the plaintiff. When given authority to acquire property for his principal, the agent violates his fiduciary duty if he either purchases such property for his own account¹⁷ or rescinds or modifies the terms of the sale after its completion.¹⁸ Moreover, a third party is subject to liability to the principal if he intentionally assists an agent in violating the duty to his principal.¹⁹

In the instant case the buyer, acting as the plaintiff's agent, had no authority to rescind the Attwood-Finzel contract with the sellers. The buyer thus held the right to purchase one half of the shares as a constructive trustee for the plaintiff since the buyer, by rescinding the Attwood-Finzel agreement, violated his fiduciary duty. In addition, the sellers were liable to the plaintiff for assisting the buyer in breaching his fiduciary duty. This analysis would seem to be verified by the fact that the court of appeals relied on an agency case, *Harmer v. King*,²⁰ to support its view that the plaintiff obtained an enforceable interest in the Attwood-Finzel contract.²¹

There is some question as to whether the Sixth Circuit was correct in its analysis that the buyer entered into the Attwood-Finzel

¹⁴ *Id.* at 812.

¹⁵ *Id.* at 819.

¹⁶ It is well established that an agent, a fiduciary with respect to matters within the scope of his agency, is under a duty to act exclusively for his principal's interest. *Sim v. Edenborn*, 242 U.S. 131 (1916); *Palmer v. Chamberlin*, 191 F.2d 532 (5th Cir. 1951); *Elco Shoe Mfrs. v. Sisk*, 260 N.Y. 100, 183 N.E. 191 (1932); RESTATEMENT (SECOND), AGENCY § 13 (1958).

¹⁷ The agent will thus be considered a constructive trustee. See *Quinn v. Phipps*, 93 Fla. 805, 113 So. 419 (1927); *Sentell v. Richardson*, 211 La. 288, 29 So. 2d 852 (1947); *Whitten v. Wright*, 206 Minn. 450, 289 N.W. 509 (1939).

¹⁸ *Huish v. Lopez*, 70 Ariz. 201, 207, 218 P.2d 727, 731 (1950) (agent has no power to rescind); *Gallagher v. California Pac. Title & Trust Co.*, 13 Cal. App. 2d 482, 492, 57 P.2d 195, 200 (Dist. Ct. App. 1936) (agent has no power to vary or cancel contract); *Quirk v. Raymond Heard, Inc.*, 222 La. 46, 54, 62 So. 2d 96, 98-99 (1952) (agent has no power to abrogate or modify contract); *Curtis v. Zurich Gen. Acc. & Liab. Co.*, 108 Mont. 275, 285, 89 P.2d 1038, 1043 (1939) (agent has no power to rescind contract); RESTATEMENT (SECOND), AGENCY § 66 (1958).

¹⁹ *In re Browning's Estate*, 177 Misc. 328, 30 N.Y.S.2d 604 (Surr. Ct. 1941). See 4 SCOTT, *op. cit. supra* note 8, § 506, at 3247; Scott, *The Fiduciary Principle*, 37 CALIF. L. REV. 539, 554 (1949); RESTATEMENT (SECOND), AGENCY § 312 (1958).

²⁰ [1933] 1 Ch. 65 (C.A.).

²¹ *Butler v. Attwood*, 369 F.2d 811, 820 (6th Cir. 1966).

contract as an agent of the plaintiff. The district court had found that the conduct of the parties demonstrated that the buyer was not intended by the parties' agreement or acts to be an agent of the plaintiff.²² It thus seems doubtful that the court of appeals was correct, at least on the basis of agency principles.

The impact of the Sixth Circuit's decision will be that courts, in order to achieve justice, will find a fiduciary or agency relationship which the parties never intended; this may cause injustice if the "principal" himself decides not to purchase the shares. In the instant case, even if the plaintiff had not wanted to buy the shares, he would have been obligated to, since he, as principal, would be liable to the sellers upon the Attwood-Finzel contract made by his agent, the buyer, acting within the scope of authority.²³

Another approach the Sixth Circuit could have adopted would be to interpret the Butler-Attwood contract as a traditional bilateral conditional option contract.²⁴ Various types of option contracts exist in which the optionee can elect between alternatives.²⁵ Under such a contract, the optionee has a conditional right to performance with a power to make that right unconditional by fulfilling at his discretion, the conditions of the contract.²⁶

By analogy, in conditional land option contracts the prevailing view is that if the option is based on valuable consideration, the option contract creates an equitable property interest for the optionee.²⁷ Under this view the optionee is vested with the right to

²² *Butler v. Attwood*, Civ. No. 25165, E.D. Mich., Aug. 2, 1965. On appeal the buyer argued that the plaintiff never considered the buyer his agent because after the plaintiff became aware of the Attwood-Finzel contract, the plaintiff chose not to contact his supposed "agent" but rather to contact his attorney who communicated to the sellers the plaintiff's desire to buy the shares. See Brief for Defendants-Appellees, p. 19, *Butler v. Attwood*, 369 F.2d 811 (6th Cir. 1966).

²³ For a discussion of this liability, see *Weeks v. United States*, 245 U.S. 618 (1918); *Dobson Coal Co. v. Delano*, 266 Pa. 560, 109 Atl. 676 (1920).

²⁴ This contract between the plaintiff and the buyer could have been interpreted to mean that "The plaintiff promises to sell fifty percent of the stock if he gets any and if the buyer gives the plaintiff notice within a reasonable time in exchange for the buyer's identical promise to sell fifty percent of the stock if he gets any and if the plaintiff gives the buyer notice within a reasonable time."

²⁵ Corbin, *Option Contracts*, 23 YALE L.J. 641 (1914).

²⁶ 1A CORBIN, CONTRACTS § 210, at 566-68 (1963); 1 WILLISTON, CONTRACTS § 61B, at 199-200 (3d ed. 1957).

²⁷ See, e.g., *House v. Jackson*, 24 Ore. 89, 32 Pac. 1027 (1893); *Kerr v. Day*, 14 Pa. 112 (1850); *Telford v. Frost*, 76 Wis. 172, 44 N.W. 835 (1890). *Contra*, *Richardson v. Hardwick*, 106 U.S. 252, 254 (1882); *Bostwick v. Hess*, 80 Ill. 138 (1875); *Gustin v. Union School-Dist.*, 94 Mich. 502, 54 N.W. 156 (1893). Professor Corbin asserts that an option unsupported by consideration gives the optionee no interest in the land because the option then becomes a mere offer to sell. However, where the

acquire an interest in the land, which when exercised by giving notice, entitles him to specific performance against the optionor²⁸ or a subsequent purchaser with notice of the irrevocable option.²⁹

In the instant case, if the Sixth Circuit had interpreted the Butler-Attwood contract as a bilateral conditional option contract, the court could have found that the plaintiff had an enforceable interest assertible against the sellers. Similarly, the court could have reasoned that the antecedent contract was a bilateral option contract to convey stock with an express condition that notice had to be given before conveyance could be required. Since the plaintiff-optionee wanted the stock, he gave notice to the buyer-optionor.³⁰ Notice by the optionee was not an acceptance of an offer but was a fulfillment of a condition precedent to the optionor's liability on the Butler-Attwood contract.³¹ Following the reasoning of the land option contract cases,³² the option contract vested in the optionee the right to acquire a one half interest in the stock contract between the optionor and the sellers, which entitled him, upon his giving notice of intent to purchase, to specific performance against the optionor and the sellers.

Although the Sixth Circuit granted relief to the plaintiff against the sellers, it did so by finding a fiduciary relationship which was intended by neither the plaintiff nor the buyer. A better approach for a court to take when interpreting similar contracts is to treat them as conditional option contracts, thus taking into account the intention of the parties. Moreover, a court under the conditional option approach will be prevented from finding that a person must purchase stock he never intended to acquire. An individ-

option is a conditional contract to convey, Corbin feels that the optionee should be held to have an interest in the land. Corbin, *supra* note 25, at 660.

²⁸ The optionee has a contractual right enforceable against the optionor. See, e.g., Guyer v. Warren, 175 Ill. 328, 51 N.E. 580 (1898); O'Brien v. Roland, 166 Mass. 481, 44 N.E. 502 (1896); Hawralty v. Warren, 18 N.J. Eq. 124 (Ch. 1866); Watkins v. Robertson, 105 Va. 269, 54 S.E. 33 (1906).

³³ The optionee has a contractual right enforceable against a third party. See, e.g., Smith v. Bangham, 156 Cal. 359, 104 Pac. 689 (1909); Tucker v. Connors, 342 Mass. 376, 173 N.E.2d 619 (1961); Barrett v. McAllister, 33 W. Va. 738, 11 S.E. 220 (1890); Sizer v. Clark, 116 Wis. 534, 93 N.W. 539 (1903); 1 WILLISTON, *op. cit. supra* note 26, § 61C, at 203 n.20. *Contra*, Varn Turpentine & Cattle Co. v. Allen, 38 Ga. App. 408, 144 S.E. 47 (1928). One eminent authority has stated that the reason the option can be enforced against such an assignee is that the optionee has a contract right which ought to be respected by third persons. 1A CORBIN, *op. cit. supra* note 26, § 272, at 581-82.

³⁰ Butler v. Attwood, 369 F.2d 811, 812 (6th Cir. 1966).

³¹ Corbin, *supra* note 25, at 650.

³² For a discussion of the conditional land option contract cases, see notes 27-28 *supra* and accompanying text.