

Dodge v. Ford Motor Co.
170 N.W. 668 (Mich. 1919)

No special dividend having been paid after October, 1915 (a special dividend of \$2,000,000 was declared in November, 1916, before the filing of the answers), the plaintiffs, who together own 2,000 shares, or one-tenth of the entire capital stock of the Ford Motor Company, on the 2d of November, 1916, filed in the circuit court for the county of Wayne, in chancery, their bill of complaint, which bill was later, upon leave granted, on April 26, 1917, amended, in which bill they charge that since 1914 they have not been represented on the board of directors of the Ford Motor Company, and that since that time the policy of the board of directors has been dominated and controlled absolutely by Henry Ford, the president of the company, who owns and for several years has owned 58 per cent. of the entire capital stock of the company; that the directors of the company are Henry Ford, David H. Gray, Horace H. Rackham, F. L. Klingensmith, and James Couzens, and the executive officers Henry Ford, president, F. L. Klingensmith, treasurer, and Edsel B. Ford, son of Henry Ford, secretary; that after the filing of the original, and before the filing of the amended, bill, at the annual meeting of the stockholders, David H. Gray retired from the board of directors and Edsel B. Ford was elected and is acting as a director. Setting up that on the 31st of July, 1916, the end of its last fiscal year, the said Henry Ford gave out for publication a statement of the financial condition of the company (the same as hereinabove set out), that for a number of years a regular dividend, payable quarterly, equal to 5 per cent. monthly upon the authorized capital stock, and the special dividends hereinbefore referred to, had been paid, it is charged that notwithstanding the earnings for the fiscal year ending July 31, 1916, the Ford Motor Company has not since that date declared any special dividends:

‘And the said Henry Ford, president of the company, has declared it to be the settled policy of the company not to pay in the future any special dividends, but to put back into the business for the future all of the earnings of the company, other than the regular dividend of five per cent. (5%) monthly upon the authorized capital stock of the company—two million dollars (\$2,000,000).’

This declaration of the future policy, it is charged in the bill, was published in the public press in the city of Detroit and throughout the United States in substantially the following language:

‘My ambition,’ declared Mr. Ford, ‘is to employ still more men; to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this, we are putting the greatest share of our profits back into the business.’

It is charged further that the said Henry Ford stated to plaintiffs personally, in substance, that as all the stockholders had received back in dividends more than they had invested they were not entitled to receive anything additional to the regular dividend of 5 per cent. a month, and that it was not his policy to have larger dividends declared in the future, and that the profits and earnings of the company would be put back into the business for the purpose of extending its operations and increasing the number of its employes, and that, inasmuch as the profits were to be represented by investment in plants and capital investment, the stockholders would have no right to complain.

Setting up unsuccessful efforts to secure a conference with Mr. Ford for the purpose of discussing the question and asking that there be a distribution of a part of the accumulations, it

is charged: That on September 28, 1916, plaintiffs addressed to him, and had delivered to him by registered letter, the following communication:

‘We have for some time, as you know, been endeavoring to make an appointment to see you, for the purpose—as you assumed and informed one of your associates—of discussing the affairs of the Ford Motor Company from the standpoint of our interest as stockholders and with a view to securing action by the board of directors looking to a very substantial distribution from its cash surplus as dividends.

‘Not having been able to make an appointment to discuss the matter with you personally, as we very much desired to do, we write you this letter upon the subject.

‘The conditions shown by your recent financial statement—showing approximately \$60,000,000 of net profits for the past year and cash surplus in bank exceeding \$50,000,000—it seems to us would suggest, without the action being requested, the propriety of the board taking prompt action to distribute a large part of the accumulated cash surplus as dividends to the stockholders to whom it belongs.

‘While we would be sorry to have any controversy over the matter, we feel that your attitude toward the stockholders of the company is entirely unwarranted.

‘The statements that you have made—that the stockholders are and have been receiving as dividends all they are entitled to—shows a most extraordinary state of mind if it represents your real feelings.

‘While a dividend of five per cent. per month, sixty per cent. per annum, on the capital stock of the company, \$2,000,000, on its face would seem to be a large dividend—the fact is, however, that the assets of the company representing its surplus is as much the property of the stockholders as the assets representing the capital stock and the stockholders are as much entitled to a dividend that will give them returns on their surplus investment as their capital stock.

‘Looking at the situation in this way, the dividend being paid the stockholders is only a little above one per cent. on their capital employed in the business and entirely out of proportion to what the stockholders are entitled to.

‘In view of the existing circumstances, we ask that you promptly call a meeting of the board of directors to consider the situation and lay before them our views as stockholders as outlined in this letter, and we desire to say in this connection that we conceive it to be the duty of the board of directors to distribute as a minimum a special dividend of not less than fifty per cent. of the accumulated cash surplus of the company.

‘We would be pleased to have your acknowledgment of the receipt of this letter and advise that you have called a meeting of the board of directors for the purpose of considering and acting upon the matters referred to in it.’

And that they sent on the same day copies to each of the members of the board of directors of the Ford Motor Company, and one to Edsel B. Ford, secretary. That, although the said Henry Ford and each of the directors were in the city of Detroit at the time of the receipt of such communication, no attention was paid to it and no acknowledgment made by said Henry Ford personally, but in his behalf his son, Edsel, under date October 10, 1916, replied:

‘I beg to acknowledge due receipt of your letter of September 23, 1916, and to say that it would have been answered before this but for my absence from town for a considerable length of time and pressure of other matters.

‘It seems to me, in view of all the conditions of business and our extensions, which have been determined upon for so long a time past and to which we have been working, that it would not be wise to increase the dividends at the present time—but, nevertheless, I will lay your letter

before the board of directors and we will give your views regarding the increase of dividends and extensions full consideration at our next meeting.’

Paragraphs 26, 27, and 28 of the bill read:

‘(26) That unless restrained by the injunction of this honorable court, the said Henry Ford will cause the cash assets that would otherwise be available for dividends, to be disbursed and invested in fixed capital assets.

‘(27) In the face of the increased labor and material cost and the uncertain conditions that will prevail in the business world at the termination of the present world war, the policy of said Henry Ford, in continuing the expansion of the business of said corporation, is reckless in the extreme and seriously jeopardizes the interest of your orators as stockholders in said corporation.

‘(28) That there are many other corporations engaged in the business of manufacturing cars in competition with the only car manufactured by the Ford Motor Company, to wit, the class recognized in the trade as ‘low-priced cars.’ That the annual production of such other companies of such class of cars runs into the hundreds of thousands of cars per annum. That if the said Henry Ford is permitted to continue the policy that he has inaugurated and announced he is determined to carry out, of increasing production, reducing the price of cars, and increasing the capital investments in the conduct of such business by withholding the dividends from stockholders to which they are entitled, the necessary result will be the destruction of competition on the sale of the class of cars manufactured by such corporation and the creation of a complete monopoly in the manufacture and sale of such cars in violation of the state, federal and common law.’

Plaintiffs ask for ... a decree requiring the distribution to stockholders of at least 75 per cent. of the accumulated cash surplus, and for the future that they be required to distribute all of the earnings of the company except such as may be reasonably required for emergency purposes in the conduct of the business.

The answer of Henry Ford ... denies that he has declared it to be the settled policy of the company not to pay any special dividends but to put back into the business for the future all the earnings of the company other than the regular dividends of 5 per cent. monthly. He denies that he made a declaration as to his future policy as controlling stockholder in fixing the policy for the management of the corporation. He admits that he used the language substantially set out in the 13th paragraph of the bill, hereinbefore set out, and he does not deny, but admits, that his ambition is as therein stated, but that his action as a director will be controlled by future conditions and with due respect to the interests of all concerned. He declares that he has been and always is open to argument and conviction as to what is best and what is right in the conduct of the affairs of the Ford Motor Company. He denies that he stated personally to plaintiffs in substance that as all of the stockholders had received back in dividends more than they had invested they were not entitled to receive anything additional to the regular dividend of 5 per cent. per month, and that it was not his policy to have larger dividends declared in the future, and that the proceeds and earnings of the company would be put back into the business, etc.

The cause came on for hearing in open court on the 21st of May, 1917. A large volume of testimony was taken, with the result that a decree was entered December 5, 1917, in and by which it is decreed that within 30 days from the entry thereof the directors of the Ford Motor Company declare a dividend upon all of the shares of stock in an amount equivalent to one-half of, and payable out of, the accumulated cash surplus of said Ford Motor Company, on hand at

the close of the fiscal year ending July 31, 1916, less the aggregate amount of the special dividends declared and paid after the filing of the bill and during the year ending July 31, 1917; the amount to be declared being \$19,275,385.96.

Defendants have appealed, plaintiffs have not appealed, from the decree. In the briefs, appellants state and discuss the following propositions:

...

'(4) The management of the corporation and its affairs rests in the board of directors, and no court will interfere or substitute its judgment so long as the proposed actions are not ultra vires or fraudulent. They may be ill advised, in the opinion of the court, but this is no ground for exercise of jurisdiction.

'(5) The board has full power over the matter of investing the surplus and as to dividends so long as they act in good faith.

'(6) Such rights of management and control over investments and dividends are not only rules of law, they are rights fixed by the contract between the parties in the formation of the corporation.

'(7) These things are so although the majority of the stock is held by one man.

'It is the right and the duty of the majority to control. This duty must be exercised, and the responsibility cannot be shifted or evaded.

'(8) Motives of the board members are not material and will not be inquired into by the court so long as the acts are within their lawful powers.

'(9) Motives of a humanitarian character will not invalidate or form the basis of any relief so long as the acts are within the lawful powers of the board, if believed to be for the permanent welfare of the company.

OSTRANDER, CJ. (after stating the facts as above)

The rule which will govern courts in deciding these questions is not in dispute. It is, of course, differently phrased by judges and by authors, and, as the phrasing in a particular instance may seem to lean for or against the exercise of the right of judicial interference with the actions of corporate directors, the context, or the facts before the court, must be considered. This court, in *Hunter v. Roberts, Throp & Co.*, 83 Mich. 63, 71, 47 N. W. 131, 134, recognized the rule in the following language:

'It is a well-recognized principle of law that the directors of a corporation, and they alone, have the power to declare a dividend of the earnings of the corporation, and to determine its amount. 5 AMER. & ENG. ENC. LAW, 725. Courts of equity will not interfere in the management of the directors unless it is clearly made to appear that they are guilty of fraud or misappropriation of the corporate funds, or refuse to declare a dividend when the corporation has a surplus of net profits which it can, without detriment to its business, divide among its stockholders, and when a refusal to do so would amount to such an abuse of discretion as would constitute a fraud, or breach of that good faith which they are bound to exercise towards the stockholders.'

In Cook on Corporations (7th Ed.) § 545, it is expressed as follows:

'The board of directors declare the dividends, and it is for the directors, and not the stockholders, to determine whether or not a dividend shall be declared.

'When, therefore, the directors have exercised this discretion and refused to declare a dividend, there will be no interference by the courts with their decision, unless they are guilty of a willful abuse of their discretionary powers, or of bad faith or of a neglect of duty. It requires a very strong case to induce a court of equity to order the directors to declare a dividend, inasmuch as equity has no jurisdiction, unless fraud or a breach of trust is involved. There have been many

attempts to sustain such a suit, yet, although the courts do not disclaim jurisdiction, they have quite uniformly refused to interfere. The discretion of the directors will not be interfered with by the courts, unless there has been bad faith, willful neglect, or abuse of discretion.

‘Accordingly, the directors may, in the fair exercise of their discretion, invest profits to extend and develop the business, and a reasonable use of the profits to provide additional facilities for the business cannot be objected to or enjoined by the stockholders.’

In *Morawetz on Corporations* (2d Ed.) § 447, it is stated:

‘Profits earned by a corporation may be divided among its shareholders, but it is not a violation of the charter if they are allowed to accumulate and remain invested in the company’s business. The managing agents of a corporation are impliedly invested with a discretionary power with regard to the time and manner of distributing its profits. They may apply profits in payment of floating or funded debts, or in development of the company’s business; and so long as they do not abuse their discretionary powers, or violate the company’s charter, the courts cannot interfere.

‘But it is clear that the agents of a corporation, and even the majority, cannot arbitrarily withhold profits earned by the company, or apply them to any use which is not authorized by the company’s charter. The nominal capital of a company does not necessarily limit the scope of its operations; a corporation may borrow money for the purpose of enlarging its business, and in many instances it may use profits for the same purpose. But the amount of the capital contributed by the shareholders is an important element in determining the limit beyond which the company’s business cannot be extended by the investment of profits. If a corporation is formed with a capital of \$100,000 in order to carry on a certain business, no one would hesitate to say that it would be a departure from the intention of the founders to withhold profits, in order to develop the company’s business, until the sum of \$500,000 had been amassed, unless the company was formed mainly for the purpose of accumulating the profits from year to year. The question in each case depends upon the use to which the capital is put and the meaning of the company’s charter. If a majority of the shareholders or the directors of a corporation wrongfully refuse to declare a dividend and distribute profits earned by the company, any shareholder feeling aggrieved may obtain relief in a court of equity.

‘It may often be reasonable to withhold part of the earnings of a corporation in order to increase its surplus fund, when it would not be reasonable to withhold all the earnings for that purpose. The shareholders forming an ordinary business corporation expect to obtain the profits of their investment in the form of regular dividends. To withhold the entire profits merely to enlarge the capacity of the company’s business would defeat their just expectations. After the business of a corporation has been brought to a prosperous condition, and necessary provision has been made for future prosperity, a reasonable share of the profits should be applied in the payment of regular dividends, though a part may be reserved to increase the surplus and enlarge the business itself.’

One other statement may be given from *Park v. Grant Locomotive Works*, 40 N. J. Eq. 114, 3 Atl. 162 (45 N. J. Eq. 244, 19 Atl. 621):

‘In cases where the power of the directors of a corporation is without limitation, and free from restraint, they are at liberty to exercise a very liberal discretion as to what disposition shall be made of the gains of the business of the corporation. Their power over them is absolute so long as they act in the exercise of their honest judgment. They may reserve of them whatever their judgment approves as necessary or judicious for repairs or improvements, and to meet contingencies, both present and prospective. And their determination in respect of these matters, if made in good faith and for honest ends, though the result may show that it was injudicious, is final, and not subject to judicial revision.’

It is not necessary to multiply statements of the rule.

To develop the points now discussed, and to a considerable extent they may be developed together as a single point, it is necessary to refer with some particularity to the facts.

When plaintiffs made their complaint and demand for further dividends, the Ford Motor Company had concluded its most prosperous year of business. The demand for its cars at the price of the preceding year continued. It could make and could market in the year beginning August 1, 1916, more than 500,000 cars. Sales of parts and repairs would necessarily increase. The cost of materials was likely to advance, and perhaps the price of labor; but it reasonably might have expected a profit for the year of upwards of \$60,000,000. It had assets of more than \$132,000,000, a surplus of almost \$112,000,000, and its cash on hand and municipal bonds were nearly \$54,000,000. Its total liabilities, including capital stock, was a little over \$20,000,000. It had declared no special dividend during the business year except the October, 1915, dividend. It had been the practice, under similar circumstances, to declare larger dividends. Considering only these facts, a refusal to declare and pay further dividends appears to be not an exercise of discretion on the part of the directors, but an arbitrary refusal to do what the circumstances required to be done. These facts and others call upon the directors to justify their action, or failure or refusal to act. In justification, the defendants have offered testimony tending to prove, and which does prove, the following facts: It had been the policy of the corporation for a considerable time to annually reduce the selling price of cars, while keeping up, or improving, their quality. As early as in June, 1915, a general plan for the expansion of the productive capacity of the concern by a practical duplication of its plant had been talked over by the executive officers and directors and agreed upon; not all of the details having been settled, and no formal action of directors having been taken. The erection of a smelter was considered, and engineering and other data in connection therewith secured. In consequence, it was determined not to reduce the selling price of cars for the year beginning August 1, 1915, but to maintain the price and to accumulate a large surplus to pay for the proposed expansion of plant and equipment, and perhaps to build a plant for smelting ore. It is hoped, by Mr. Ford, that eventually 1,000,000 cars will be annually produced. The contemplated changes will permit the increased output.

The plan, as affecting the profits of the business for the year beginning August 1, 1916, and thereafter, calls for a reduction in the selling price of the cars. It is true that this price might be at any time increased, but the plan called for the reduction in price of \$80 a car. The capacity of the plant, without the additions thereto voted to be made (without a part of them at least), would produce more than 600,000 cars annually. This number, and more, could have been sold for \$440 instead of \$360, a difference in the return for capital, labor, and materials employed of at least \$48,000,000. In short, the plan does not call for and is not intended to produce immediately a more profitable business, but a less profitable one; not only less profitable than formerly, but less profitable than it is admitted it might be made. The apparent immediate effect will be to diminish the value of shares and the returns to shareholders.

It is the contention of plaintiffs that the apparent effect of the plan is intended to be the continued and continuing effect of it, and that it is deliberately proposed, not of record and not by official corporate declaration, but nevertheless proposed, to continue the corporation henceforth as a semi-*elemosynary* institution and not as a business institution. In support of this contention, they point to the attitude and to the expressions of Mr. Henry Ford.

Mr. Henry Ford is the dominant force in the business of the Ford Motor Company. No plan of operations could be adopted unless he consented, and no board of directors can be elected whom he does not favor. One of the directors of the company has no stock. One share

was assigned to him to qualify him for the position, but it is not claimed that he owns it. A business, one of the largest in the world, and one of the most profitable, has been built up. It employs many men, at good pay.

‘My ambition,’ said Mr. Ford, ‘is to employ still more men, to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this we are putting the greatest share of our profits back in the business.’

‘With regard to dividends, the company paid sixty per cent. on its capitalization of two million dollars, or \$1,200,000, leaving \$58,000,000 to reinvest for the growth of the company. This is Mr. Ford’s policy at present, and it is understood that the other stockholders cheerfully accede to this plan.’

He had made up his mind in the summer of 1916 that no dividends other than the regular dividends should be paid, ‘for the present.’

‘Q. For how long? Had you fixed in your mind any time in the future, when you were going to pay— A. No.

‘Q. That was indefinite in the future? A. That was indefinite; yes, sir.’

The record, and especially the testimony of Mr. Ford, convinces that he has to some extent the attitude towards shareholders of one who has dispensed and distributed to them large gains and that they should be content to take what he chooses to give. His testimony creates the impression, also, that he thinks the Ford Motor Company has made too much money, has had too large profits, and that, although large profits might be still earned, a sharing of them with the public, by reducing the price of the output of the company, ought to be undertaken. We have no doubt that certain sentiments, philanthropic and altruistic, creditable to Mr. Ford, had large influence in determining the policy to be pursued by the Ford Motor Company—the policy which has been herein referred to.

It is said by his counsel that—

‘Although a manufacturing corporation cannot engage in humanitarian works as its principal business, the fact that it is organized for profit does not prevent the existence of implied powers to carry on with humanitarian motives such charitable works as are incidental to the main business of the corporation.’

And again:

‘As the expenditures complained of are being made in an expansion of the business which the company is organized to carry on, and for purposes within the powers of the corporation as hereinbefore shown, the question is as to whether such expenditures are rendered illegal because influenced to some extent by humanitarian motives and purposes on the part of the members of the board of directors.’

In discussing this proposition, counsel have referred to decisions such as *Hawes v. Oakland*, 104 U. S. 450, 26 L. Ed. 827; *Taunton v. Royal Ins. Co.*, 2 Hem. & Miller, 135; *Henderson v. Bank of Australia*, L. R. 40 Ch. Div. 170; *Steinway v. Steinway & Sons*, 17 Misc. Rep. 43, 40 N. Y. Supp. 718; *People v. Hotchkiss*, 136 App. Div. 150, 120 N. Y. Supp. 649. These cases, after all, like all others in which the subject is treated, turn finally upon the point, the question, whether it appears that the directors were not acting for the best interests of the corporation. We do not draw in question, nor do counsel for the plaintiffs do so, the validity of

the general proposition stated by counsel nor the soundness of the opinions delivered in the cases cited. The case presented here is not like any of them. The difference between an incidental humanitarian expenditure of corporate funds for the benefit of the employes, like the building of a hospital for their use and the employment of agencies for the betterment of their condition, and a general purpose and plan to benefit mankind at the expense of others, is obvious. There should be no confusion (of which there is evidence) of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his codirectors owe to protesting, minority stockholders. A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.

There is committed to the discretion of directors, a discretion to be exercised in good faith, the infinite details of business, including the wages which shall be paid to employes, the number of hours they shall work, the conditions under which labor shall be carried on, and the price for which products shall be offered to the public.

It is said by appellants that the motives of the board members are not material and will not be inquired into by the court so long as their acts are within their lawful powers. As we have pointed out, and the proposition does not require argument to sustain it, it is not within the lawful powers of a board of directors to shape and conduct the affairs of a corporation for the merely incidental benefit of shareholders and for the primary purpose of benefiting others, and no one will contend that, if the avowed purpose of the defendant directors was to sacrifice the interests of shareholders, it would not be the duty of the courts to interfere.

We are not, however, persuaded that we should interfere with the proposed expansion of the business of the Ford Motor Company. In view of the fact that the selling price of products may be increased at any time, the ultimate results of the larger business cannot be certainly estimated. The judges are not business experts. It is recognized that plans must often be made for a long future, for expected competition, for a continuing as well as an immediately profitable venture. The experience of the Ford Motor Company is evidence of capable management of its affairs. It may be noticed, incidentally, that it took from the public the money required for the execution of its plan, and that the very considerable salaries paid to Mr. Ford and to certain executive officers and employes were not diminished. We are not satisfied that the alleged motives of the directors, in so far as they are reflected in the conduct of the business, menace the interests of shareholders. It is enough to say, perhaps, that the court of equity is at all times open to complaining shareholders having a just grievance.

Assuming the general plan and policy of expansion and the details of it to have been sufficiently, formally, approved at the October and November, 1917, meetings of directors, and assuming further that the plan and policy and the details agreed upon were for the best ultimate interest of the company and therefore of its shareholders, what does it amount to in justification of a refusal to declare and pay a special dividend or dividends? The Ford Motor Company was able to estimate with nicety its income and profit. It could sell more cars than it could make. Having ascertained what it would cost to produce a car and to sell it, the profit upon each car depended upon the selling price. That being fixed, the yearly income and profit was determinable, and, within slight variations, was certain.

Defendants say, and it is true, that a considerable cash balance must be at all times carried by such a concern. But, as has been stated, there was a large daily, weekly, monthly,

receipt of cash. The output was practically continuous and was continuously, and within a few days, turned into cash. Moreover, the contemplated expenditures were not to be immediately made. The large sum appropriated for the smelter plant was payable over a considerable period of time. So that, without going further, it would appear that, accepting and approving the plan of the directors, it was their duty to distribute on or near the 1st of August, 1916, a very large sum of money to stockholders.

In reaching this conclusion, we do not ignore, but recognize, the validity of the proposition that plaintiffs have from the beginning profited by, if they have not lately, officially, participated in, the general policy of expansion pursued by this corporation. We do not lose sight of the fact that it had been, upon an occasion, agreeable to the plaintiffs to increase the capital stock to \$100,000,000 by a stock dividend of \$98,000,000. These things go only to answer other contentions now made by plaintiffs, and do not and cannot operate to estop them to demand proper dividends upon the stock they own. It is obvious that an annual dividend of 60 per cent. upon \$2,000,000, or \$1,200,000, is the equivalent of a very small dividend upon \$100,000,000, or more.

The decree of the court below fixing and determining the specific amount to be distributed to stockholders is affirmed.