

1895

# Contractual and Non-Contractual Provisions in Corporate Charters

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C O N T R A C T U A L   A N D   N O N - C O N T R A C T U A L  
P R O V I S I O N S   I N   C O R P O R A T E   C H A R T E R S

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Presented for the Degree of

Master of Laws.

by

Benjamin Fagan, LL.B.

Cornell University.

1895.



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## Introduction

The subject of this thesis owes its origin to the celebrated Dartmouth College Case, around whose mighty form the roots of all subsequent adjudications upon collateral stipulations in corporate charters, are so entwined, that to overturn it would destroy all its vigorous offspring which lie like flaming mile-stones along the pathway of vested corporate rights.

This case contains one of the fullest and most elaborate expositions of the sanctity of vested corporate rights to be found in any of the law reports, and though three quarters of a century has now elapsed since the United States Court speaking through Chief Justice Marshall, declared that a charter to a private corporation was a contract between the state and corporators inviolable by the clause in the constitution forbidding a state to impair the

obligation of contract; yet, the decision has stood from the day it was made until the present hour, as a bulwark under whose sheltering protection corporations have grown so powerful and aggressive that nearly all the states found it necessary in order to preserve their inherent powers of government, to act upon the suggestion made by Justice Story in his concurring opinion, and insert in their constitutions a provision to the effect, "that all charters hereafter granted may be altered from time to time or repealed".

The principle enunciated in the case last mentioned, has become so firmly imbedded in our jurisprudence, that any attempt to show that the case was wrongly decided, however sound and logical, would have no practical value. It is now too late a day to attack the soundness of a decision, which has for three quarters of a century, withstood all the tests known to the judicial mind. And which

because of the unparalleled exposition of the sanity of corporate contracts, and the learning and integrity of the court, have caused the profession to regard it with almost veneration.

The real cause of apprehension resulting from this case, is, the unwarrantable extension of the principles therein, which corporations seek to obtain by skilful and ingenious construction, and the use of the "sly and stealthy arts" so often practised by those interested in the extension of corporate privileges.

It being settled then that the charter of a private corporation is a contract which the state may not impair; the next question which presents itself for our consideration is,- are all the collateral stipulations which the charter may contain, which are not necessary to corporate existence, or the accomplishment of the principal objects of its



creation, but which may be very useful and beneficial thereto and which limit the exercise of the sovereign powers,- are they also contracts within the meaning of the constitution? The collateral stipulations of this kind may be grouped into three classes: those which limit the states power of taxation; those which limit the states power of eminent-domain, and those which limit the states police power. And the subsequent pages will be devoted to treating these three essential attributes of sovereignty in the order indicated.

#### Taxation

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Taxation is defined to be "the imposition of a tax; the act or process of imposing and levying a pecuniary or enforced contribution, ratable, or proportionate to value or some other standard, upon persons or property, by or on behalf of a government or one of its divisions or agencies, for the purpose of providing revenue for the maintenance

and expenses of the government". Black's Law Dictionary.

Now, the power of taxation being inherent in every sovereignty, and one of the most essential powers of government can a state by contract bargain away its right, and the right of future legislators to exercise this function? The answer to this question has given rise to an incalculable amount of litigation in both state and Federal courts, and though the United States Courts have invariably answered in the affirmative, yet, their decisions have usually been accompanied by a strong, earnest protest from the minority<sup>(1)</sup> and from the state courts,<sup>(2)</sup> to the effect, that such pledges are impolitic and unwise, and there is always the possibility that if sustained, they might be carried to the extreme of crippling the sovereign power of the state to perform its accustomed function. And therefore, such pledges or limitations could not constitutionally be made; for no legislature is competent to limit

the powers of its successor, but must transmit to those who come after it the complete power which it received from its predecessor.

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New-Jersey V. Wilson,----- 7 Cranch, 164.  
Gorden V. The App. Tax Court, ----- 3 Iow. 1333  
Ohio Life Ins. Co.,V. Debbolt, ----- 16 Iow. 416.  
Piqua Bank V. Knoup, ----- 16 Iow. 369.  
Dodge V. Woodlsey, -----59- 18 Iow. 331.  
Mechanics & Traders B. V. Debolt, --- 18 Iow. 380.  
Home Of The Friendless V. Rouse, -----8 Wall. 430.  
Washington Univ. V. Rouse, -----8 Wall. 439.  
Willmington &c. R. R. V. Reid, -----13 Wall. 264.  
Raleigh Etc. R. R. Co., V. "" ----- 13 Wall. 269.

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Debolt V. Ohio Life Ins. Co., -----1 Ohio St. 563.  
Mechanics Bank V. Debolt,-----1 Ohio St. 591.  
Brewster V. Iough, -----10 N. I. 138.  
Mott V. Penn. R. R. Co., ----- 30 Penn. St. 9.

But the supreme court in the early case of New-Jersey V. Wilson; in which the facts were that a legislative act

declared that certain lands which should be purchased for the Indians, should not thereafter be subject to any tax, held, that this constituted a contract which could not be rescinded by a subsequent legislative act.

The right of a state to sell out for a consideration her taxing power, was strenuously denied by the courts of Ohio in the following cases:

Debolt V. Life Ins. Co., -----	I Ohio St. 583.
Mechanics & Traders Bank V. Debolt, --	I "" "" . 591.
Knoup V. Piqua Bank, -----	I "" "" . 603.
Toledo Bank V. Bond, -----	I "" "" . 621.

In the two cases first mentioned, the court emphatically declared that bank charters are not contracts, and in all it declared that stipulations in regard taxation are not binding upon the state, and not a contract protected by the United States Constitution. Their conclusion was based upon the argument already indicated; that the power of taxation being

a part of the state sovereignty, is not the subject of contract, barter or sale by the legislature. And any attempt to make such a contract would be fraud upon the government and of necessity void.

From these decisions an appeal was taken to the United-States Supreme Court where the sophistry of the Ohio judges was quickly brushed away. Two years later, (1855), other

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cases from Ohio involving the same principle were decided by the Supreme Court, and they adhered strictly to their reasoning in the other cases of this kind, and reaffirmed their previous conclusion that collateral stipulations limiting the taxing power, was a contract which future legislators could not impair. But Ohio's highest tribunal was not so easily convinced that her position was untenable, and after submitting

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Dodge V. Woolsey, ----- 18 low. 331.  
Mechanics & Traders B., V. Debolt, ----- 18 " " . 380.

to the authority of the National Tribunal in Matney V. Gold-

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-man and State V. Moore; returned again to their old plat-

-form when the cases of Sandusky Bank V. Wilbur and Skelly V.

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Jefferson Bank came before them for decision. The case last

mentioned was carried to the Supreme Court of the United -

States, in the foolish hope that that court would recede from

its former position, but instead of finding the court falter-

ing or waivering; they found it firm as the Rock of Ages. And

to further impress upon the minds of the tenacious Ohio judges

that they were the supreme tribunal, they declared that their

construction of the Constitution was authoritative, not only

upon individuals but upon states.

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5 Ohio State, ----- 481.

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8 " " " " -----606.

Thus, while the right and power of the state to contract away her taxing power, has been vigorously denied by the state courts, and questioned by authorities of the highest character, yet, the Supreme Court seems to have risen above the smoke of adverse criticism, and has, with calm, stately dignity, continued to pile up precedent after precedent until she has rendered her position almost invulnerable.

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But the intention of the state to so contract must be clear and unmistakable, and like contracts between individual must be supported by a consideration. "If it be a mere gratuity on the part of the state, made from motives of state

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Gorden V. The App. Tax Court, ----- 3 How. 133.  
Piqua Bank V. Knoup, ----- 16 "" 369.  
Washington Univ. V. Rouse, ----- 8 Wall. 439  
Home Of The Friendless V. Rouse, ----- 3 "" 430,  
Univ. V. People, ----- 99 U. S. 30  
and cases cited on P. 338; Cooley's Const. Limitations.

policy and forming no part of the inducement to the corporation, it is a mere bounty expressive only of the present will of the legislature upon the subject; and the law granting it like laws in general, is subject to modification or repeal in the legislative discretion.

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Therefore, "Staree Decisis that great principle,- the sheet-anchor of our jurisprudence, establishes beyond controversy that a limitation upon sovereign powers will never be implied. The rule of construction as adopted by the United Supreme Court in construing ambiguous grants to corporations,

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Christ Church V. Phila. -----	24 How. 300.
Salt Co. V. East Saginaw, -----	13 Wall. 373.
Parmely V. Railroad Co., -----	3 Dill. 25.
Tucker V. Furgerson, -----	22 Wall. 527.
West Wis. R. R. V. Supervisors, -----	93 U. S. 595.
Loge V. Railroad, -----	99 U. S. 348.
New Jersey V. Yard, -----	95 U. S. 104.



is well stated by Mr. Justice Swayne in Tucker v. Furgerson, who says: " The taxing power is vital to the functions of government. It helps to sustain the social compact and to give it efficacy. It is intended to promote the general welfare. It reaches the interest of every member of the community. It may be restrained by contract in special cases for the public good, where such contracts are not forbidden. But the contract must be shown to exist. there are no presumptions in its favor. Every reasonable doubt should be resolved against it. Where it exists it should be rigidly scrutinized, and never ~~be~~ permitted to extend, either in scope or duration, beyond what the terms of the concession clearly require. It is in derogation of ~~the~~ public right, and arrows a trust created for the good of all".

It would seem therefore, to be well settled, that a state may for a consideration, preclude herself for a time, or

or forever, from exercising her prerogative of taxation. But the contract containing this limitation, must be couched in language so plainly evidencing the intent of the state to so bind herself, that it will bear no other construction without doing violence to the words considered severally and as a whole.

--- Eminent Domain ---

Eminent domain is defined to be that sovereign power<sup>#</sup> vested in the people, by which they can, for any public purpose, take possession of the property of an individual upon just compensation paid to him."<sup>(1)</sup>

This right or power of the government to appropriate private property when the public needs require it, belongs to every government. It needs no constitutional provision to

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authorize its exercise. It is founded upon public exigency, according to the maxim, "Salus Rei Republicae lex suprema est," and springs up with the government itself. It seems to have been accurately defined and recognized in the Roman Empire during the days of Augustus and his immediate successors but was seldom resorted to because the right of way or the private property required for public use. We see, therefore, that this power exists wholly independent of constitutions. But in America and in most of the modern European states, we find provisions in the constitutions which forbid a state to exercise this power without making just compensation to the owner whose property is appropriated. Thus, in the code

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of Napoleon the limitation upon the sovereign power is expressed as follows: "No one can be compelled to give up his

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property, except for public good, and for a first and previous indemnity".

We have now reached the inquiry, whether any legislature can so tie up its hands that when the public exigency requires the exercise of eminent domain, they will be powerless to meet the public needs.

The state courts have long maintained that this power is one of the essential ~~elements~~ of sovereignty, often necessary to promote the public interest, and that one legislature has no power to enter into a contract that will restrain its

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free and repeated exercise. They did not deny that charters

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Railroad V. Railroad, ----- 97 Ill. 506.

Hyde Park V. Oakwood Cemetery, ----- 19 Ill. 141.

Enfield Tool Bridge V. Hartf. & N. H. R. R. 17 Conn. 40, 454.

Matter of Kerr, ----- 43 Barb.

Eastern R. R. V. B & M. R. R. ----- 111 Mass. 131.

were contracts, but held, that they, like all things of value, were subject to be taken by the right of eminent domain.

Indeed, this power of the state was never questioned until with the growth of corporations, the idea obtained that contracts with, and property of corporations, was more sacred than the same rights and property in individuals. The reasoning of the state courts upon this question appears to be logical and based upon sound principle. And though the United States Court has never passed upon the direct question of the states power to limit this <sup>right</sup> ~~power~~ by express contract; yet, from the dicta in cases in which it was urged that the sanctity of contract was impaired by the exercise of this power; it is plain that should the question ever arise, they will follow the state courts and declare that such contracts are in excess of authority and therefore void.

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The case of Charles River Bridge Co., V. Dix, is one of great importance upon this subject, and the following quotation from the opinion delivered by Judge Daniels, probably contains the best summary of the law of eminent domain, and throws the clearest light upon the attitude of the Supreme Court toward contracts of this kind, to be found in any of the law books. He says: "Under every established government, the tenure of property is derived mediately or immediately from the sovereign power of the political body, organized in such mode or exerted in such way as the community or state may have thought proper to ordain. It can rest on no other foundation; can have no other guarantee. It is owing to these characteristics only, that appeals can be made to the

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8 Howard, 507.

the laws either for the protection or assertion of the rights of property. Upon any other hypothesis, the law of property would be simply the law of force. Now it is undeniable that the investment of property in a citizen by the government; whether made for a pecuniary consideration or founded upon conditions of civil or political duty, is a contract between the state or government acting as its agent, and the grantee; and both parties thereto are bound to fulfill it. But into all contracts, whether made between the state and individuals, or between individuals only, there enters conditions which arise not out of the literal terms of the contract itself; they are superinduced by the preexisting and higher authority of the laws of nature; of nations or of the community to which the parties belong; they are always presumed, and must be presumed to be known and recognized by all, are binding

upon all, and need never, therefore, be carried into express stipulation; for this could add nothing to their force. Every contract is made in subordination to them, and must yield to their control as conditions inherent and paramount, whenever the necessity for their execution shall occur. Such is the right of eminent domain. This right does not operate to impair the contract effected by it, but recognizes its obligation to the fullest extent, claiming only the fulfillment of an inseparable condition. Thus in claiming the resumption or qualification of an investure, it insists merely on the true right and nature of the right invested. The impairment of contracts inhibited by the constitution, can scarcely by the greatest violence of construction, be made applicable to the enforcing of the terms or necessary import of the contract.



The language and meaning of the prohibition were intended to embrace proceedings attempting the interpolation of some new term or condition foreign to the original agreement, and therefore inconsistent with and violative thereof".

From this it is apparent that corporate franchises and every specie of property, may be entirely annihilated when in the descretion of the government it is needed to promote the public wellfare. That this should be so is obvious; for if it were otherwise, the state would be powerless to promote the improvments and progression which an ever advancing civilization requires.

It seems therefore, to be acknowledged on all sides that the obligation of contract is not impaired by the exercise of eminent domain, even though the entire subject matter thereof, be destroyed.

But this power of eminent domain must be carefully distinguished from taxation; for while it is analogous to eminent domain, in that the state may exact from its citizens or subjects, so much property as is required for public needs; yet the rule of compensation running through eminent domain, and the rules of apportionment governing the laying of taxes, shows clearly that there is a radical difference in principle. Private property taken by virtue of eminent domain, is not the proportion of property which the individual should contribute to the support of government as compensation for the rights and privileges secured thereunder, but as so much over and above his share, and therefore he is, with a few exceptions, entitled to compensation. While taxation, has no thought of compensation, except the benefits all derive from good government, and operates upon a class of persons or things

in accordance with well defined rules and without creating any liability by its exercise.

### Police Power.

Though many attempts have been made to define this important power by learned judges and text-writers; none have been entirely successful or without fault. In *Stone V. Mississippi*,<sup>(1)</sup> Waite C. J., realizing the impossibility of framing a definition that would be exactly accurate; refused to do so, saying that "it is always easier to determine whether a particular case comes within the scope of the <sup>general</sup> power, than to give an abstract definition of the power itself which will be in all respects accurate. Judge Cooley defines it as follows: The police of a state, in a comprehensive sense, embraces its whole system of internal regulation, by which the state seeks not only to

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preserve the public order and to prevent offenses against the state, but also to establish for the intercourse of citizens with citizens those rules of good manners and good neighborhood which are calculated to prevent a conflict of rights, and to insure to each the uninterrupted enjoyment of his own so far as it is reasonable consistent with a like enjoyment of rights by others".

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Blackstone defines public police and economy to be "the due regulation and domestic order of the Kingdom, whereby individuals of the state like members of a well governed family, are bound to conform their general behavior to the rules of propriety, good neighborhood, and good manners; and to be decent, industrious and inoffensive in their respective stations..

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Mr. Tiedeman in his valuable work on real-property defines it thus: "The conservation of private rights is attained by the imposition of wholesome restraint upon their exercise; such a restraint as will prevent the infliction injury upon others in the enjoyment of theirs; it would involve a provision and means of enforcing the legal maxim which underlies the fundamental rule of both human and national law: Sic Utere tuo ut alienum non laedas. The power of the government to impose this restraint is called police power. But probably as good a definition as has been given is found in New-Orleans

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Gas Co., V. Hart, where it is said: Police power is the right of the state functionaries to prescribe regulations for the good order, protection, comfort and convenience of the community which do not encroach upon the like power vested in

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congress by the Federal Constitution.

From this it is evident that the term police power is a flexible and comprehensive expression, and very difficult of exact definition. But although there has been much quarreling over the definition of police power, and however important it may be for text-writers to present an accurate definition of it; it is enough for our purpose to say that it extends to the preservation of the health, lives, property and morals of community.

This power resembles in several respects the power of the states last adverted to. It is, like that an inherent element of sovereignty, and so far inalienable that no legislature has the right or power to restrain subsequent legislatures from exercising the right as often as the public emergencies may require. Its preservation in full vigor, unrestricted by

any limitations are of vital importance in carrying out the ends for which governments are created. But like taxation it differs from eminent domain, in that it can be exercised without due compensation being made.

The courts have been ever ready <sup>to declare</sup> void and unconstitutional any legislative act which impaired the obligation of contract; but they have also been equally prompt in declaring ~~that~~ any legislative grant which in any way limited the legislative power over matters of internal police, a breach of the trust reposed in them by the people and therefore of no effect. <sup>(1)</sup>

And it is eminently wise and expedient that the state acting through its legislature should have the power to suppress all things dangerous to the welfare of society; for if it were

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People V. Morris, -----	13 Wend. 323
State V. Holmes, -----	38 N. H. 225.
Wyneharmer V. People, -----	3 Kern, 378.
State V. Miss., -----	101 U. S. 19.
License Cases, -----	5 How. 504.
Butchers Union, -----	111 U. S. 746-52
Beer Co. V. Mass. -----	97 U. S. 25.

not so, the legislature would be unable to remedy legislative grants, which in their time were wise and judicious, but which in the process of time has become a menace to the community in which the evil exists. This is well illustrated in the case

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Presbyterian Church v. City of New York. In that case the corporation of the City of New York, conveyed lands for the purpose of a church and cemetery, with a covenant for the quiet enjoyment; and afterwards, pursuant to a power granted by the legislature, passed a law prohibiting the use of these lands as a cemetery; held, that this was not a breach of the covenant which entitled to damages, but a repeal of the covenant, which did not impair the obligation of contract, for a corporation cannot by contract abridge their legislative power.

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The decisions of the state courts upon this subject, are so abundant and full in declaring that the law making department cannot divest itself of the power to regulate and abate all evil practises and vices hurtful to society, that discussion of even the leading cases would extend this thesis beyond all reasonable limits. And we will therefore at this point, turn our attention to the United States Courts, whose decisions upon this question must be regarded as final; and see if their adjudications have been as unanimous and to the same effect as those of the state courts.

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The case of *Boyd V. Alabama*, challenges our attention as squarely raising the question of the impairment of contract by the exercise of police power. In that case the defendant having been indicted under a statute of Alabama, for setting up

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and carrying on a lottery without legislative authority, claimed in defense a right to set up and carry on the lottery in question under a subsequent statute passed on the tenth of October, 1868: this later statute was repealed in 1871. The defendant claimed that the repeal of the act of 1868 authorizing him to set up and carry on a lottery, impaired the obligation of contract. But the question raised was not distinctly passed upon as the act was declared void <sup>because</sup> the object of it was not stated in the title as required by the state constitution. But the closing paragraph of the opinion given below, shows clearly that the court did not intend to be understood as saying, that if the statute had been constitutional it would have constituted an irrepealable contract between the state and the defendant. MR. Justice Field concluded the opinion in the case with the following words: "We are not prepared to

admit that it is competent for one legislature, by any contract with an individual, to restrain the power of a subsequent legislature to legislate for the public welfare, and to that end suppress any and all practices tending to corrupt the public morals". Citing Moore V. State, 48 Miss. 147, and Metropolitan Board of Excise, V. Barrie, 34 N. Y. 663.

The next case in point of order is that of Beer Co., V.

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Mass. There the franchise was that of manufacturing malt liquors in all their varieties in the City of Boston, and while the said Boston Beer Co., were transporting certain malt liquors

liquors to their place of business, in said county,

with intent there to sell them in violation of the act of the legislature of Massachusetts, passed June 19, 1869, Ch. 415, commonly known as the Prohibitory Liquor Law. The company

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claimed that under its charter granted in 1848, it had the right to manufacture said liquors; and that the said law impaired the obligation of contract contained in the charter, and was void so far as the liquors in question were concerned. Mr. Justice Bradley, speaking for the court, held, that the state could not make an irrevocable contract restricting the police power of the state; thus confirming the cautionary declaration in the case of *Boyd v. Alabama*.

Another leading case directly in point is that of *Fertilization Co., v. Hyde Park*. The fertilizing company was chartered by the Illinois legislature for the purpose of manufacturing and converting dead animals and other animal matter into an agricultural fertilizer, and other chemical products. When this charter was granted their works were

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located in a swampy and nearly uninhabited place, but now forming a part of the village of Hyde Park. Ordinances were passed prohibiting the carrying of this putrid animal matter through the streets, which the company claimed impaired the obligation of the contract conferred by their charter.

The court speaking through Judge Swayn, quoted the language of Justice Bradley in *Beer Co. V. Mass.*, and held that the charter conferred no irrepealable right for the fifty years of its duration to continue a practice injurious to the public health, citing many other cases in which the private right had to yield to the public good.

The last case to which I shall refer as establishing the proposition laid down in the early case of *Presbyterian Church V. the City of New York*, is that of *Stone V. Miss.*<sup>(1)</sup>, which case was carried from the Miss. State Court to the

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101 U. S. 810-19.

U. S. Supreme Court on appeal. Stone and his associates had been granted by the legislature of that state in 1867, a charter providing that they should enjoy the privileges of conducting a lottery in the name of the "Mississippi Agricultural, Educational and Manufacturing Aid Society". The new constitution of the state adopted in 1867, declared that "the legislature should never authorize any lottery; nor shall the sale of lottery tickets be allowed; nor any lottery heretofore authorized be permitted to be drawn or tickets therein be sold". In 1870, the legislature passed an act entitled: "An act enforcing the provisions of the constitution of Mississippi", prohibiting all kinds of lotteries within the said State and making it unlawful to conduct one in that State. In 1874, the Attorney General instituted and successfully prosecuted a proceeding by Quo warranto against the appellants,

to revoke and forfeit their charter, on the ground that they were conducting a lottery in violation of the above constitutional provision enacted in pursuance thereof.

The opinion affirming the state court was delivered by Waite C.J., who said: "All agree that the legislature cannot bargain away the police power of the state. Irrevocable grants of property and franchises may be made if they do not impair the supreme authority to make laws for the right government of the state; but no legislature can curtail the power of its successors to make such laws as they may deem proper in matters of Police". Citing *Met. Board of Excise v. Barrie*, 34 N.Y. 663, and *Boyd v. Alabama* 94 U.S. 665.

The examination of these leading cases together with the authorities cited therein, leads us to the conclusion that the police power of a state, like its kindred subject

It would seem therefore, to be a rule supported not by a current of authority, but as Justice Black would say, "but by a torrent of authority, that no state can sell out, weaken or abridge those essential powers of government, necessary to accomplish the objects of its creation. If taxation be regarded as an exception to this rule, it must be considered as a nominal rather than a real one; for no government dependent upon taxation for its support, would bargain away the whole power,- that would be substantially abdication. All that has been determined thus far is, that a state may surrender a part of this power for a consideration, which is, or is supposed to be, equivalent to the benefits that would have accrued to the state from an exercised of the relinquished power in the ordinary mode.

Ithaca, N. Y. June 1895.



