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THE STOCKHOLDER'S SUIT-CORPORATE AND INDIVIDUAL GRIEVANCES

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As the stockholder's suit is nowadays a standard remedy, it might be thought that the outlines of its underlying theory were of easy tracing. Yet even to-day we hear expressions from high places that are hard to reconcile. An eminent judge in the New Jersey chancery describes the object of the suit as "the specific performance of a continuing contract in writing, consisting of a certificate of capital stock." But that is hardly consistent with the well-recognized principle that, generally speaking, the benefits of the suit are taken by the corporation and only indirectly by the person who files the bill, although the corporation is not even a co-plaintiff, but is to be found among the defendants. Indeed, a standard text writer regrets this very circumstance, opining that the innocent shareholders are disheartened, and the guilty encouraged, because of the rule that "the results of even a successful suit belong to the corporation, and not to the stockholders who sue." But whether this is the inevitable result of the plaintiff's success depends upon what it is that we call a stockholder's suit; for it is quite possible to find instances where the plaintiff, by obtaining direct relief, demonstrated that the corporation was not of necessity the beneficiary of his action.

Plainly, therefore, we must be careful in our use of the term under discussion. Like other definitions, it describes; but to be of value it must define. It invokes by its mention an immense body of law, but we will not be on our way to a clear understanding unless we take our bearings. And, like other things of our common law, the subject cannot properly be discussed entirely from the standpoint of procedure. Back of that, and informing it, are substantive thoughts which it is our duty to apprehend. But, because ultimate ideas are simple in their nature, to get a proper view of them we must deal with elementary rules on the way.

The first of these rules has to do with the derivative nature of the stockholder's suit. For, as we have already noted, the plaintiff does not sue in his own right, but in that of the corporation. To it should go the fruits of the recovery, and it is erroneous for the decree to allow

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2 3 Cook, Corporations (7th ed. 1913) sec. 643.
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the stockholder anything personally. The cause of action is the asset of the corporation; and therefore no suit can be brought unless the plaintiff shows that he has asked the directors of the corporation to sue in the company's name, and they have refused, or that it would be futile to make such a request, because of their collusion with the wrongdoer.

The same reasoning makes the courts let a stockholder defend a suit against the corporation, if he can show that the directors, by reason of their affiliation with the plaintiff, are not to be trusted to defend the case properly.

Indeed, a judgment already obtained will be opened up. "Landis v. Sea Isle Hotel Co. (1896) 53 N. J. Eq. 654, 33 Atl. 964; Pollitz v. Wabash R. R. (1915, 1st Dept.) 167 App. Div. 659, 152 N. Y. Supp. 803, and cases there cited. "Such being the character of these allegations, the rule is so well settled as to require no citation of authorities that under any ordinary circumstances the fraud of the officers or managers of a corporation whereby its assets are misappropriated must be redressed by an action brought by the corporation to whom the assets belonged or by a stockholder derivatively in behalf of the corporation."

"Brock v. Poor (1915) 216 N. Y. 387, 396, 111 N. E. 229, 232. "A stockholder, as such, does not have a legal or equitable estate in the corporate property; his only right of property is to a proportionate share of the profits of the business while the company is in operation, and to a proportionate share of the net assets on its dissolution. Unauthorized dealing with the franchises or funds of the corporation directly injure it as a legal entity; it is the franchises of the corporation which are to be misused, the funds of the corporation which are to be misappropriated, and the corporation, therefore, is the party to be injured and should itself seek redress." Green, V. C., in Willoughby v. Chicago Jcn. Rys. Co. (1892) 50 N. J. Eq. 656, 664, 25 Atl. 277, 280. The mischief of a contrary suggestion, recently made (Harris v. Rogers [1919, 4th Dept.] 190 App. Div. 208, 179 N. Y. Supp. 799) was pointed out in later litigation affecting the same subject. "Harris v. Pearsall (1921, Sup. Ct.) 116 Misc. 356.

"Hawes v. Oakland (1881) 104 U. S. 490. It is not necessary to make demand of the stockholders, because such a plebiscite would not of necessity govern the action of the Board, for even the majority cannot control the Board during its term of office. See Matter of Kohler (1921) 231 N. Y. 353, 132 N. E. 114. The case might be different, of course, if the demand were coincident with the election of a new board. See Continental Securities Co. v. Belmont (1912) 206 N. Y. 7, 17, 99 N. E. 138; Del. & Hudson Co. v. Albany, etc. R. R. (1909) 213 U. S. 435, 29 Sup. Ct. 540. "The cause of action belonged to the corporation; but the plaintiff's institution of the suit is justified in law by the alleged futility of a demand that the plaintiff sue. The effect of the plaintiff's recovering a judgment upon his demand would be to restore the moneys and property misappropriated by McClanahan to the possession of the corporation. (Sage v. Culver, 147 N. Y. 241; Kavanaugh v. Commonwealth Trust Co., 181 ib. 121.) McCrea v. Robertson (1908) 192 N. Y. 150, 154, 84 N. E. 950, 951.

for defense if the shareholder acts promptly.\(^6\) In each instance, therefore, what the shareholder does is to protect the corporation.

That being the object of the suit, obviously it should not be complicated with any considerations personal to the shareholder. Thus, if he is to defend a suit against the company, he must first obtain leave to do so. As he is not a party to the record, he can do nothing without the court's leave. \(Qua\) shareholder, he cannot appeal from a decree which has been rendered against the company unless under special circumstances\(^7\) or remove into the Federal court a suit pending against the company.\(^8\) It is for that reason that the stockholder can bring no suit that joins a grievance personal to himself, even to himself as a stockholder, with one properly to be asserted by the company.\(^9\) And although the corporation, since it is to receive the proceeds of the recovery, is an indispensable party to the suit,\(^10\) yet the plaintiff cannot turn a personal action, brought for his own benefit against the directors, into a suit of this character simply by joining the company as a party defendant. He must do more than call the roll of the defendants; he must show that the gravamen of the suit is an injury to the company rather than to himself.\(^11\)

Naturally, the derivative nature of the suit requires that it be brought in equity. The right which the stockholder seeks as plaintiff to enforce is not his; hence no common law court could hear him. It follows that, even though the company could have recovered in an action at law, the stockholder who sues in its right must resort to equity in order to obtain for the unwilling company that to which it may be entitled.\(^12\)


\(^9\) *Brock v. Poor*, supra note 3; *Ringler v. Jetter* (1923, 1st Dept.) 206 App. Div. 478. If the point is not raised on demurrer, the plaintiff at least should be required to elect on the trial. See *Brewster v. Hatch* (1890) 122 N. Y. 340, 25 N. E. 505. After judgment, of course, the false joinder cannot constitute a grievance unless the point has been raised at or prior to the trial. *Kreitner v. Burgwanger* (1916, 4th Dept.) 174 App. Div. 48, 160 N. Y. Supp. 256.


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The equity court, naturally, can draw no line in this regard; and so it will vindicate, at the stockholder's behest, all corporate rights, legal and equitable, except where a statute limits enforcement to an action at law. In that event corporate rights must go without remedy; for, if the company will not sue to enforce them at law, the shareholder cannot, in its behalf or otherwise, assert them in equity.18

The other aspect of the stockholder's suit is its representative character. Whether, as usually happens, the plaintiff states that he files his bill for the benefit of the other shareholders, actually it is of interest to them; and consequently they may become co-plaintiffs for the asking. There are several results. The decree binds all, whether they actually have intervened or not.14 But prior to decree the suit is in the control of the plaintiffs for the time being, whether they be original plaintiffs or intervenors, and they can drop it at will.25 It does not follow, however, that a discontinuance would bar a fresh action by other shareholders. "The right of action is in no sense joint,"16 and this is illustrated by the fact, that, even if the original plaintiff were in no position to seek the aid of equity by reason of his laches or estoppel, the objection is removed if another joins in the bill.17 And so if one or more of the plaintiffs should part with his stock pendente lite,—that would dispose of the suit did he stand alone,18 but, if there are other plaintiffs who still have their stock, the bill cannot be dismissed.19 The same reasoning results in an intervening stockholder being allowed to revive a suit that has abated by reason of the death of the original plaintiff.20

But we must not let the representative character of the suit obscure

18 It is hardly necessary to add that situations of this sort are rare; but such a case actually arose recently. A shareholder endeavored to enforce the corporate right to sue for treble damages under the Sherman Anti-Trust Law, but was dismissed; the Supreme Court refusing to allow the statute to "be read as attempting to authorize liability to be enforced otherwise than through the verdict of a jury in a court of common law." Fleitman v. Welsbach Co. (1916) 240 U. S. 27, 29, 36 Sup. Ct. 233, 234.
16 Hirshfeld v. Fitzgerald (1898) 157 N. Y. 166, 51 N. E. 997.
17 Endicott v. Marvel (1913, Ch.) 81 N. J. Eq. 378, 388, 87 Atl. 230, 234; affirmed 1914, 83 N. J. Eq. 632, 92 Atl. 373.
18 "The objection of laches of the individual stockholder goes to his right to assert the property rights of the corporation; that right cannot be impaired by the laches of another stockholder who may have joined in the bill." Endicott v. Marvel, supra note 16, at p. 388 87 Atl. at p. 234.
the salient feature which was first above noted. Representative it is, because all the shareholders are interested in the company; but, first of all, the suit is derivative. Its sole object is to redress an injury which has been inflicted upon the corporation, as distinct from the stockholder, although it goes without saying that the suit also lies to prevent a threatened injury. But always, it will be observed, the injury, actual or prospective, is to the corporation. The shareholder plaintiff responds, indeed, to the call of his stock, but only as a part of the entity which is injured. The damage to his stock is a matter of reflex action. Primarily, the company feels the pain; it reaches the shareholders through the stock as nerves, but it is the company that receives the blow. Thus company A, owning stock in company B, may part with that asset, and this, in the view of an A shareholder, may justify a stockholder's suit to rescind the sale. In that suit the res is the B stock, not the A stock, and it is the A company, not the B company, that is interested in the outcome. When a corporation is authorized to increase its capital stock, each of the present shareholders has the prior option, over the public, of subscribing for a proportionate amount of the new issue; but the infringement of that right does not justify a stockholder's suit, for the grievance is individual, not corporate. On the other hand, a company may have a very lively interest in the title to its outstanding shares, and yet its contentions may be adverse to those of the claimant; as where it is sued either to compel it to recognize the plaintiff as the rightful owner of shares, and as such, entitled to a transfer of record, or for damages based on its refusal to make a transfer. The cases, in short, are of infinite variety where a suit by virtue of the ownership of stock cannot be described as a stockholder's suit, if we are to use that term accurately.

To stop with that assertion, however, does not give much in the way of results. Fortunately, it is possible to mark heavier lines of definition. At the outset, let us consider the nature of a business company, as it appears to the shareholder. It is quite true that a corporation is created by statutory law; but when we have said that, we have not told all that there is to tell about its essential nature. After legislation has

21 The injunctive method of relief in a stockholder's suit has become a common method of testing the constitutionality of tax laws. The shareholder alleges that the directors are about to pay taxes due under the law to which he objects; and, on his application to enjoin this, the court passes on the constitutionality of the law itself, allowing the Attorney General to be heard, by way of being amicus curiae, in behalf of the government. Pollock v. Farmers' Loan & Trust Co. (1895) 157 U. S. 429, 15 Sup. Ct. 673 (income tax law of 1894); Brushaber v. Union Pac. Ry. (1915) 240 U. S. 1, 36 Sup. Ct. 236 (income tax law of 1913).


created the thing, it plays no part in life until people put money into it. The statutes which forbid some classes of companies from doing business until a certain part of their capital stock has been paid in, are but precautionary expressions of this general idea. Except for purposes of fraud, no company can be set going until it gets capital. This the legislature does not furnish; on the contrary, the corporate heart is made to beat through contributions which people make in exchange for its stock and other securities. These contributions are the result of agreement; the issue of stock is no matter of fiat from the State. Agreements between people, or between people and the company, therefore, underlie the organization. And always these agreements have the same object, that the company shall perform the functions for which it was organized, that it shall do business, that it shall make money. Whenever it fails in this regard, then the main desire of the contributors is to get their money back again, or as much of it as may be left. Thus to the shareholder the company assumes aspects varying with its fortunes. At the start he asks whether the company was organized in accordance with agreement, or were there departures from the plan of financing which had been promulgated. Afterwards the matters in which he has interest relate to the company as a going concern. So long as it is doing business at a profit his money is in it to stay, and so the gains and losses of the company are his own gains and losses. But when the venture ceases to function on the lines intended, then the shareholder’s intention is, not only that further losses be stopped, but that the business be wound up, and the remnant of his capital contribution be restored to him.

This outline of what goes on in a shareholder’s mind is not scientific; it expresses no polished thought in law. But it will help us to follow the boundaries of the stockholder’s suit. For the courts have responded to these ideas in shaping their remedies. And so we will be aided if we keep in mind that the stockholder’s rights regarding corporate affairs vary with three situations; these having to do, respectively, with pre-organization agreements, with the company as a going concern, and with the corporate venture when viewed as a failure.

With the company as a going concern, the theory of the stockholder’s suit finds its ideal application. This is illustrated by the rule that, if the act complained of constitutes a wrong to the corporation, then it cannot also constitute a wrong to any individual stockholder. When one puts his money into corporate stock, he invests in the activities of the corporation as well as its property. His investment is inseparable from the general mass, and when any corporate loss has been made good, the stock regains its former relative value. Essentially his investment is in a going concern. That is why, unless a statute allows otherwise, it

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requires the unanimous consent of the shareholders for a company to sell out its business, distribute the proceeds of the sale, and stop; and that, too, even if the proceeds consist of the stock of another company similarly caparisoned as to assets and liabilities.\textsuperscript{27} 

To this rule, it is believed, there are no exceptions. The fact that the majority of the stock can lawfully vote to sell the company's assets when the business is losing money\textsuperscript{28} is only an exception that proves the rule. The directors by that method have saved the courts the trouble of liquidating the company's affairs. Certainly it is no exception that "stockholders of a holding company may maintain a representative action for the benefit and in the behalf of the subsidiary company, the directors of both companies having refused, after due request, to institute an action in the name of either company."\textsuperscript{29} That does not seriously stretch the outlines of the stockholder's suit, as we have viewed them. In fact the only basis on which the shareholder can go directly against the wrongdoer is that the latter owed the shareholder a special

\textsuperscript{27} Am. Seating Co. v. Bullard, supra note 12, and cases there cited; Jones v. Mo. Edison Electric Co., supra note 12; Barnett v. Phila. Market Co. (1907) 218 Pa. 649, 6 Atl. 912; Riker & Son Co. v. United Drug Co. (1912) 79 N. J. Eq. 380, 82 Atl. 873; Lauman v. Lebanon Valley R. R. (1868) 30 Pa. St. 42. This is illustrated by Geddes v. Anaconda Copper Co. (1919) 254 U. S. 590, 41 Sup. Ct. 209. There the directors had sold the corporate property for what was alleged to be an inadequate price. The lower court had ordered a rescission on condition that first the property be exposed for sale at public auction, and that the original sale stand as made unless a bid were received higher than the price at which the directors had sold the property. But the Supreme Court reversed this decree on the basis that the stockholders should not be put to any such test, if the condition of the company did not warrant a sale at all.


duty. No director or officer owes this duty, simply by virtue of his office; no, not even if he has personally promised the shareholder faithfully to protect the interests of the company. The plaintiff must show more than that; he must show a legal obligation owing him by the defaulter, and having origin in circumstances which exclude the mere fact that the plaintiff is a shareholder. Such instances can be found in the books. We have that sort of case where the defendant was the plaintiff’s personal agent as well as the company’s, and therefore bound by the agency properly to manage everything in which the plaintiff might have interest. Hence a holding company has a theoretical cause of action against its own director when he, installed as manager of a subsidiary, allows it to be ruined. And the same result will be reached if the plaintiff, having hypothecated his stock with persons who happen to be directors of the company, finds them conspiring to exhaust its resources so as to depreciate the value of the stock, in the hope that, the plaintiff being unable to obtain funds elsewhere for its redemption, they will be able to buy it in on a foreclosure sale. In each of those cases the plaintiff, in law, had his own grievance; and the corporate grievance, however important a consideration in the assessment of damages, was, so far as the cause of action might be concerned, a matter of accident. But if there is no special tie of that sort between a particular shareholder and the wrongdoer, the grievance is exclusively corporate, so long as the corporation is a going concern.

Taking the stockholder’s suit from this angle, the philosophy underlying it is apparent. The suit is derivative for a sound reason; and its representative character is due to logic equally good. The suit is derivative because the company is a separate entity, not only for juristic reasons but because, as a going concern, the stockholders have recognized it as the person to whom their money has been entrusted for handling. If its rights are invaded, it is the one to seek redress. Nay more, if the company throws away its rights through control exercised over its officers or governing board by people who work in adverse interest, it may sue to recover whatever it may thus have lost. In other words, it may go back on its own bargain. To know why this is so, however, we cannot leave the case as it is put by Noyes, J., that the company cannot “conspire that its own directors

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*Van Boskerck v. Aronson*, supra note 26. See also other cases there cited.


shall be unfaithful to it," because, in and of themselves, these words merely describe a result of reasoning. But we are given the underlying thought if we recall that this language reflects the well-known rule that a trustee, who has parted with trust funds in violation of the trust, nevertheless may sue to recover them, and, when he succeeds, holds the recaptured assets on the same trusts as before. The reason is that the wrongdoer is not to be conceded the power to destroy the trust. With the restoration of the thing taken, the trust must be resumed, and therefore the trustee is the man to hold the title, at least until such time as the court can remove him and appoint a successor. By the same token, a corporation should not go out of business simply because it has been robbed; the logical thing to do is to restore to it that which it has lost, and let it resume its course. It is only when the trustee refuses to sue, or the corporation is so under enemy control that its proper consent to sue cannot be obtained,—for naturally a stockholder cannot use its name, even in a suit in its own behalf, without proper authority,—that the court allows the beneficiary in the one case, or the stockholder in the other, to sue in the right of the trustee or of the corporation.

This reasoning involves the conclusion that, despite a contrary suggestion which occasionally comes from eminent sources there is no difference, in the right of relief, between a shareholder's suit and a suit by the corporation. The suggestion is that the corporation cannot sue because it cannot uproot a transaction to which it has consented, whereas a minority stockholder, who has not shared in the combined action of the majority which led to the corporate consent being given, is not estopped and can obtain that relief for the corporation to which it would not be entitled should it sue for itself. The error of this thought lies in what it overlooks. On the surface, it disregards the derivative nature of the stockholder's suit, with the necessary conclusion that the shareholder cannot sue if the corporation itself had no cause of action. What it overlooks at the bottom is that a company organized for business holds, in ultimate analysis, its assets and goodwill as in dedication to the real purpose of its being, which is to do business at a profit, and, to that end, it can lawfully do nothing that honest judgment would

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90 See Stone, Nature of the Rights of a Cestui que Trust (1917) 17 Col. L. Rev. 467.
refuse to sanction. In that regard, as we have seen, there is no difference between a trustee and a corporation. If the trustee has wrongfully parted with trust funds, he may sue to recover them; and so with the corporation. Of course, if all of the trustee’s beneficiaries agree with what he has done, he cannot recover, because the effect of a favorable decree would be to reconstitute the trust in behalf of people who had agreed otherwise—and consequently, unless a statute forbids, a trust may be destroyed by the beneficiaries all agreeing that the trustee may transfer the assets.\textsuperscript{40} In like manner the agreement of all its shareholders will justify a corporation in making any disposition of its assets that does not defraud its creditors or evade any duty it may owe the public.\textsuperscript{41} But, so long as there is one beneficiary who has not agreed, the trustee’s suit will result in the diverted assets being restored to the trust. So with the corporation. There are, of course, things of which the majority may lawfully approve, and the corporate acts thus involved bind the company in all respects. But to cite such a case is to beg the question, for corporate conduct of that sort is within the terms of the trust, and so the minority have no right to say that the company has been injured. But when we find a corporate act which is outside the scope and purpose of the company’s course of affairs as rightfully to be conducted, then, unless all the shareholders have agreed that this is what they wanted the company to do, the corporate trust has received injury, and the corporation is the party to right the wrong. It is because the company could have sued that a derivative suit lies at the instance of a shareholder. Naturally, if he personally has given his approval of what has been done, the court will not hear him. But it does not follow that the company has no grievance; the court’s only thought is that, even in a representative suit, the representative must at least be as clean as he would like his principal to be.

That is why in this class of cases there is ordinarily no need for the appointment of a receiver. The most that is ever done is to appoint a receiver until final decree, and then only if a case of waste \textit{pendente lite} is shown. Nor is such a receiver required by the final decree to do more than turn over the assets to the corporation, for in its nature the suit would not, in the usual circumstances, require more than that sort of relief. It is only when the robbery has so injured the company as to involve a stoppage of its business that this sort of case can be turned into one of liquidation, requiring a distribution of the recovered funds by the court, through the medium of a receiver, among the parties ultimately in interest.\textsuperscript{42} But then the receivership would be of quite a different nature; for a stopped company usually passes into the hands

\textsuperscript{40} Parker v. Converse (1855, Mass.) 5 Gray, 336; Newman v. Newman (1885) L. R. 26 Ch. Div. 674. For the rule in such a state as New York, where legislation has intervened, see Matter of Wentworth (1920) 230 N. Y. 176, 129 N. E. 646.
\textsuperscript{41} Jacobs v. Mergenthaler, supra note 28.
of a liquidating receiver at the outset, and it is he who, in the corporate right, brings the suit to recover stolen assets.

It is now in order to discuss an equity principle which was touched earlier in this essay, but laid aside for the time being. For that principle, it is believed, will aid our understanding in several ways. As showing the distinctions applicable to the stockholder's suit, between the case of the going concern and the case of the pre-organization agreement, and between both and the case of the insolvent company, this rule of equity has great value.

To appreciate the rule we must recur to a feature of the stockholder's suit that was cited at the outset. The suit as was then noted, is always representative.

It does not usually happen that the shareholder who sues is the only party in similar interest. Of course, with two-men companies the necessity for this form of action is technical at best,—in reality the quarrel is between two equal interests, and therefore slips in forms of pleading or practice are not seriously regarded. But in the usual case where we have a number of shareholders, the plaintiff, while suing in the right of the corporation, represents the other shareholders just as much as himself. Hence these people, while not properly to be made defendants, inasmuch as their interest lies on the opposite side, should have the right to intervene; and, because of that, they should be bound by any non-collusive judgment which has disposed of the case on the merits.

In that respect the case is the same as any other where a number of people are interested in a common fund. Interference with that fund injures all, and a representative suit lies in behalf of all. "Here," said an English judge in an early case, "is a fund in which all the shareholders are interested; 15,000 l. has been improperly taken out of it: a fraud has been committed on them all. Is it necessary that all should come into a court of justice, for the purpose of joining in a suit with a view to obtain redress? .... In the present case, it appears to me that justice may be done in one suit. All the shareholders stand in the same situation; the property has been taken out of their common fund; they are entitled to have that property bought back again for the benefit of the concern. When all parties stand in the same situation, and have one common right and one common interest, in what respect

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44 "It would have been proper enough for the plaintiff, suing in his own name and in behalf of the other stockholders, to bring an action against McClanahan and to join with him the directors, whose negligent administration made McClanahan's alleged misconduct possible. In such a case it would have been open to any, or all, of the other stockholders to intervene in the action, as they might feel disposed, or be advised. But that they should be brought in as parties defendant is, certainly, without excuse on the face of the complaint." McCrea v. Robertson, supra note 4, at p. 154, 84 N. E. at p. 462.
can it be inconvenient that two, or three or more, should sue in their own names for the benefit of all?45 The case, in short, is precisely similar to that of a mortgage securing bonds, where the bondholders are numerous, and the trustee under the mortgage refuses to act;46 of legatees or beneficiaries where the executor or trustee will not sue;47 also, it parallels the creditors’ bill for distribution of the estate of a decedent or of an insolvent corporation.48 There is a limited fund, in the shape of the corporation’s assets and good-will, including its rights against those who have wronged it or are about to do so; and the parties interested in it are numerous. This, according to the rule everywhere, gives the right to a representative action.

But unless the subject of the suit be a limited fund, no representative action will lie. That, at least in this country, is well settled.49 And so the shareholder’s suit must relate solely to this fund and its protection; otherwise it will be dismissed. This is shown by the case of a corporate lease with the lessee covenanting to pay rent directly to the lessor’s shareholders. That agreement is made for their direct benefit; and, at least in States allowing suit on a contract by a beneficiary to it, a separate suit would lie in behalf of each shareholder. But, as the agreement is not a corporate asset, the suit should not be derivative, because it does not sound in behalf of the corporation.50 To that doctrine the writer subscribes in spite of the rule of expediency which the Federal courts recently have adopted, that in such cases the lessor company is taxable upon the total of the rentals as corporate income.51

With these thoughts in mind, we can turn from the corporation as a
going concern to the cases that deal with pre-organization agreements. And when we test these cases by the ideas underlying the derivative and the representative features of the stockholder's suit, we are able to understand why, concerning these cases, this form of relief has a very restricted field.

If the plaintiff is one of those who agree that the company shall be organized, his agreement presupposes, as a general thing, that the company will be financed in the method for which the agreement provides; and it is not until then that his agreement becomes enforceable,—enforceable generally speaking, at the suit of the company. If the company, being entitled to enforce this contract, refuses to do so as against any particular person, then, indeed, we have a case for the stockholder's bill. But if the plaintiff wishes to avoid his bargain because of such things as the fraud of the promoters of the undertaking, the action that he takes, whatever it may be, is individual and not representative, and his grievance is personal, not derivative. And it goes the same way, naturally, if, instead of asserting or seeking rescission, he sues for damages in an action of deceit. These cases, in short, deal with such questions as, how the plaintiff got the stock, and whether he must abide by his bargain; whereas his rights on the stock itself are necessarily to be postponed to a determination of such matters in limine. There can be no stockholder's suit, as such, in connection with these points.


More or less, the same observations apply to matters connected with corporate death. The emphasis of that term is not limited by strictly legal conceptions. A corporation dies, from one point of view, only when its charter expires by limitation or forfeiture, or it is dissolved by statutory proceedings; for neither bankruptcy nor an equity receivership can destroy corporate life. But the working of corporate affairs in the sight of the courts has resulted in a practical as well as a theoretical conception of corporate death. A company for all practical purposes can be killed through the act of its directors, wrongful though that act may be, and incapable of effecting a corporate dissolution. And the consequence of interest to us is that corporate death, however caused, has its effects on the stockholder's suit in its range of application.

Let us first consider the death which is caused by the wrongful act of the directors. They, we will say, decide to sell the assets, including goodwill. We may have a case where it is quite proper for the directors to sell all the assets, provided they reserve the goodwill, because the business of the company is of such a nature that its profits are made in just that way. In cases of that sort the company continues in business with the proceeds of its sale, and gets ready, indeed, for another turnover of the like kind. Nobody can complain of that. But it is different when goodwill is sold as well as assets, for that means that the corporation is to quit business, and converts the shareholder's interest into something quite different from that which he had in a going concern. To appraise his right of action requires a survey of the situation as it actually existed.

If the stockholder can so untangle the coil as to restore his company to its former position by a suit in the way of rescission, then obviously he must sue in the name of his company; it must be a true stockholder's suit. But the court may find that rescission is impossible. In that event the shareholder's right is just as personal as it was concerning the agreements which led to the formation of the company. Undoubtedly he is entitled at law to damages; and the most that equity can give him is a lien on the old assets, if still in the hands of the buyer, for the value of his stock. But while on final hearing the court is in a position to know what it can do for the stockholder, the latter is not endowed with any such knowledge at the outset. His position at that time is difficult, for he knows but little of the facts, especially of the buyer's acts subsequent to the purchase; and he cannot then ascertain whether rescission would be possible. These reasons have led to the courts allowing an amorphous action, which is always representative. It also professes to be derivative; but at the trial the plaintiffs are allowed to resolve their suit into either a true stockholder's bill for rescission or a personal suit, according to the relief which the court finds itself able to give. The

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relief, in short, varies according to whether the old company can be set on its legs again. If so, the transaction is rescinded, the company’s assets are returned to it, and the plaintiffs take nothing personally by their suit. But if rescission cannot be had, the plaintiffs are given the next best thing; they are allowed the value of their shares, and their recovery is enforced by the decree impressing the assets of the old company, so far as they can be located as still in the wrongdoer’s hands, with a lien to that extent.56 This suit, therefore, is justifiably derivative, and properly representative. If the court can restore to the old company its property, that will be done. If not, then its shareholders go against a common fund in the shape of the corporate assets. It is only when both methods of relief fail that a simple money decree is given them. But the essential nature of the grievance being both derivative and representative, the court is justified in retaining the cause for such decree as it finds itself able to give. It cannot lose jurisdiction because the wrongdoer has made impossible the full measure of relief to which the nature of the case entitled the plaintiff on the filing of his bill.

The cases just discussed involved something additional to a mere sale of the corporate assets. What the wrongdoing directors proposed was a distribution among the shareholders of the net proceeds of the sale, after payment of corporate debts. They purposed, in short, a liquidation of the company’s affairs. The minority shareholders protested against a liquidation of the kind offered, and the courts upheld them. But there are cases, of course, where liquidation occurs without valid objection. It remains for us to speak of these different sorts of winding up in so far as they bear upon the topic under review.

It would not be possible, with any decent regard for the amenities relating to time and space, to do more than enumerate the different forms of corporate liquidation. A company may make a general assignment for the benefit of its creditors. It may be adjudged a bankrupt. It may be dissolved under statutory proceedings instituted in the courts of the state by virtue of whose laws it was created. Under other provisions of those same laws it may dissolve itself without judicial aid. Its affairs may be wound up by a court of equity on the bill

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56 Jones v. Mo. Edison Co., supra note 12; Am. Seating Co. v. Bullard, supra note 12; and cases there cited; O’Brien v. O’Brien, supra note 28; Southern Pac. Ry. v. Bogert (1918) 250 U. S. 483, 39 Sup. Ct. 533. “Now, as the court may under this prayer rehabilitate the Edison Corporation, it may do less. It may grant a decree nisi, a decree that all its property, powers and franchises be restored to the Edison Company unless within a time certain the defendants pay to the complainant and those who join him the value of their share of the property transferred to the Consolidated Company. Such a decree would be consistent with the repudiation of the contract of consolidation and with the first prayer in the bill.” Jones v. Mo. Edison Co., supra note 12, at p. 779. If, as part of the scheme, a legal dissolution of the company has been effected, the action, while representative, cannot be considered as strictly derivative. See O’Brien v. O’Brien (1921) 223 Mass. 403, 131 N. E. 177.
of a shareholder, or—to take the more common case—on the bill of a creditor for general administration. There are cases where, as we have seen, its directors lawfully may sell the assets and distribute the proceeds. Again, corporations engaged in certain lines of business, as banks and insurance companies, are, under the laws of many states, so subject to state control that an administrative officer may by fiat shut the doors and wind up the corporate affairs. National banks, also, are under this sort of subjection to the Comptroller of the Currency. For present purposes we can stop with the catalogue thus presented if we draw from it one or two simple thoughts.

All forms of winding up result in the creation of a liquidator, in whom are vested the functions necessary to gather in the assets for the purpose of distribution. There is, however, as to liquidators a distinction in terms of office. The officer in the one case may be a receiver, in another we find the liquidator in the person of the trustee in bankruptcy, and in other cases the statute may delegate the duty in the first instance to the board of directors. But these diversities do not prevent classification, and the intentions of this essay will be fully served if we separate liquidators into but two classes. The one comprises those officers who, judicially appointed at the outset, act in all things under judicial direction. That sort of officer, in effect, is really a sub-agent; the court itself, in ultimate analysis, being the real liquidator. Of such are receivers when judicially appointed, and trustees in bankruptcy. The other class includes those liquidators who are not immediately subject to judicial control. In that category, therefore, we find directors, liquidators appointed by such an administrative officer as a Superintendent of Banks, and assignees under a general assignment.

The usefulness of this method of indexing becomes apparent when the liquidator finds that, prior to the passage of the company's affairs into his hands, something had occurred that inflicted injury on the company, something for which a stockholder's bill would have lain had the company refused to act. But, as the company has died for all practical purposes, it follows that the liquidator is the one to bring the necessary suit. And if he refuses to act, then, in accordance with the principles we have considered, the shareholder should find himself vested with a derivative cause of action,—not in behalf of the company, indeed, but of the liquidator. But it is just there that the distinction applies regarding the different kinds of liquidators.

If the liquidator is appointed by the company, or even by a statutory authority acting in such cases, as the State Superintendent of Banks, then the suit may be brought without further ado. The liquidator is a necessary party defendant; and so, too, is the company, if it is still

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alive, and the liquidation is being conducted in its name. But if the
liquidator is a judicial officer, such as a receiver, or a trustee in bank-
ruptcy, then sound reason requires that suit should lie only by him,
recourse to the court being proper to compel him to sue if he wilfully
refuses. For when a liquidating court takes control, the corporate
assets are then in court, the officer being merely its arm, and it is a
perversion of reason to allow any suit to be brought that will not draw
the proceeds directly into the court. With a judicial liquidation, then,
the stockholder's action ceases to have place; for there is no need of it,
an universal representative being on the scene in the shape of the court
and its officer.

In the course of this article many things have been said that tempt to
further discussion. Other pleasant topics, indeed, have been passed
without mention, such as the difference between the rules prevailing in
the Federal courts and those of certain States, as to allowing a stock-
holder's suit to be brought by one who bought his stock after the
company had suffered the injury in question. And in the setting
down of these thoughts many more would suggest themselves. But
enough has been said to develop what the writer believes to be the
principal features of the form of action under discussion. And, his
duty in that regard having been done as he conceived it, it is impera-
tive that he stop. For, such are the fascinations of our law to any
one who undertakes to write concerning it, that the hardest part of the
work is, having chosen a path, to walk it straightly.

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161 Ill. 422, 44 N. E. 891.
59 For a discussion of these different rules see Pollitt v. Gould (1911) 202 N. Y. 11, 94 N. E. 1088. This, it will be noted, has nothing to do with the question
whether the plaintiff should be precluded by reason of his assignor having ratified
the transaction before he parted with his stock. See Babcock v. Farwell (1910)
245 Ill. 14, 91 N. E. 683.