

Corporations--Power of President to Institute Suit in the Corporate Name (West View Hills, Inc. v. Lizau Realty Corp., 6 N.Y.2d 344 (1959))

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*Gendell v. Orr*³⁸ held the existence of the building on a public highway for three years to be sufficient dedication to forfeit the common-law copyright.³⁹ *Kurfiss v. Cowherd*⁴⁰ held the public exhibition of the building without restriction upon the right to measure and copy was a publication.⁴¹

However, in deciding this issue, the *Smith* case has disregarded the dedication and abandonment theories of the *Gendell* and *Kurfiss* cases. In their stead it has extended the *Apollo* rule. The house, the Court reasoned, was not a *copy* of the architectural plans and therefore could not be a publication of them.⁴²

The *Apollo* rule is not new to the area of copyright.⁴³ However, in the United States the courts have confined it to the area of musical compositions and recordings. The *Smith* case is the first instance of its application in the area of architectural plans. This has left the door open for its further extension in the performance fields. The requirement of a copy and its strict definition furnishes the courts with a more solid criteria of publication than the traditional abandonment and dedication concept. Armed with this, the forewarning of the *Gendell* case concerning the possible uselessness of statutory copyright⁴⁴ may become reality in the performance areas.



CORPORATIONS — POWER OF PRESIDENT TO INSTITUTE SUIT IN THE CORPORATE NAME.—Defendant, a three-man corporation, con-

³⁸ *Ibid.*

³⁹ The court may have anticipated the *Apollo* holding and its effect on statutory copyright when it pointed out: "Three years upon the highway must certainly be regarded as an abandonment of any right, else the copyright law . . . would become useless." *Gendell v. Orr*, *supra* note 37. (Emphasis added.)

⁴⁰ *Supra* note 36.

⁴¹ The building was a model home on exhibition. The court treated it much the same as a painting exhibited in a gallery. *Kurfiss v. Cowherd*, *supra* note 37, at 287. See note 17, *supra*.

⁴² *Smith v. Paul*, 174 Cal. App.2d 804, 345 P.2d 546, 553 (Dist. Ct. App. 1959). The court also indicated that the exhibition of a film, the performance of a script, and the broadcast of a radio script are not copies. *Id.* at 553 (dictum).

⁴³ "The performance in public of a dramatic or musical work, and the delivery in public of a lecture, are not publication of the work or lecture . . . for obviously a performance is not an 'issue of copies'"

"Neither is the exhibition in public of an artistic work or the construction of an architectural work of art, publication of it." COPINGER, LAW OF COPYRIGHT 36 (6th ed. 1927). The concept that publication requires an issuance of copies is found in the United Kingdom's Copyright Act, 1911, 1 & 2 GEO. 5, c. 46, §1(3). This concept is also found in Article VI of the Universal Copyright Convention which defines publication as the reproduction in tangible form and the general distribution to the public of *copies* of a work. Universal Copyright Convention, 17 U.S.C. §9 (1958).

⁴⁴ See note 39, *supra*.

structed an apartment house. As sole directors and stockholders, the three men agreed to make plaintiff corporation, a similar organization in which the same three men were sole stockholder-directors, pay the \$200,000 bill for work, labor, and services. By this move, the house became the defendant corporation's asset while the stock in plaintiff corporation was rendered worthless.

Zaubler, one of the three men, was president, and, along with the other two, one-third stockholder and a director in both corporations. He later sold his interest in several organizations, including the defendant corporation, to the two remaining stockholders, but they did not buy his one-third interest in plaintiff corporation since it now had considerably lower value.

The two remaining men then decided to sell the apartment house and divide all the assets of defendant corporation between them. Zaubler, as president of plaintiff corporation, brought this action against them as individual defendants, alleging that as directors of plaintiff corporation they had mismanaged that corporation in forcing it to pay for the labor for the house, and against the defendant corporation to prevent the liquidation of its assets wrongfully received, alleging that plaintiff corporation, in which he retained a third interest, was rightfully entitled to the money. Zaubler predicated his authority to bring the action on the implied powers of his presidential office, and retained a New York attorney to prosecute the action in the plaintiff corporation's name.

The Court of Appeals, affirming a judgment of the Appellate Division, *held* that despite the lack of specific enumeration in the charter or by-laws of the plaintiff corporation, the president under the circumstances had the power to institute action in the corporate name. *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 160 N.E.2d 622, 189 N.Y.S.2d 863 (1959).

Zaubler, as both president and minority stockholder, had two possible avenues of approach open at the commencement of this action. He could have brought either a presidential suit in the name of the corporation, or a stockholder's derivative action.¹ There are several reasons why a stockholder's derivative action would be undesirable to him.

In a derivative suit, the plaintiff must pay all legal fees and expenses personally.² He must also exhaust his remedies within the

¹The obvious elements of acquiescence, ratification, and laches present would put an individual minority *representative* action out of the picture.

²*Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 298 N.Y. 483, 493, 84 N.E.2d 790, 794 (1949); *La Vin v. La Vin*, 281 App. Div. 888, 119 N.Y.S.2d 573, *appeal denied*, 281 App. Div. 984, 121 N.Y.S.2d 89 (2d Dep't 1953). A *successful* plaintiff in a derivative suit may, however, be awarded counsel fees at the court's discretion and on a strict *quantum meruit* basis. See BALLANTINE, *CORPORATIONS* § 156 (rev. ed. 1946). See also Hornstein, *Counsel Fees in Stockholders Derivative Suits*, 39 COLUM. L. REV. 784, 786 (1939). N.Y. GEN. CORP. LAW §§ 61-a, 64-67.

corporation. This entails a formal demand on the directors³ and a wrongful refusal not based on reasonable discretion.⁴ A good-faith decision not to sue by the directors acting in the business interest would normally bar the action.⁵ The plaintiff's burden of proof must not merely show an error of judgment on their part, but actual negligent, illegal, or fraudulent mismanagement⁶—a difficult undertaking.

In New York, there are also additional qualifications for the plaintiff in a derivative suit. He must own the shares either when the transaction complained of arose or they must have devolved upon him by operation of law;⁷ they must also be owned at the time of the suit and during its continuance.⁸ He must also meet the statutory requirements of stock ownership or value or else he may be required to post bond for the corporation's legal expenses.⁹

The derivative stockholder labors under a presumption that the directors acted in the business interest¹⁰—there is no presumption of legitimacy or authority to bring suit in his favor. Moreover, the court can re-appoint counsel to represent all the stockholders if it deems this expedient.¹¹

Other disadvantages to the plaintiff may be the intervention of other stockholders against him,¹² the imposition of a kind of fiduciary obligation on him as plaintiff,¹³ the passive role played by the cor-

³ *Isaac v. Marcus*, 258 N.Y. 257, 265, 179 N.E. 487, 490 (1932). Where the demand would be futile, it need not be made. *Price v. Standard Oil Co.*, 55 N.Y.S.2d 890 (Sup. Ct. 1945), *aff'd*, 273 App. Div. 890, 77 N.Y.S.2d 686 (1st Dep't 1948).

⁴ *Mendelson Bros. Factors v. Sachs*, 253 App. Div. 270, 1 N.Y.S.2d 838 (1st Dep't), *aff'd*, 279 N.Y. 604, 17 N.E.2d 459 (1938); *Smith v. Western Union Tel. Co.*, 276 App. Div. 210, 93 N.Y.S.2d 653 (1st Dep't 1949), *aff'd*, 302 N.Y. 683, 98 N.E.2d 482 (1951); *Myer v. Myer*, 271 App. Div. 465, 66 N.Y.S.2d 83 (1st Dep't 1946), *motion for leave to appeal dismissed*, 271 App. Div. 823, 66 N.Y.S.2d 618, *aff'd mem.*, 296 N.Y. 979, 73 N.E.2d 562 (1947). Some authorities hold, in addition, that the exhaustion of corporate remedies must include an application to other stockholders as a body, and an attempt to convene a meeting to ratify the suit or vote new directors. See BALLANTINE, CORPORATIONS § 146 (rev. ed. 1946) and cases cited therein.

⁵ *Koral v. Savory, Inc.*, 276 N.Y. 215, 11 N.E.2d 883 (1937); *Hornstein v. Paramount Pictures, Inc.*, 37 N.Y.S.2d 404 (Sup. Ct. 1942), *aff'd*, 292 N.Y. 468, 55 N.E.2d 740 (1944).

⁶ *J.C.F. Holding Corp. v. General Gas & Elec. Corp.*, 181 Misc. 283, 46 N.Y.S.2d 605 (Sup. Ct. 1943), *aff'd mem.*, 267 App. Div. 863, 47 N.Y.S.2d 303 (1st Dep't 1944).

⁷ N.Y. GEN. CORP. LAW § 61.

⁸ *Hanna v. Lyon*, 179 N.Y. 107, 71 N.E. 778 (1904). See also BALLANTINE, CORPORATIONS § 148 (rev. ed. 1946). For the rule in the federal courts, see *Gallup v. Caldwell*, 120 F.2d 90 (3d Cir. 1941), and *FED. R. CIV. P.* 23(b).

⁹ N.Y. GEN. CORP. LAW § 61-b.

¹⁰ See cases cited notes 4 and 6 *supra* and BALLANTINE, *op. cit. supra* note 8, § 147.

¹¹ *Fleitman v. Simpson*, 9 Misc.2d 398, 166 N.Y.S.2d 727 (Sup. Ct., 1957).

¹² See *Fleitman v. Simpson*, *supra* note 11; *Mathews v. American Tobacco Co.*, 130 N.J. Eq. 470, 23 A.2d 301 (1941). *Cf.* N.Y. CIV. PRAC. ACT § 193-b(2).

¹³ *Koster v. American Lumbermens Mut. Cas. Co.*, 330 U.S. 518 (1947). See also BALLANTINE, CORPORATIONS § 145 (rev. ed. 1946).

poration against him,¹⁴ and the possible lack of a jury trial.¹⁵ The minority stockholder is also subject to a judicial suspicion of his suit as a possible strike suit brought for harassment or nuisance value, to further his own economic interests, or to gain control.¹⁶

The substantive area would also present formidable obstacles to a derivative action in this case. Although the instant case was not decided on the merits, it is highly probable that, had it been brought as a minority derivative suit, it would have failed on the grounds of estoppel,¹⁷ laches,¹⁸ ratification,¹⁹ acquiescence,²⁰ and possibly the statute of limitations.²¹

Finally, an unfavorable aura would surround Zaubler as a minority stockholder; his interests would be more obvious than in a presidential suit brought ostensibly in the business interest.

Zaubler's other avenue was to institute, as president, a suit in the name of plaintiff corporation. The source of power to bring suit in the corporate name is ordinarily associated with and exercised by the board of directors in managing the corporation.²² The power to bring suit may, however, be delegated to the president. This may be accomplished *expressly* in the corporate charter or by-laws, or by

¹⁴ *Hall v. Craigo Sweets*, 177 Misc. 120, 29 N.Y.S.2d 381 (Sup. Ct.), *aff'd mem.*, 262 App. Div. 866, 29 N.Y.S.2d 512 (2d Dep't 1941).

¹⁵ *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 298 N.Y. 483, 84 N.E.2d 790 (1949). The stockholder's derivative action is one in equity. *Koral v. Savory, Inc.*, 276 N.Y. 215, 11 N.E.2d 883 (1937); *Fanchon & Marco v. Paramount Pictures, Inc.*, 202 F.2d 731 (2d Cir. 1953).

¹⁶ See, e.g., *Cohen v. Beneficial Loan Corp.*, 337 U.S. 541, 548 (1949).

¹⁷ The dissent in the Court of Appeals assumed that Zaubler would be estopped in a derivative action. *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 351, 160 N.E.2d 622, 626, 189 N.Y.S.2d 863, 868 (1959) (dissenting opinion).

¹⁸ Cf. *Goldboss v. Reimann*, 55 F. Supp. 811, *aff'd mem.*, 143 F.2d 594 (2d Cir. 1944). This case held that a shareholder's prejudicial delay in bringing suit barred a derivative action. "Laches is perhaps the most common and effective defense against a derivative suit by a minority shareholder." BALLANTINE, CORPORATIONS § 151 (rev. ed. 1946).

¹⁹ See *Atkinson v. McCabe Hanger Mfg. Co.*, 55 N.Y.S.2d 274 (Sup. Ct. 1945).

²⁰ *Quintal v. Kellner*, 264 N.Y. 32, 189 N.E. 770 (1934). Here, stockholder acquiescence was held to bar a derivative action.

²¹ N.Y. CIV. PRACT. ACT §§ 48, 48-8. The instant case presents an interesting and intricate problem in applying the statute of limitations. The precise nature of the action against the defendant corporation was not stated; but the action against the directors would have failed in mismanagement, negligence, waste, injury, or any other usual form of this type of suit. *Ibid.* The shorter statute is applied to the derivative stockholder rather than the longer equity statute. Cf. *Potter v. Walker*, 276 N.Y. 15, 11 N.E.2d 335 (1937). See also PRASHKER, NEW YORK PRACTICE §§ 27, 28c (4th ed., 1959). Section 48 of the Civil Practice Act (an action based on the fraud of the directors and defendant corporation) is apparently inapplicable because of Zaubler's original acquiescence and the prolonged inactivity of the corporation.

²² See N.Y. GEN. CORP. LAW § 27.

agreement;²³ *implicitly*, through a past course of conduct by the president with the acquiescence of the board;²⁴ or through the apparent authority vested in the president in the eyes of an outsider.²⁵

Where the power has not been delegated to the president by the board, there is a conflict of authority in New York as to whether or not the president has an inherent power *ex officio* to bring suit in the corporate name.²⁶ While other jurisdictions say that he has the power to institute and defend *normal* litigation,²⁷ the case law in New York up to this point was apparently settled by *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*,²⁸ which held that the president had no presumptive power at all.²⁹

Other holdings, however, had intimated that the power might be *implied* when certain elements are present.³⁰ Whether the courts meant an *implied delegation* or a *presumption of power* is debatable. The issue of the president's power usually arises in cases of deadlock indicating a paralyzation of corporate management.³¹ The Court of

²³ *Matter of Paloma Frocks*, 3 N.Y.2d 572, 147 N.E.2d 779, 170 N.Y.S.2d 509 (1958) (agreement to arbitrate); *Twyeffort v. Unexcelled Mfg. Co.*, 263 N.Y. 6, 188 N.E. 138 (1933). See *Rothman & Schneider v. Beckerman*, 2 N.Y.2d 493, 499, 141 N.E.2d 610, 613, 161 N.Y.S.2d 118, 122 (1957). *But see Tidy-House Paper Corp. v. Adlman*, 4 App. Div.2d 619, 168 N.Y.S.2d 448 (1st Dep't), *aff'd mem.*, 4 App. Div.2d 709, 164 N.Y.S.2d 1005 (2d Dep't 1957). Where the president has acted for the corporation in the past, by handling its business or bringing suits in its name, the board of directors would be estopped from denying his authority now. See *Twyeffort v. Unexcelled Mfg. Co.*, *supra*. This is the doctrine of habitual presidential control and no such analogous doctrine protects the derivative stockholder.

²⁴ *Rothman & Schneider v. Beckerman*, *supra* note 23, at 498, 141 N.E.2d at 613, 161 N.Y.S.2d at 121. See also *Twyeffort v. Unexcelled Mfg. Co.*, *supra* note 23; N.Y. STOCK CORP. LAW § 60.

²⁵ *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 298 N.Y. 483, 490, 84 N.E.2d 790, 792-93 (1949). See also *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 349, 160 N.E.2d 622, 625, 189 N.Y.S.2d 863, 867 (1959) (dissenting opinion).

²⁶ Compare *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, *supra* note 25, with *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 160 N.E.2d 622, 189 N.Y.S.2d 863 (1959). "The merry-go-round of the corporate president's power to institute legal action in the corporate name still spins; and dizzily!" Prunty, *Business Associations*, 34 N.Y.U.L. REV. 1425, 1432 (1959).

²⁷ *Fanchon & Marco v. Paramount Pictures, Inc.*, 202 F.2d 731, 733 (2d Cir. 1953). Cf. *Hardin v. Morgan Lithograph Co.*, 247 N.Y. 332, 160 N.E. 388 (1928) (president has power to make ordinary contracts for his corporation).

²⁸ 298 N.Y. 483, 84 N.E.2d 790 (1949).

²⁹ *Id.* at 490, 84 N.E.2d at 792.

³⁰ See *Twyeffort v. Unexcelled Mfg. Co.*, 263 N.Y. 6, 188 N.E. 138 (1933); *Rothman & Schneider v. Beckerman*, 2 N.Y.2d 493, 141 N.E.2d 610, 161 N.Y.S.2d 118 (1957). See also *Tidy-House Paper Co. v. Adlman*, 4 App. Div.2d 619, 168 N.Y.S.2d 448 (1st Dep't), *aff'd mem.*, 4 App. Div.2d 709, 164 N.Y.S.2d 1005 (2d Dep't 1957).

³¹ See, e.g., *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, *supra* note 28; *Rothman & Schneider v. Beckerman*, *supra* note 30; *Matter of Paloma Frocks*, 3 N.Y.2d 572, 147 N.E.2d 779, 170 N.Y.S.2d 509 (1958). See also

Appeals further suggested that there must be an *urgent* necessity to bring the suit.³² The third and perhaps most constant element in all the cases dealing with the president's power has been the necessity of a lack of direct prohibition by the board.³³

The New York case law can be represented by the views of *Sterling* at one extreme, presuming no power at all; the instant case at the other extreme, presuming the power in all cases of necessity; and the large area in between, construing the presence, absence, and necessity of the various elements. It is in the necessity of these elements that the confusion lies. The Court of Appeals had not said which of the elements is controlling, or indeed, whether one element alone will suffice or whether some or all must be present conjunctively to sustain the power.

Perhaps the most important change in the court's policy as enunciated in the *Sterling* case is the present holding that the president has the *presumptive* authority to bring suit in the corporate name. By presuming that the president has a separate and independent source of power to bring suit, the Court has effectively ruled out at least two of the three previously necessary elements. In the instant case there was no sign of deadlock, indecision, or paralysis.³⁴ In the future, corporation presidents may therefore intervene, in the absence of these elements, against the wishes of the majority of the board.

Secondly, the Court justified the suit on the grounds of its mere necessity to protect and preserve the corporate interest.³⁵ The element of *urgency* has been lost.³⁶ It may therefore be argued that *every* corporate suit is to preserve and protect the corporate interest, and the president is permitted by the instant case to bring suit at any time on the justification that it is for the corporate interest.

Another important difference can be seen in the Court's changing attitude toward the presence of the third element—the necessity of a lack of direct prohibition by the board. The problem of construing the “direct prohibition” of the directors in a small, close corporation was met in *Sterling* by equating their deadlock with a refusal, the

West View Hills, Inc. v. Lizau Realty Corp., 6 N.Y.2d 344, 349, 160 N.E.2d 622, 625, 189 N.Y.S.2d 863, 867 (1959) (dissenting opinion).

³² See *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, *supra*, note 28, at 492, 84 N.E.2d at 794.

³³ See Rothman & Schneider v. Beckerman, *supra* note 30, at 497, 141 N.E.2d at 613.

³⁴ *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 347, 160 N.E.2d 622, 624, 189 N.Y.S.2d 863, 865 (1959).

³⁵ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 34, at 346, 160 N.E.2d at 623, 189 N.Y.S.2d at 864.

³⁶ Compare *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 298 N.Y. 483, 492, 84 N.E.2d 790, 794 (1949), with *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 34, at 346, 160 N.E.2d at 623, 189 N.Y.S.2d at 864.

court interpreting "direct refusal" broadly.³⁷ In the principal case, however, the Court interpreted "direct refusal" strictly and held that even though the directors were obviously opposed to the suit and would have refused had they been asked, the suit was properly brought since they had not been asked and therefore did not directly prohibit the suit.³⁸

Once the power of the president to bring suit has been settled affirmatively, the courts have treated the presidential suit itself, in every other aspect, as identical to the usual suit by the corporation and its management. It possesses all the characteristics of the directors' action, is open to the same defenses, and goes on just as if it had been brought by the directors as a normal management suit—it is truly a suit in the corporate name.³⁹

In the instant case the majority held that the president's power was properly presumed in the circumstances, which amounted to "situations requiring the exercise of such power to preserve and protect the interests of the corporation"⁴⁰ despite the absence of the usual elements, deadlock, indecision, and urgent or compelling necessity from which the power is implied.⁴¹

³⁷ *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, *supra* note 36, at 490, 84 N.E.2d at 793. See also *Tidy-House Paper Co. v. Adlman*, 4 App. Div.2d 619, 168 N.Y.S.2d 448, *aff'd mem.*, 4 App. Div.2d 709, 164 N.Y.S.2d 1005 (1st Dep't 1957).

³⁸ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 34, at 349-50, 160 N.E.2d at 625-26, 189 N.Y.S.2d at 867-68 (dissenting opinion). In a small corporation, the necessity for a direct demand, refusal and prohibition by the board has been commented on as an intolerable formality where the board is obviously, or will obviously be opposed to the suit and the president knows it. See Prunty, *Business Associations*, 34 N.Y.U.L. Rev. 1425, 1433 (1959). See also *Tidy-House Paper Co. v. Adlman*, *supra* note 37, at 621, 168 N.Y.S.2d at 449. *Contra*, *Rothman & Schneider v. Beckerman*, 2 N.Y.2d 493, 141 N.E.2d 610, 161 N.Y.S.2d 118 (1957). Sound reason seems to support the dissent's view in the instant case that the circumstances are equivalent to a direct prohibition. See Prunty, *Business Associations*, 34 N.Y.U.L. Rev. 1425, 1433-34 (1959).

³⁹ The immediate substantive and procedural advantages of the presidential suit over a stockholders' derivative suit in the instant case are obvious. The corporation, not Zaubler, pays the legal fees, expenses, and court costs. There are no requirements of exhaustion of remedies, no necessity of formal demand or wrongful refusal to sue, no derivative stockholder qualifications to meet. A prior burden of proof is put on the defendants to *disprove* the president's authority to act; the corporation and management acting for its interest are behind him rather than passively interested, and he may get a jury trial. The discretionary power of the president's office would also be an effective vehicle for cloaking ratification and acquiescence. See notes 2-21 *supra*; see generally BALLANTINE, *CORPORATIONS* § 51 (rev. ed. 1946).

⁴⁰ *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 346, 160 N.E.2d 622, 623, 189 N.Y.S.2d 863, 864 (1959).

⁴¹ *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 160 N.E.2d 622, 189 N.Y.S.2d 863 (1959).

The dissents in both the lower⁴² and higher⁴³ courts felt that the power could not be implied because there was no deadlock, in-decision, urgency, or present necessity. Both dissents further reasoned that the obvious desire of the directors under the circumstances not to bring suit, which was known to the president, amounted to a direct prohibition.⁴⁴

Although Zaubler had alleged that the defendants were protecting their "selfish interests," the dissent in the higher court realized that he, too, was effectively hiding his own selfish minority interests behind the president's cloak of authority, intimating that he had brought the suit purely for its strategic value in furthering these interests, disguising the action as a management suit which should have been brought over four years ago.⁴⁵

The difference in attitude between the two opinions is remarkable. The majority, preserving the corporate entity theory, reasoned that the corporation itself had a cause of action⁴⁶ which could not be prejudiced by the fact that all those who made up the corporation—directors, president, and every last stockholder—participated in the fraud. The dissent pierced the corporate veil to look at the real parties in interest and reasoned that Zaubler should be estopped from accomplishing as president that which he could not do as a minority stockholder.⁴⁷

The dissent's peek under the corporate facade, besides revealing Zaubler's prejudicial minority interests and changing the entire complexion of the case, is representative of a growing tendency of several courts to treat small, close corporations as partnerships.⁴⁸ By treating these "partnership corporations" no better than the parties themselves treat them, not as entities but as facades, the courts have remitted the parties in justice to the consequences of their own dealings.

The instant case seems to be an encroachment on the powers of directors to manage a corporation and a violation of the court's

⁴² *West View Hills, Inc. v. Lizau Realty Corp.*, 6 App. Div.2d 844, 845, 175 N.Y.S.2d 879, 880 (1st Dep't 1958) (memorandum decision) (dissenting opinion).

⁴³ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 41, at 348, 160 N.E.2d at 625, 189 N.Y.S.2d at 866 (dissenting opinion).

⁴⁴ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* notes 41 and 42.

⁴⁵ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 41, at 350-51, 160 N.E.2d at 626, 189 N.Y.S.2d at 867-68 (dissenting opinion).

⁴⁶ *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 347, 160 N.E.2d 622, 624, 189 N.Y.S.2d 863, 865 (1959).

⁴⁷ *West View Hills, Inc. v. Lizau Realty Corp.*, *supra* note 46, at 350, 160 N.E.2d at 626, 189 N.Y.S.2d at 868 (dissenting opinion).

⁴⁸ See, *e.g.*, *Rothman & Schneider v. Beckerman*, 2 N.Y.2d 493, 499, 141 N.E.2d 610, 614, 161 N.Y.S.2d 118, 122 (1957); *Helms v. Duckworth*, 249 F.2d 482 (D.C. Cir. 1957). See also Prunty, *Business Associations*, 34 N.Y.U.L. Rev. 1425, 1434 (1959).

policy as enunciated in the *Sterling* case.⁴⁹ By encouraging presidents to intervene in the running of a corporation on spurious pretexts or to further their "coincidental" minority interests, the stability and management of corporations is jeopardized.

No set rule can be formulated where the president is a minority stockholder,⁵⁰ nor can the courts disregard the corporate entity theory without good reason. The proper approach should be similar to that used by the dissent in this case. The courts should begin to abandon their traditional reluctance to disregard the entity theory, and look at the actions of the individual parties and their interests and motives as conflicting with or ignoring the legitimate interests of the corporation they have created.⁵¹ This should include a thorough investigation of why a president holding sizable minority stock would have failed in a derivative action or why it would have been otherwise undesirable to bring it. Where the suit is obviously to further primarily the president's personal interests, the courts should not hesitate to relegate him to whatever rights he may properly have as a derivative or representative shareholder.⁵²

In the alternative, where all the stockholders and directors—in fact, the entire corporation, has participated in an internal fraud,

⁴⁹ "We have consistently held that section 27 of the General Corporation law, which provides that the business of a corporation shall be managed by its board of directors, cannot be circumvented." *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 298 N.Y. 483, 492, 84 N.E.2d 790, 793-94 (1949).

⁵⁰ Since every corporation president in New York owns some stock, the difference between a strike suit to further minority interests and an act of legitimate presidential interference is properly one of degree depending ultimately on the facts and circumstances of each individual case. The New York courts have been content thus far to say merely: "One side should not be entitled to maintain an action in the name and at the expense of the corporation simply because the president happens to be allied with its interests." *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, 273 App. Div. 460, 469, 77 N.Y.S.2d 691, 699 (1st Dep't 1948) (dissenting opinion).

⁵¹ Thus, the substantive and procedural elements of the present case seem to reinforce the dissent's picture of this action by Zaubler as a well-concealed minority strike suit brought purely for his own personal selfish interest. See *West View Hills, Inc. v. Lizau Realty Corp.*, 6 N.Y.2d 344, 351, 160 N.E.2d 622, 626, 189 N.Y.S.2d 863, 868 (1959) (dissenting opinion). Zaubler, having asserted his authority, is now in an excellent position to sell his previously worthless stock in the plaintiff corporation to the defendants, or, upon recovery, to "siphon" the money over to the plaintiff corporation in which he retains a one-third interest. *Ibid.* The Court, by its "unbelievably naive" adherence to the entity theory (*cf.* Prunty, *Business Associations*, 34 N.Y.U.L. REV. 1425, 1433 (1959)), has actually placed Zaubler in a position whereby he stands to profit personally from his own questionable dealings in the past with West View Hills, Inc.

⁵² See *Tidy-House Paper Corp. v. Adlman*, 4 App. Div.2d 619, 168 N.Y.S.2d 448, (1st Dep't), *aff'd mem.*, 4 App. Div.2d 709, 164 N.Y.S.2d 1005 (2d Dep't 1957); *Sterling Industries, Inc. v. Ball Bearing Pen Corp.*, *supra* note 49. Compare *Kardwheel Corp. v. Karper*, 1 Misc.2d 707, 148 N.Y.S.2d 132 (Sun. Ct. 1956) (suit by officers in name of corporation dismissed), with *Cole Steel Equip. Co. v. Kardwheel Corp.*, 150 N.Y.S.2d 415 (Sup. Ct. 1956) (derivative suit instituted by same officers permitted).

such considerations should be admissible against the corporation in a presidential action at the court's discretion.⁵³



COURTS — FEDERAL JURISDICTION — LIMITS ON DISCRETION OF DISTRICT COURT IN DIVERSITY CASE RELATING TO PROBATE AND ADMINISTRATION. — Plaintiff, beneficiary of a testamentary trust, brought an action in the District Court for the Northern District of New York, seeking, *inter alia*, damages for breach of trust and a construction of the will of the testatrix to declare plaintiff the owner of certain stock. The district court declined jurisdiction although there was diversity of citizenship. In reversing in part and affirming in part the order of the district court, the Court of Appeals for the Second Circuit *held* that while the district court was correct in disavowing jurisdiction over part of plaintiff's claim, it had no discretion to decline jurisdiction of those claims of plaintiff that would not interfere with the previously attached quasi in rem jurisdiction of the state surrogate's court, notwithstanding the fact that the estate was still in administration. *Beach v. Rome Trust Co.*, 269 F.2d 367 (2d Cir. 1959).

Plaintiff's complaint in the case presented an opportunity for the Court to consider many of the problems of federal jurisdiction over claims against decedents' estates, *i.e.*, to what extent do federal courts, sitting in equity, have subject matter jurisdiction over such matters, the effect of state law on such jurisdiction and the discretionary power of the federal court to decline the exercise of jurisdiction otherwise existing. Actions in federal courts affecting decedents' estates present jurisdictional questions in more than one sense of that term. A district court's jurisdiction is both defined and limited by the statute that grants it.¹ Also in entertaining actions against executors and administrators the district court is sitting as a court of equity, and the considerations that govern equity's subject matter jurisdiction apply.² Finally, in the area under discussion, the jurisdiction of the federal court is limited by the principles of comity which obtain when courts of concurrent jurisdiction entertain actions respecting the same subject matter.³

⁵³ *Cf.* *Tidy-House Paper Co. v. Adlman*, *supra* note 52. A final consideration is that the use of the presidential suit by unscrupulous presidents may lead, as in the case of minority stockholders' suits, to oppressive legislation which would make legitimate and sincere presidential interference difficult.

¹ Actions based on diversity of citizenship, 28 U.S.C. § 1332 (1958), constitute the bulk of litigation that will be considered.

² See generally *Case of Broderick's Will*, 88 U.S. (21 Wall.) 503 (1874).

³ See 1 MOORE, FEDERAL PRACTICE ¶ 0.222 (2d ed. 1959).