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## **Corporations--Reimbursement for Litigation Expenses Incurred in Defending Criminal Action Denied (Matter of Schwarz v. General Aniline & Film Corp., 305 N.Y. 395 (1953))**

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forbids these unions when solemnized within its boundaries.<sup>17</sup>

Many states, on the other hand, proscribe uncle-niece marriages by statutory enactment.<sup>18</sup> Thus, although such a validly contracted foreign marriage is not deemed void as being opposed to the generally accepted opinion of Christendom, it is declared invalid in those jurisdictions wherein the prohibitory statute is given extraterritorial application to domiciliaries.<sup>19</sup> Not all states, however, give this effect to their inhibitive statutes.<sup>20</sup> The basis used in determining the scope of the statutes is the intent of the legislature.<sup>21</sup>

The instant case delineates the New York position on the two exceptions to the general rule. The Court of Appeals refused to consider the uncle-niece marriage involved as repugnant to the policy of the state and refrained from applying the domestic statute prohibiting such unions to a valid foreign marriage of its domiciliaries.<sup>22</sup>

This decision clearly aligns New York with those jurisdictions favoring the broadest interpretation of the general rule that the *lex loci contractus* should control.<sup>23</sup>



CORPORATIONS — REIMBURSEMENT FOR LITIGATION EXPENSES INCURRED IN DEFENDING CRIMINAL ACTION DENIED.—The petitioner, former vice-president and director of defendant corporation, was indicted by a federal grand jury for alleged violations of the Sherman Anti-Trust Act.<sup>1</sup> He pleaded *nolo contendere*.<sup>2</sup> and was

<sup>17</sup> *Campione v. Campione*, 201 Misc. 590, 107 N. Y. S. 2d 170 (Sup. Ct. 1951); *Fensterwald v. Burk*, 129 Md. 131, 98 Atl. 358 (1916).

<sup>18</sup> See, e.g., N. Y. DOM. REL. LAW § 5(3); CAL. CIV. CODE § 59 (1951); ILL. REV. STAT. c. 89, § 1 (1951); MASS. ANN. LAWS c. 207, § 2 (1933).

<sup>19</sup> *Matter of De Wilton*, [1900] 2 Ch. 481 (marriage between Jewish uncle and niece, English domiciliaries, deemed invalid in England although it was validly contracted abroad).

<sup>20</sup> See *Van Voorhis v. Brintnall*, 86 N. Y. 18 (1881); *Matter of Perez*, 219 P. 2d 35 (Cal. 1950); *Putnam v. Putnam*, 25 Mass. 433 (1829). Those states which have adopted the Uniform Marriage Evasion Act determine the validity of marriages of foreign domiciliaries within their jurisdiction by applying the laws of the domicile of the parties. *Beaudoin v. Beaudoin*, 270 App. Div. 631, 62 N. Y. S. 2d 920 (3d Dep't 1946).

<sup>21</sup> See *Van Voorhis v. Brintnall*, *supra* note 20 at 35.

<sup>22</sup> N. Y. DOM. REL. LAW § 5(3).

<sup>23</sup> *But cf. Cunningham v. Cunningham*, 206 N. Y. 341, 99 N. E. 845 (1912).

<sup>1</sup> 26 STAT. 209 (1890), 15 U. S. C. § 1 (1946).

<sup>2</sup> FED. R. CRIM. P. 11. Although a plea of *nolo contendere* is not to be deemed an admission of facts in any other action [38 STAT. 731 (1914), 15 U. S. C. § 16 (1946)] the trial court in the instant civil case held that the imposition of a fine was such an adjudication of defendant's negligence in the performance of his duties as to deny him the right to reimbursement under

fined \$500. To recover litigation expenses incurred as a result of this prosecution, the present petition was brought under the General Corporation Law.<sup>3</sup> The Court of Appeals in affirming a dismissal of the complaint held that the New York statute does not entitle an officer of a corporation to reimbursement for expenses incurred in defense of a criminal proceeding. *Matter of Schwarz v. General Aniline & Film Corp.*, 305 N. Y. 395, 113 N. E. 2d 533 (1953).

At common law it has been held that a corporation was under no obligation to reimburse its officers or directors for litigation expenses incurred in defense of suits brought against them in their representative capacity.<sup>4</sup> Thus in *New York Dock Co. v. McCollum*<sup>5</sup> an action was brought by a corporation for a declaratory judgment to quell demands for reimbursement by directors who had successfully defended a stockholders' suit. The court there decided that in the absence of an express contract therefor, a corporation was not obliged to reimburse the directors on the theory of *implied* contract. But whether a corporation could expressly contract with directors for indemnification was not clear.<sup>6</sup> Case law, however, indicates two theories by which corporate officials, guilty of no wrongdoing,<sup>7</sup> could recover litigation expenses. Under one theory, reimbursement may be had where the defense of the action has brought some benefit to the corporation;<sup>8</sup> under the other, reimbursement could be effected by unanimous consent of the stockholders.<sup>9</sup> Nevertheless, a definitive statement regarding the legality of indemnity agreements between a corporation and its officials is lacking.<sup>10</sup> It had been suggested that the broad language of the New York corporation laws would allow

Section 64 of the General Corporation Law. *Matter of Schwarz v. General Aniline & Film Corp.*, 198 Misc. 1046, 102 N. Y. S. 2d 325 (Sup. Ct. 1951).

<sup>3</sup> N. Y. GEN. CORP. LAW §§ 64-68.

<sup>4</sup> *Bailey v. Bush Terminal Co.*, 46 N. Y. S. 2d 877 (Sup. Ct. 1943), *aff'd mem.*, 267 App. Div. 899, 48 N. Y. S. 2d 324 (1st Dep't), *aff'd mem.*, 293 N. Y. 735, 56 N. E. 2d 739 (1944); see PRASHKER, *CASES AND MATERIALS ON CORPORATIONS* 804 (2d ed. 1949). *Contra*: *Solimine v. Hollander*, 129 N. J. Eq. 264, 19 A. 2d 344 (1941).

<sup>5</sup> 173 Misc. 106, 16 N. Y. S. 2d 844 (Sup. Ct. 1939).

<sup>6</sup> See 1945 LEG. DOC. NO. 65(E), REPORT, N. Y. LAW REVISION COMMISSION 131, 154-156 (1945).

<sup>7</sup> "It would certainly seem to be a travesty upon justice that the company should be compelled to pay the expenses of a suit brought by minority stockholders for the purpose of restoring delinquent trustees to a proper sense of their duties." *McConnell v. Combination Min. & Mill. Co.*, 31 Mont. 563, 79 Pac. 248, 251 (1905).

<sup>8</sup> See *Godley v. Crandall & Godley Co.*, 181 App. Div. 75, 78, 168 N. Y. Supp. 251, 254 (1st Dep't 1917), *aff'd mem.*, 227 N. Y. 656, 126 N. E. 908 (1920); *New York Dock Co. v. McCollum*, *supra* note 5 at 111, 16 N. Y. S. 2d at 849; *Griesse v. Lang*, 37 Ohio App. 553, 175 N. E. 222, 223 (1931).

<sup>9</sup> See *Griesse v. Lang*, *supra* note 8.

<sup>10</sup> See *Jervis, Corporate Agreements to Pay Directors' Expenses in Stockholders' Suits*, 40 COL. L. REV. 1192, 1194 (1940).

inclusion of such agreements in certificates of incorporation and in by-laws.<sup>11</sup>

To deny reimbursement to innocent officers and directors, it was urged, would discourage the less affluent, albeit competent, individuals from assuming these positions of responsibility.<sup>12</sup> Furthermore, officials of limited means would be deprived of the right to competent counsel in the expensive corporate litigation, and would be subject to pressures exerted by litigious stockholders who threaten groundless suits.<sup>13</sup>

With these objections in mind,<sup>14</sup> therefore, the legislature of the State of New York enacted two types of remedial statutes. The first of these, permissive in nature, granted authorization to include reimbursement provisions in new certificates of incorporation or to modify existing certificates or by-laws by addition of such provisions.<sup>15</sup> The other remedial statute<sup>16</sup> allowed officers or directors to recover, by court action, expenses incurred in the successful<sup>17</sup> defense of "any action, suit or proceeding" brought by the corporation or in its behalf. The legislature, however, recognizing the need for a more inclusive statute, expanded the scope of the statute to permit reimbursement to directors, officers, and "employees" for such expenses.<sup>18</sup> It has also removed the limitation that the action which engendered the expenses be one by the corporation or in its behalf.<sup>19</sup>

In deciding the instant case, the court has held that *criminal proceedings* are not compensable actions within the intendment of the statute. Therefore, any corporate official indicted, as in this case, for criminal violations of the Sherman Anti-Trust Act, or for

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<sup>11</sup> *Id.* at 1202. See N. Y. GEN. CORP. LAW § 13(2) (which states that "[t]he certificate of incorporation . . . may contain any provision for the regulation of its business and the conduct of its affairs. . ."); N. Y. GEN. CORP. LAW § 14(5) (which grants the power to a corporation ". . . to make by-laws, not inconsistent with law, for the management of its business, [and] the regulation of its affairs. . .").

<sup>12</sup> See Washington, *Litigation Expenses of Corporate Directors in Stockholders' Suits*, 40 COL. L. REV. 431, 432, 451 (1940).

<sup>13</sup> See *Solimine v. Hollander*, 129 N. J. Eq. 264, 19 A. 2d 344, 348 (1941).

<sup>14</sup> See 1945 LEG. DOC. NO. 65(E), REPORT, N. Y. LAW REVISION COMMISSION 131, 149-166 (1945).

<sup>15</sup> N. Y. GEN. CORP. LAW § 27-a (now GEN. CORP. LAW § 63). For such provisions, see 1945 LEG. DOC. NO. 65(E), REPORT, N. Y. LAW REVISION COMMISSION 131, 170-174 (1945).

<sup>16</sup> N. Y. GEN. CORP. LAW § 61-a (now embodied in GEN. CORP. LAW §§ 64-68).

<sup>17</sup> In the event of a settlement with the court's approval, it is within judicial discretion to allow reimbursement. *Id.* § 67.

<sup>18</sup> *Id.* § 64.

<sup>19</sup> See 1945 LEG. DOC. NO. 65(E), REPORT, N. Y. LAW REVISION COMMISSION 131, 158-166 (1945). The introduction of similar statutes in other states is indicative of the trend. DEL. CODE ANN. tit. 8, c. 1, § 122(10) (1953); KY. REV. STAT. § 271.375 (Baldwin, 1953); N. J. STAT. ANN. tit. 14, c. 3, § 14 (Supp. 1952).

any other criminal act connected with the management of a corporation, may not look to the corporation for recovery of his litigation expenses.<sup>20</sup> In a divided court, the majority was of the opinion that inasmuch as the statute is in derogation of the common law it should be strictly construed.<sup>21</sup> The dissenting judges, in sharp contrast, contended that compensation for criminal proceedings was within the intention of the legislators<sup>22</sup> as manifested, among other things, by the ". . . broad and . . . all-inclusive . . ." <sup>23</sup> wording of the statute.

The court, in denying reimbursement, stated that "[i]t would be a very strange public policy, indeed, which would set up legal machinery whereby one *charged with*, or convicted of, a crime, of whatever kind, could require the corporation . . . to pay his legal expenses."<sup>24</sup> Where guilt is established, the statement appears to be correct.



CUSTODY—JURISDICTIONAL REQUIREMENTS FOR FULL FAITH AND CREDIT.—In a habeas corpus proceeding to regain custody of three children, Ohio courts felt bound under the full faith and credit clause of the Constitution<sup>1</sup> to recognize a Wisconsin decree, rendered in an *ex parte* divorce action, granting custody of the children to their father.<sup>2</sup> The United States Supreme Court reversed and *held* that full faith and credit need not be given to a custody decree where the court awarding the decree lacked in personam jurisdiction over the mother. *May v. Anderson*, 345 U. S. 528 (1953).

The purpose of the full faith and credit clause of the Constitution as declared by the United States Supreme Court is that ". . . litigation once pursued to judgment shall be as conclusive of the rights of the parties in every other court as in that where the judgment was rendered so that a cause of action merged in a judg-

<sup>20</sup> In the event of a conviction, the official cannot be held personally liable to the corporation for losses caused by his acts if it can be shown that he acted in good faith and with the intention of benefiting the corporation. *Simon v. Socony-Vacuum Oil Co.*, 179 Misc. 202, 38 N. Y. S. 2d 270 (Sup. Ct. 1942), *aff'd mem.*, 267 App. Div. 890, 47 N. Y. S. 2d 589 (1st Dep't 1944).

<sup>21</sup> See *Matter of Schwarz v. General Aniline & Film Corp.*, 305 N. Y. 395, 404-406, 113 N. E. 2d 533, 537-538 (1953) (concurring opinion).

<sup>22</sup> *Id.* at 407-409, 113 N. E. 2d at 538-540 (dissenting opinion).

<sup>23</sup> *Id.* at 407, 113 N. E. 2d at 539.

<sup>24</sup> *Id.* at 402, 113 N. E. 2d at 536 (emphasis added).

<sup>1</sup> "Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State." U. S. CONST. Art. IV, § 1.

<sup>2</sup> *Anderson v. May*, 91 Ohio App. 557, 107 N. E. 2d 358, *appeal dismissed*, 157 Ohio St. 436, 105 N. E. 2d 648 (1952).