

Corporations--Cumulative Voting Provision Voids Removal By-Law (Matter of Rogers Imports, Inc., 202 Misc. 761 (Sup. Ct. 1952))

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answered by the Court has been, in the opinion of the writer, correctly decided by the lower tribunals.¹⁸

In the most significant passage of the opinion, the Court stated that where both damages and profits are *proven*, the court, in its discretion, may disregard such proof and award statutory damages.¹⁹ But when the copyright owner can prove both his damages and the infringer's profits, the underlying basis for the "in lieu" clause is eliminated. To allow a court in such cases to summarily dismiss the true amount of damage and substitute a discretionary amount, far exceeds the scope of the statute. If, therefore, the direct holding is followed, and the dicta disregarded, the instant case will have greatly furthered the clarification of this troublesome statute.



CORPORATIONS — CUMULATIVE VOTING PROVISION VOIDS REMOVAL BY-LAW.—Pursuant to a by-law providing for such action, a corporate director was removed without cause, and an election was held to fill the vacancy. Petitioner, owner of forty per cent of the voting stock of the corporation, brought an action pursuant to Section 25 of the General Corporation Law¹ to set aside the election on the ground that it violated her rights under a cumulative voting provision adopted subsequent to the enactment of the by-law. *Held*: the adoption of a cumulative voting provision invalidated the by-law insofar as it provided for the removal of a director without cause. *Matter of Rogers Imports, Inc.*, 202 Misc. 761, 116 N. Y. S. 2d 106 (Sup. Ct. 1952).

The purpose of cumulative voting is to afford minority interests the opportunity to secure representation on the board of directors;² and it appears that express statutory authorization is a necessary prerequisite to its use.³ In gauging the effect of a cumulative voting

¹⁸ See note 12 *supra*.

¹⁹ See *Woolworth Co. v. Contemporary Arts, Inc.*, *supra* note 14, at 226. "We think that the statute empowers the trial court in its sound discretion to determine whether on all the facts a recovery upon *proven* profits and damages or one estimated within the statutory limits is more just." *Ibid.* (emphasis added).

¹ "Upon the application of any member aggrieved by an election . . . the supreme court . . . shall forthwith hear the proofs and allegations of the parties, and confirm the election or order a new election, as justice may require."

² See *Matter of Jamaica Consumers' Ice Co.*, 190 App. Div. 739, 741, 180 N. Y. Supp. 384, 386 (1st Dep't), *aff'd*, 229 N. Y. 516, 129 N. E. 897 (1920); see BALLANTINE, CORPORATIONS 402 (Rev. ed. 1946); PRASHKER, CASES AND MATERIALS ON CORPORATIONS 481-90 (2d ed. 1949).

³ See *Matter of Brophy*, 13 N. J. Misc. 462, 179 Atl. 123, 129 (Sup. Ct. 1935). *But see* *Quilliam v. Hebbroville Utilities, Inc.*, 241 S. W. 2d 225

statute, it is proper to consider whether the provision guarantees⁴ or merely permits⁵ exercise of the privilege. Where of the guarantying type, it may properly be held that a by-law enabling a majority interest to remove a director without cause⁶ is subordinate to the purpose underlying the provision, and therefore inapplicable to minority interest directors who are innocent of official misconduct.⁷ Where, however, the authorization is merely permissive, it is questionable whether such a removal by-law so conflicts with a public policy favoring cumulative voting that the courts should nullify the by-law in the absence of legislative authority.⁸

The New York provision⁹ falls within the permissive type, and thus depends for its existence on its express inclusion in the original charter, or on an amendment ratified by the holders of two-thirds of the voting stock.¹⁰ But the mere inclusion of the provision in the original charter, or its subsequent addition thereto, does not give the minority a vested right to vote cumulatively. The charter may be subsequently amended to remove the provision,¹¹ or its effectiveness can be frustrated by the reduction¹² and classification¹³ of

(Tex. Civ. App. 1951) (by-law providing for cumulative voting without statutory authority therefor amended to provide for straight voting).

⁴ *E.g.*, CAL. CORP. CODE § 2235 (Deering, 1948); MICH. COMP. LAWS § 450.651 (1948); MINN. STAT. § 301.26(3) (1949); OHIO CODE ANN. § 8623-50a (Baldwin Supp. 1948-52); PA. STAT. ANN. tit. 15, § 2852-505 (Purdon Supp. 1952); WASH. REV. CODE § 23.32.070 (1951).

⁵ *E.g.*, LA. REV. STAT. tit. 12, § 32B (1950); NEV. COMP. LAWS § 1629 (Hillyer, 1929); N. Y. STOCK CORP. LAW § 49. For full list of states and type statute adopted, see WILLIAMS, CUMULATIVE VOTING FOR DIRECTORS 7-9 (1951).

⁶ The power, while given statutory approval in several states (*e.g.*, MINN. STAT. § 301.29 (1949); OHIO CODE ANN. § 8623-56 (Baldwin Supp. 1948-52); PA. STAT. ANN. tit. 15, § 2852-405 (Purdon, 1938)), can be exercised in New York without such authority. *Abberger v. Kulp*, 156 Misc. 210, 281 N. Y. Supp. 373 (Sup. Ct. 1935) (case contains concise summary of rules applicable to removal of directors). In some jurisdictions, however, it is held that there is no such common-law right. *See Walsh v. State*, 199 Ala. 123, 74 So. 45, 47 (1917); *see Imperial Hydropathic Hotel Co. v. Hampson*, 23 Ch. D. 1 (1882) *passim*.

⁷ *See Bowes and De Bow, Cumulative Voting at Elections of Directors of Corporations*, 21 MINN. L. REV. 351, 367 (1937).

⁸ The by-laws of a corporation constitute a contract among the shareholders. *See Weisblum v. LiFalco Mfg. Co.*, 193 Misc. 473, 476, 84 N. Y. S. 2d 162, 166 (Sup. Ct. 1947). It would appear that the court, in the absence of a violation of statute or public policy, would be impairing the obligation of contracts by substituting its judgment for that of the parties and in effect altering their contract.

⁹ N. Y. STOCK CORP. LAW § 49.

¹⁰ N. Y. STOCK CORP. LAW §§ 35(2) (D), 37(1) (C) (2).

¹¹ *Ibid.* For a decision allowing dissenting stockholder right of appraisal, *see Application of New York Hanseatic Corp.*, 200 Misc. 530, 103 N. Y. S. 2d 698 (Sup. Ct. 1951).

¹² N. Y. STOCK CORP. LAW §§ 35(2) (G), 37(1) (C) (1) (f).

¹³ *Id.* §§ 35(2) (J), 37(1) (C) (2); *see Bond v. Atlantic Terra Cotta Co.*, 137 App. Div. 671, 122 N. Y. Supp. 425 (1st Dep't 1910); WILLIAMS, CUMU-

directors. By the latter method, the statutory provisions of even those states which guaranty the privilege can be circumvented.¹⁴

A provision for the removal of directors without cause is also used to achieve the same result. Of the eight states¹⁵ which have legislatively recognized this conflict, six have refrained from invalidating the removal by-law, but have merely limited its use.¹⁶ It is significant that of these six states, five guarantee the cumulative voting right.¹⁷ It would appear, then, that in New York, whose public policy is not as strong¹⁸ as the aforementioned five states, it should not be held as a *matter of law* that the adoption of a cumulative voting provision *ipso facto* invalidates the removal by-law. Conceding, arguendo, that under the particular facts (forty per cent dissenting stockholder) the decision achieved substantial justice, its scope was too broad in unqualifiedly invalidating the by-law. To hold that the adoption of a cumulative voting provision *ipso facto* abrogates the removal by-law might well work a clearly inequitable result. In a situation where the director to be removed was elected by the majority, rather than by the dissenting minority's exercise of their cumulative voting powers, the automatic abrogation rule would operate to prevent the majority from removing their own director, and thus frustrate their intention in originally enacting the removal clause.

A more logical solution to the problem would provide that only where the objecting stockholder wields sufficient votes which, if cumulatively voted, could elect a director should the by-law be suspended; but that in all other cases it would remain valid and operative. Authority for such a position may be found in the legislation of six¹⁹ of those eight states which have provided against such a contingency. In only one²⁰ of those states has the legislature seen fit to do what the decision in the instant case effects. If the

LATIVE VOTING FOR DIRECTORS 48 (1951). For an interesting discussion of classification and its effect on cumulative voting provisions, see Note, 56 *DICK. L. REV.* 330 (1952).

¹⁴ Some states, however, have provided against this possibility and prohibit reduction or classification which would have the effect of defeating the cumulative voting provision. See, e.g., *MICH. COMP. LAWS* § 450.13(3) (1948).

¹⁵ California, Louisiana, Michigan, Minnesota, Nevada, Ohio, Pennsylvania and Washington.

¹⁶ See note 19 *infra*.

¹⁷ California, Minnesota, Ohio, Pennsylvania and Washington.

¹⁸ Prior to the decision in the instant case, the most that could be said with reference to the public policy of New York concerning cumulative voting was that it was neutral. "We find in these sections of the statute [authorizing cumulative voting] a legislative declaration that provision for cumulative voting is not against public policy. . . ." *Matter of American Fibre Chair Seat Co.*, 265 N. Y. 416, 420, 193 N. E. 253, 255 (1934).

¹⁹ *CAL. CORP. CODE* § 810 (Deering, 1948); *MINN. STAT.* § 301.29 (1949); *NEV. COMP. LAWS* § 1632 (Hillyer, 1929); *OHIO CODE ANN.* § 8623-56 (Baldwin Supp. 1948-52); *PA. STAT. ANN.* tit. 15, § 2852-405 (Purdon, 1938); *WASH. REV. CODE* § 23.36.040 (1951). See *WILLIAMS, op. cit. supra* note 13, at 56.

²⁰ *LA. REV. STAT.* tit. 12, § 34C(4) (1950).

legislatures of various states can disagree on the method of solving this problem, it is submitted that the *court's* action in the instant case was improper as an undue usurpation of the legislative function, especially since it chose the least logical of the several possible solutions.



CORPORATIONS—IS ACTION TO COMPEL DECLARATION OF DIVIDEND DERIVATIVE?—In an action by a stockholder against a corporation and its directors to compel the declaration of a dividend, the corporation moved for an order requiring plaintiff to provide security for expenses, on the ground that the action was derivative within the meaning of the New York statute.¹ The motion was granted.² In affirming, the Appellate Division *held* that the present suit is within the statute since it is an action brought in the right of the corporation, and not in the personal right of the stockholder.³ *Gordon v. Elliman*, 280 App. Div. 655, 116 N. Y. S. 2d 671 (1st Dep't 1952).

A "derivative" action, cognizable only in Equity,⁴ is a suit by a stockholder to enforce a corporate cause of action.⁵ As conditions precedent to its institution and maintenance, the plaintiff must allege and prove that the corporation has been damaged, and a cause of action exists in its favor;⁶ that a demand has been made, but the corporation refuses to commence the action;⁷ and that he was a stockholder at the time of the transaction of which he complains.⁸ The corporation, of necessity, is made a party defendant,⁹ since the relief

¹ N. Y. GEN. CORP. LAW § 61-b.

² *Gordon v. Elliman*, 115 N. Y. S. 2d 567 (Sup. Ct. 1952).

³ Callahan, J., dissenting.

⁴ See *Isaac v. Marcus*, 258 N. Y. 257, 263, 179 N. E. 487, 489 (1932).

⁵ See *Price v. Gurney*, 324 U. S. 100, 105 (1945); see *Hawes v. Oakland*, 104 U. S. 450 (1881) (comprehensive treatment of necessary elements of a derivative action).

⁶ *Waters v. Horace Waters & Co.*, 201 N. Y. 184, 94 N. E. 602 (1911); *Lifshutz v. Adams*, 285 N. Y. 180, 33 N. E. 2d 83 (1941); *Moriarty v. James Butler Grocery Co.*, 261 App. Div. 20, 24 N. Y. S. 2d 105 (1st Dep't 1940), *aff'd mem.*, 286 N. Y. 687, 37 N. E. 2d 36 (1941); *Scheinman v. National Container Corp.*, 165 Misc. 267, 300 N. Y. Supp. 780 (Sup. Ct. 1937).

⁷ *Corbus v. Alaska Treadwell Gold Mining Co.*, 187 U. S. 455 (1903); *NY PA NJ Utilities Co. v. Public Service Comm'n*, 23 F. Supp. 313 (S. D. N. Y. 1938); see *Brinckerhoff v. Bostwick*, 88 N. Y. 52, *appeal dismissed*, 106 U. S. 3 (1882) (if demand shown to be futile, stockholder may dispense with it); *Dunphy v. Travelers' Newspaper Ass'n*, 146 Mass. 495, 16 N. E. 426 (1888) (plaintiff failed to show futility of demand).

⁸ N. Y. GEN. CORP. LAW § 61 (he may also show that his stock thereafter devolved upon him by operation of law).

⁹ *Davenport v. Dows*, 18 Wall. 626 (U. S. 1873); see *Jones v. Van Heusen*