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Amendment to the Stock Corporation Law Relating to Certificates of Incorporation Requiring More Than Statutory Majority for Corporate Action

Isador Liddie

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then, perhaps it would be void only because the court said so. To allow a defendant to commit legal suicide by urging that the instrument under which he claims is void, and for the court to hold on that ground that the plaintiff needs no relief, although his title is seriously clouded in fact, is neither just nor reasonable."²³

It is evident, therefore, that the amendment to Section 500 which has just been enacted was not only desirable but necessary in order that the uncertainties and inequities which are now prevalent, might be finally resolved.

The procedure available under the new amendment is also applicable to outlawed vendors' liens as the problems inherent in such liens are analogous to those presented by outlawed mortgages.²⁴ The vendor's lien contemplated by this statute is the lien implied by law in favor of a vendor who has conveyed without taking security for the purchase price and also the lien which is expressly reserved by contract but which has not been raised to the dignity of a mortgage.²⁵

The statute also provides that the interest of any mortgagee is an "interest in real property," as that phrase is used in the statutory proceeding and thus the remedy of cancellation is made available to a junior mortgagee whose mortgage might become a first lien upon cancellation of the outlawed mortgage. The remedy is also available to a contract vendee who has not as yet taken a conveyance as the statute likewise defines the interest of a contract vendee as an "interest in real property."²⁶

HAROLD E. COLLINS.

AMENDMENT TO THE STOCK CORPORATION LAW RELATING TO CERTIFICATES OF INCORPORATION REQUIRING MORE THAN STATUTORY MAJORITY FOR CORPORATE ACTION.—Effective September 1, 1948, the Stock Corporation Law has been amended by inserting a new section to be Section 9.¹ The amendment permits certificates of incorporation to include therein provisions requiring more than a statutory majority or plurality for a quorum vote or consent of directors or shareholders. Four specific limitations are placed upon certificates of incorporation requiring more than the statutory majority. No such requirement will be deemed valid unless (1) it appears in the certificate as originally filed or as originally amended;

²³ 38 Minn. 70, 71, 72, 35 N. W. 723, 724, 725 (1887).

²⁴ N. Y. LAW REVISION COMMISSION REPORT, LEGIS. DOC. NO. 65(N) (1948).

²⁵ Franklin Savings Bank v. Ascension Memorial Church, — Misc. —, 55 N. Y. S. 2d 808 (Sup. Ct. 1945).

²⁶ N. Y. LAW REVISION COMMISSION REPORT, LEGIS. DOC. NO. 65(N) (1948).

¹ Laws of N. Y. 1948, c. 862.

(2) notice of its existence appears on the face of all stock certificates; (3) it specifies a period of duration no longer than ten years; and (4) the certificate shall be subscribed and acknowledged by every subscriber to stock if no stock has been issued.

Legislative action was prompted by the decision in *Benintendi v. Kenton Hotel*.² In that case two shareholders owning one-third and two-thirds respectively of the corporate stock agreed to four amendments to the by-laws requiring unanimous vote (1) for all elections of directors, (2) for all shareholders' resolutions, (3) for all directors' resolutions, and (4) for all amendments of the by-laws by shareholders. The court, in a divided decision, struck down the first three by-laws as being inconsistent with the statutory scheme of corporate government set up by the General Corporation Law³ and the Stock Corporation Law.⁴

The principle that a requirement of unanimity for corporate action may violate statutory requirements first appeared in New York in *Matter of Boulevard Theatre and Realty Co.*⁵ There it was held that a clause in the certificate of incorporation requiring unanimous consent of stockholders to elect directors was in contravention of Section 55 of the General Corporation Law. That section provides that directors shall be chosen "by a plurality of the votes."

In the *Benintendi* case the court applied the same reasoning to unanimous resolutions by stockholders and directors. Since Section 27 of the Stock Corporation Law permits a corporation to enact a by-law fixing "the number of directors necessary to constitute a quorum at a number less than a majority of the board but not less than one-third of its number," the conclusion, said the court, is inescapable that a by-law requiring every action of the board to be by unanimous vote is inconsistent with this section. The basic idea of a "quorum" compels the conclusion that, when that required number of persons goes into session as a body the votes of a majority thereof constitutes a sufficient number for binding action. Although the second by-law violated no known decision or specific statute, nevertheless it violated the legislative intent as manifested by the statutory specification of the total vote percentages required to authorize various types of corporate action.⁶

The minority opinion, however, argued that, as in this case, where no rights of third persons are affected or public policy con-

² 294 N. Y. 112, 60 N. E. 2d 829 (1945).

³ N. Y. GEN. CORP. LAW § 27.

⁴ N. Y. STOCK CORP. LAW § 55.

⁵ 195 App. Div. 518, 186 N. Y. Supp. 430 (1st Dep't 1921), *aff'd*, 231 N. Y. 615, 132 N. E. 910 (1921).

⁶ See N. Y. Stock Corp. Law §§ 36, 37, requiring an affirmative two-third vote for changing the capitalization, and N. Y. Gen. Corp. Law §§ 102, 103, empowering the holders of a majority of the stock to dissolve the corporation and giving the same power to holders of half the stock, if there be a deadlock on the question of dissolution.

travened, stockholders may agree to anything they wish.⁷ It would seem that this view is not at variance with well-reasoned opinion. It has been held that the owners of 100% of the stock of a corporation may do with it what they will, even to the extent of giving it away, provided the rights of creditors are not involved, and the public policy of the state is not offended.⁸ While it is true that courts have, at times, laid down various tests as determinative of the enforceability of agreements which are admittedly illegal as by-laws, in the final analysis damages suffered or threatened to someone should be the sole criterion of enforceability. As pointed out in *Clark v. Dodge*, ". . . if the enforcement of a particular contract damages nobody—not even, in any perceptible degree, the public—one sees no reason for holding it illegal, even though it impinges slightly upon the broad provisions of Section 27. Damage suffered or threatened is a logical and practical test, and has come to be the one generally adopted by the courts."⁹

In *Little v. Garabrant*¹⁰ the court held that with the consent of all the stockholders, and with no rights of creditors involved, the corporate assets might be given away. Pursuing further this trend of thought, it would seem that if funds are misapplied by directors of a corporation, or converted to their own use, abuse of authority as between the directors and the corporation may be cured by the unanimous consent or ratification of the stockholders. To countenance the practice of larceny and conversion by fiduciaries is strongly in contravention of public policy, and yet unanimous consent or ratification validates even such acts.¹¹

It is to be noted that the *Benintendi* case dealt with a situation where the controverted provisions were in the by-laws of the corporation, whereas the Stock Corporation Law as amended by Section 9 deals with certificates of incorporation. Although there has been no decision following the *Benintendi* case specifically applying the law as there set forth to a situation involving certificates of in-

⁷ *Ripin v. U. S. Woven Label Co.*, 205 N. Y. 442, 98 N. E. 855 (1912).

⁸ *Clark v. Dodge*, 269 N. Y. 410, 199 N. E. 641 (1936); *Matter of American Fibre Chair Seat Corp.*, 265 N. Y. 416, 193 N. E. 253 (1934). Courts have constantly adverted to public policy arguments in holding agreements invalid, when it is difficult to see where the public is involved, e.g., *McQuade v. Stoneham*, 263 N. Y. 323, 329, 189 N. E. 234, 236 (1934). *But cf. Lorillard v. Clyde*, 86 N. Y. 384, 389 (1881), where Judge Andrews, delivering the opinion of the court, said, "I can see no objection on the score of public policy, to an agreement between parties about to form a corporation, agreeing upon the general plan upon which it is to be organized and conducted, so long as nothing is provided for inconsistent with the provisions of the statute, or immoral in itself."

⁹ 269 N. Y. 410, 415, 199 N. E. 641, 642 (1936), Note, 28 COL. L. REV. 366, 372 (1928).

¹⁰ 90 Hun 404 (N. Y. 1895), *aff'd*, 153 N. Y. 661 (1897).

¹¹ MORAWETZ, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS § 625 (2d ed. 1886).

corporation, the reasoning in that case strongly indicated that the courts would probably have followed the *Benintendi* ruling in such later case. By making the amendment applicable to certificates of incorporation only, the new legislation does not specifically rectify the *Benintendi* decision. However, as the court in the latter case based its statutory interpretation largely on the intent of the legislature, if such a case were to come before the court today, it is possible that the intent of the legislature as set forth in the new Section 9, Stock Corporation Law, will be given effect as being directly in point. On the other hand, it is possible that courts will place a limited construction on the new section, holding that though such corporate action is now possible, it is desirable that such requirements be placed in the certificate of incorporation which, after all, is a document of public record, whereas by-laws are not. This is suggested by the fact that the legislature set forth certain specific limitations to the validity of such requirements, as indicated above.

It is submitted that the new legislation will be of salutary effect. The new Section 9 will enable one or more shareholders of a close corporation, subject to certain statutory safeguards, to exercise some form of veto power over the actions of directors or shareholders. This may be accomplished by requiring either unanimity or majority vote greater than prescribed by statute, either for the taking of any action or the taking of specific action. Then, too, the legislature by a clearly formulated policy, and by an unmistakable manifestation of its intent in reference to close corporations, has probably laid to rest much of the controversial matter evoked by the decision of the *Benintendi* case.

ISADOR LIDDIE.

DISQUALIFICATION OF WITNESS AS TO TRANSACTIONS WITH DECEDENT OR LUNATIC—RECENT EXCEPTION.—In 1948 the New York Legislature further amended Section 347 of the Civil Practice Act to provide that a party to an action may testify where the other party has died, as to the facts of an accident and the results therefrom where such accident arose out of the ownership or operation of an airplane or vessel within the state.¹

Thus the disqualification of a party or of one from through or under whom the party derived his interest is relaxed once again by our legislature. It would appear, therefore, that New York is gradually adopting a more liberal attitude towards such testimony whereas previously a strict adherence to the rule of disqualification was indicated. This state of the law as exhibited by the 1948 amendment may be contrasted with the situation as it stood formerly. At early

¹ Laws of N. Y. 1948, c. 705.