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of rent thereafter accruing, that until the termination of the summary proceedings, the statutory tenant has, by reason of the emergency rent legislation, a lawful right to occupy the premises.³⁵

In the recent case of *Boynon v. Bassford*³⁶ the emergency rent regulations prevented the landlord from commencing summary proceedings for several months following the expiration date specified in the notice of termination and the court held that since "he had no choice in the matter, no conclusion as to an intent to waive the notice or renew the tenancy can be drawn from the fact that he accepted rent during those months."³⁷ Although in its reference to the absence of choice the court was probably thinking particularly of the matter of time of initiating the proceedings, the decision, is, nevertheless, sound and should be followed, but, it is submitted, on the broader ground that in a statutory tenancy the nature of the holding and the status of the landlord relative thereto make unwarranted the implication of such intent from the mere fact of the acceptance of rent.

CORPORATIONS—STOCKHOLDERS' CONTROL BY AGREEMENT

Group business enterprises are conducted under various forms: the corporation, the partnership and unincorporated business associations such as the joint stock company and the business trust. The really distinctive feature about the corporation is that it is entirely the creature of the state.¹ The other forms of business endeavor result from the common law agreement of the members even though the state may require certain acts on their part not actually affecting their being.² For certain purposes the federal and state governments and the courts may even assimilate these business groups into the category of corporations;³ yet the outstanding characteristic of the corporation is that the

35. In *Morrison v. Jacobs*, [1945] 1 K. B. 577 (C. A.), Scott, L. J., states (at 581): "The true view is that the landlord takes the rent, knowing that the tenant is granted a statutory tenancy by the Rent Restrictions Acts and that his right to gain possession of his dwelling-house depends entirely on his establishing that he brings himself within the conditions laid down by the Acts."

36. 188 Misc. 188, 67 N. Y. S. 2d 369 (App. Term 1st Dep't 1947).

37. *Id.* at 188, 67 N. Y. S. 2d at 370.

1. *People ex rel. Winchester v. Coleman*, 133 N. Y. 279, 287, 31 N. E. 96, 98 (1892). In pointing out the distinction between a joint stock association and a corporation, Judge Finch remarked: ". . . the one derives its existence from the contract of individuals, the other from the sovereignty of the state." Chief Judge Cullen, writing for the court in *Ripin v. United States Woven Label Co.*, 205 N. Y. 442, 447, 98 N. E. 855, 856 (1912), speaks of the certificate of incorporation as the instrument "by which the corporation got life." In *Benintendi v. Kenton Hotel*, 294 N. Y. 112, 121, 126, 60 N. E. 2d 829, 832, 835 ((1945) (dissenting opinion), Judge Conway conceded that "Since corporations are creatures of statute, their charters and by-laws must conform to the will of the creating power."

2. See, e.g., N. Y. GEN. ASS'NS LAW § 4; N. Y. PENAL LAW § 440-b.

3. "The term 'corporation' includes associations, joint-stock companies, and insurance

state requires it to fit into the pattern of organization and conduct which the state has decreed for its existence.

Businessmen for the most part emphasize only the practical feature of limited liability of shareholders to distinguish the corporation from other group enterprises. Yet lawyers know that the state through its legislature insists that corporations observe certain inflexible⁴ statutory requirements, an observance not demanded of unincorporated groups. One of these requirements is that the corporation be managed by its board of directors⁵ and not by the stockholders who elect the board of directors.

Why, it may be asked, should the state be any more concerned with the manner in which the corporation, as distinct from the partnership, joint stock association or business trust, conducts its business?

Those cases deciding that only the directors may perform corporate action proceed upon the theory that directors derive their original authority from the legislature through the corporate charter.⁶ Some English cases, however, proceed rather on the theory that the directors are the representatives of the incorporated body of stockholders, that the directors acquire their power from the consent of the incorporators—a consent effectuated by legislative enactment—and that the directors' powers are made exclusive (*i.e.*, of stockholders' control) by contract.⁷

companies." INT. REV. CODE § 3797 (a) (3). "The term corporations . . . shall be construed to include all associations and joint-stock companies having any of the powers or privileges of corporations not possessed by individuals or partnerships." N. Y. CONST. Art. X, § 4. See also § 37 of the New York General Construction Law. For relevant expressions by the courts see, *e.g.*, *United States v. White*, 322 U. S. 694, 701 (1944), 13 FORD. L. REV. 238; *UMW v. Coronado Co.*, 259 U. S. 344 (1922).

4. *Jackson v. Hooper*, 76 N. J. Eq. 592, 75 Atl. 568 (Ct. Err. & App. 1910); *Seitz v. Michel*, 148 Minn. 80, 181 N. W. 102 (1921); *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*, 297 N. Y. 174, 77 N. E. 2d 633 (1948); *Benintendi v. Kenton Hotel*, 294 N. Y. 112, 60 N. E. 2d 829 (1945), 45 COL. L. REV. 960; *cf. Hayden v. Beane*, 293 Mass. 347, 199 N. E. 755 (1936); *Clark v. Dodge*, 269 N. Y. 410, 199 N. E. 641 (1936); *Ripin v. United States Woven Label Co.*, 205 N. Y. 442, 98 N. E. 855 (1912).

5. 14 N. J. STAT. ANN. § 7-1 (1939); N. Y. GEN. CORP. LAW § 27. See cases cited note 14 *infra*.

6. *Jackson v. Hooper*, 76 N. J. Eq. 592, 75 Atl. 568 (Ct. Err. & App. 1910); *Hoyt v. Thompson's Ex'rs*, 19 N. Y. 207 (1859); *Dubbs v. Kramer*, 302 Pa. 455, 153 Atl. 733 (1931); *Creed v. Copps*, 103 Vt. 164, 152 Atl. 369 (1930); 2 FLETCHER, CORPORATIONS § 507 (rev. ed. 1931). This view has been strongly criticized by Professor Stevens who says that simply "because a board of directors cannot be controlled by the vote of a majority of shareholders, it does not and should not follow that therefore the board is not representative of the whole body of shareholders, and that it cannot be controlled by such decision of the shareholders as does not constitute a breach of the contract between the latter." STEVENS, CORPORATIONS 549 (1936).

7. "I do not think it true to say that the directors are agents. I think it is more nearly true to say that they are in the position of managing partners appointed to fill that post by a mutual arrangement between all the shareholders." *Automatic Self-Cleansing*

Position of the New York Courts Prior to Clark v. Dodge

New York's adherence to the first of the two theories set forth above was firmly enunciated in the early case of *Hoyt v. Thompson's Ex'rs*⁸ where Judge Comstock spoke of the powers of a board of directors as being "in a very important sense, original and undelegated. The stockholders do not confer, nor can they revoke those powers. They are derivative only in the sense of being received from the state in the act of incorporation." Despite the criticism levied against it⁹ that view has, until recently, consistently received the approval of the New York Court of Appeals.¹⁰ Whether, however, it is still accepted without qualification remains to be seen.¹¹

In *Manson v. Curtis*¹² plaintiff sued to recover damages for breach of a contract wherein the defendant, for a good consideration, had promised to vote his stock in such a way as in effect to establish the plaintiff as a one-man board of directors.¹³ The court struck down the agreement as illegal and void on the ground that "Clearly the law does not permit the stockholders to create a sterilized board of directors."¹⁴ The statutory requirement that "The business of a corporation shall be managed by its board of directors"¹⁵ had been rendered a complete nullity. The language used by the Court of Appeals in declaring the agreement invalid was strong and unequivocal: "Corporations are the creatures of the state and must comply with the exactions and regulations it imposes."¹⁶ Nevertheless, the full force of that language was considerably dissipated by the *dictum* in the very last paragraph of the opinion, *viz.*: "The rule that all the stockholders by their universal consent may do as they choose with the corporate concerns and assets, provided the interests of creditors are not affected, because they are the complete owners of the corporation, cannot be invoked here."¹⁷ Whether or not that statement was in-

Filter Syndicate Co., Ltd v. Cuninghame, [1906] 2 Ch. D. 34, 45; *cf.* Marshall's Valve Gear Co., Ltd. v. Manning, Wardle & Co., Ltd., [1909] 1 Ch. D. 267. See also MORAWETZ, PRIVATE CORPORATIONS § 511 (2d ed. 1886); STEVENS, CORPORATIONS 548-49 (1936).

8. 19 N. Y. 207, 216 (1859).

9. BALLANTINE, CORPORATIONS § 46 (rev. ed. 1946); STEVENS, CORPORATIONS 547-48 (1936).

10. See, *e.g.*, *Manson v. Curtis*, 223 N. Y. 313, 322, 119 N. E. 559, 562 (1918); *People ex rel. Manice v. Powell*, 201 N. Y. 194, 200, 94 N. E. 634, 637 (1911).

11. See notes 24, 34-38, and accompanying text.

12. 223 N. Y. 313, 119 N. E. 559 (1918).

13. In the language of the court: "The fundamental and dominant intent and purpose of the agreement was that through its fulfillment there should be vested in or continue to be vested in the plaintiff solely and exclusively, for the period named, the executive administration of the affairs of the corporation." *Id.* at 320-21, 119 N. E. at 561.

14. *Id.* at 323, 119 N. E. at 562. Authorities in accord are numerous. See, *e.g.*, *West v. Camden*, 135 U. S. 507 (1890); *Ray v. Homewood Hosp.*, 27 N. W. 2d 409 (Minn. 1947); *Hamblen v. Horwitz-Texan Theatres Co.*, 162 S. W. 2d 455 (Tex. Civ. App. 1942); *cf.* *Miller v. Vanderlip*, 285 N. Y. 116, 33 N. E. 2d 51 (1941), 54 HARV. L. REV. 1398.

15. N. Y. GEN. CORP. LAW § 27.

16. 223 N. Y. 313, 323, 119 N. E. 559, 562.

17. *Id.* at 325, 119 N. E. at 562-63.

tended to mean that the decision in that case would have been different had all the stockholders entered into the agreement can only be a matter for speculation. One thing is certain: in subsequent decisions involving unanimous agreement of stockholders the Court of Appeals has not seen fit to draw an affirmative inference from the quoted statement.¹⁸ In addition to the above quoted *dictum* the court in the *Manson* case uttered another gratuity, which served to render even more uncertain the state of the law with respect to stockholders' agreements, when it said that "Shareholders have the right to combine their interests and voting powers to secure such control of the corporation and the adoption of and adherence by it to a specific *policy* and course of business."¹⁹ Whether the New York courts will sanction an agreement which tends to bind a director's discretion as to policy is subsequently to be considered.

In *McQuade v. Stoneham*,²⁰ decided some sixteen years after the *Manson* case, a much more innocuous agreement than that invalidated in the earlier case was also declared invalid. Therein the contract between the parties provided for the election and remuneration of officers and for the adherence by the

18. Long Park, Inc. v. Trenton-New Brunswick Theatres Co., 297 N. Y. 174, 77 N. E. 2d 633 (1948); Benintendi v. Kenton Hotel, 294 N. Y. 112, 60 N. E. 2d 829 (1945); cf. Clark v. Dodge, 269 N. Y. 410, 199 N. E. 641 (1936). *But cf.* Spencer v. Lowe, 198 Fed. 961 (C. C. A. 8th 1912), 13 Col. L. Rev. 257 (1913) (although the by-laws gave to the directors the power to declare dividends, it was held that a dividend declared unanimously by the stockholders, at a meeting attended by all the directors, was valid); Groh's Sons v. Groh, 80 App. Div. 85, 80 N. Y. Supp. 438 (1st Dep't 1903) (when all the stockholders of a "family" corporation have agreed to divide profits there is a corporate act). In Kassel v. Empire Tinware Co., 178 App. Div. 176, 180, 164 N. Y. Supp. 1033, 1035 (2d Dep't 1917), the court stated that since "the parties to the action are the complete owners of the corporation, there is no reason why the exercise of the power and discretion of the directors cannot be controlled by valid agreement between themselves, provided that the interests of creditors are not affected." That language was quoted with approval by the Court of Appeals in Clark v. Dodge, 269 N. Y. 410, 416, 199 N. E. 641, 643 (1936); yet, when read in connection with another observation made by the court in the *Kassel* case with respect to the facts before it, *i.e.*, that "The rule of law which confides to the directors of a corporation the power to determine what dividends shall be declared, will not avail to confer on them the power to commit a fraud," the first quoted statement would seem to lose much of its significance. 178 App. Div. at 179, 164 N. Y. Supp. at 1035.

19. 223 N. Y. 313, 320, 119 N. E. 559, 561 (1918) (italics supplied). Judge Lehman, concurring in *McQuade v. Stoneham*, 263 N. Y. 323, 333, 335, 189 N. E. 234, 238, 239 (1934), found it "difficult to reconcile" the decision in the *McQuade* case with the "statements in the opinion in *Manson v. Curtis* that 'it is not illegal or against public policy for two or more stockholders owning the majority of the shares of stock to unite upon a course of corporate policy or action, or upon the *officers* whom they will elect,' and that 'shareholders have the right to combine their interests and voting powers to secure such control of the corporation and the adoption of and *adhesion* by it to a specific policy and course of business.'"

20. 263 N. Y. 323, 189 N. E. 234 (1934), Note, 44 YALE L. J. 873 (1935).

corporation to established policies. The Court of Appeals, without placing particular emphasis on the fact that all the shareholders were not parties to the agreement,²¹ conceded as well settled the rule that stockholders may unite to elect directors, and added: "The power to unite is, however, limited to the election of directors and is not extended to contracts whereby limitations are placed on the power of directors to manage the business of the corporation by the selection of agents at definite salaries."²² And then followed the language which would seemingly admit of no exception: ". . . a contract is illegal and void so far as it precludes the board of directors, at the risk of incurring legal liability, from changing officers, salaries or policies or retaining individuals in office, except by consent of the contracting parties."²³

Clark v. Dodge

Despite the just quoted language from *McQuade v. Stoneham* the Court of Appeals in *Clark v. Dodge*,²⁴ a decision which has undoubtedly become a landmark in the law of corporations in this state, expressly limited the *McQuade* case to its facts, disclaiming what the court now chose to term the "broad dicta" in the latter.²⁵ In the *Dodge* case plaintiff, one of the two sole stockholders of the corporation, entered into an agreement with the defendant, the other and majority stockholder, wherein the latter agreed that in return for plaintiff's divulging the formula of a secret process (known to the plaintiff alone) to the defendant's son, which plaintiff did, the defendant would (1) vote his stock so as to continue plaintiff as director, (2) continue him as general manager so long as he should prove faithful, efficient and competent, (3) see

21. See note 27 *infra*. In *Dubbs v. Kramer*, 302 Pa. 455, 153 Atl. 733 (1931), the contract between plaintiff (a director, officer and minority stockholder) and defendant (a director, officer and majority stockholder) provided that the board was to vote plaintiff a named compensation which was to continue for five years and which was not to be reduced unless the corporation became unable to pay. The court quoted and approved as correctly stating the law a portion of the opinion of the lower court in which there was included the statement that "He [a director] cannot contract to use his vote for the benefit of anyone else, or even for the benefit of the corporation." *Id.* at 457, 153 Atl. at 734.

22. 263 N. Y. 323, 329, 189 N. E. 234, 236 (1934).

23. *Id.* at 330, 189 N. E. at 237.

24. 269 N. Y. 410, 199 N. E. 641 (1936). This decision was commented upon in a number of Law Reviews. See, e.g., 36 COL. L. REV. 836 (1936) and Note, 13 N. Y. U. L. Q. REV. 585. In connection with the *Dodge* case cf. *Roberts v. San Jacinto Shipbuilders*, 198 S. W. 2d 488 (Tex. Civ. App. 1946); see *Jones v. Williams*, 139 Mo. 1, 33, 39 S. W. 486, 492 (1897).

25. Any critical appraisal of the decision in *McQuade v. Stoneham* must recognize that it was a "two-pronged" decision. Aside from its holding that the agreement therein violated Section 27 the court gave "a further reason for reversal," i.e., that the contract resulted in an employment which was itself illegal. In fact, Judge Lehman, in a concurring opinion in which Judge Crouch joined, refused to go along with the majority on the ground that the agreement violated Section 27 and based his opinion for reversal entirely on the second ground.

to it that plaintiff received one-fourth of the net income as salary or dividends and (4) see that no unreasonable salaries were paid to other officers and agents. The court granted specific performance of the agreement.²⁶ In addition to the strong equities existing in favor of the plaintiff in the *Dodge* case, there are two important differences between the agreement in it and that in the *McQuade* case. First, the agreement in the *Dodge* case was entered into by the two *sole* stockholders of the corporation, a fact not present in the *McQuade* case.²⁷ Secondly, there was in the *Dodge* case agreement no general limitation upon the power of the directors to take action in any matter which might "in any wise affect . . . rights of minority stockholders."²⁸ The quoted limitation upon the directors' discretion in the *McQuade* case, which could be waived only upon the unanimous consent of the parties to the agreement, might well be considered a most vital obstacle to the validity of the agreement in that case. No such limitation was present in the *Dodge* case; nevertheless, the court, after referring to the "statutory norm,"²⁹ asked itself this question partly by way of *dictum*: "Are we committed by the *McQuade* case to the doctrine that there may be no variation, however slight or innocuous, from the norm where salaries or *policies* or the retention of individuals in office are concerned?"³⁰ The court included in its rhetorical question the term "policies" despite the fact that the only provisions of the agreement which could in any way be deemed a limitation upon the discretion of the board were the second and third and they referred only to salaries and the retention of individuals in office,³¹ not to policies in the broad sense in which that term was apparently used in the question.

Notwithstanding the court's seemingly unqualified approval of the so-called "damage test,"³² the actual holding of the *Dodge* case would seem to be re-

26. It has been pointed out by one writer that as a practical matter specific performance should not ordinarily be granted. Meck, *Employment of Corporate Executives by Majority Stockholders*, 47 YALE L. J. 1079, 1090 n. 28 (1939). For cases denying specific performance see, e.g., *Haldeman v. Haldeman*, 176 Ky. 635, 197 S. W. 376 (1917); *Sullivan v. Parkes*, 69 App. Div. 221, 74 N. Y. Supp. 787 (1st Dep't 1902). In a recent case, however, the court decreed specific performance of a voting agreement. *Ringling v. Ringling Bros.-Barnum & Bailey Combined Shows, Inc.*, 53 A. 2d 441 (Del. Ch. 1947), 60 HARV. L. REV. 651 (1947) (see note 58 *infra*).

27. See text accompanying notes 34-38 *infra*.

28. *McQuade v. Stoneham*, 263 N. Y. 323, 326-27, 189 N. E. 234, 235 (1934).

29. N. Y. GEN. CORP. LAW § 27.

30. *Clark v. Dodge*, 269 N. Y. 410, 415, 199 N. E. 641, 642 (1936) (italics supplied). In *West v. Camden*, 135 U. S. 507 (1890), it was held that a contract with one who held the controlling interest in a company that the plaintiff should be *permanently* retained as an officer at a fixed salary was void as against public policy. *Luedke v. Olcen*, 72 N. D. 1, 4 N. W. 2d 201 (1942); see *Bond v. Graf*, 163 Ore. 264, 96 P. 2d 1091, 1093 (1939).

31. As to the "faithful, efficient and competent" requirement of the second provision, the presence of such conduct would seem to be required even in the absence of an express provision to that effect. *Fells v. Katz*, 256 N. Y. 67, 175 N. E. 516 (1931).

32. Note, 28 COL. L. REV. 366, 372 (1928), cited with approval in *Clark v. Dodge*. See also note 48 *infra*.

stricted to this: An agreement as to salaries and the retention of individuals in office entered into by *all* the stockholders of a *close* corporation, which agreement amounts to nothing more than a *slight* impingement upon the provisions of Section 27 of the General Corporation Law, will be upheld by the New York courts *if* there is "no damage suffered by or threatened to anybody."

Some More-Recent Cases

That the unnecessarily broad language in *Clark v. Dodge* prompted what would now appear to be unwarranted constructions of the decision in that case may perhaps be illustrated by a discussion of *Matter of Buckley*.³⁴ In that case it seems that less than all the stockholders passed a by-law which forbade the board of directors to remove without cause the chairman of the board or its president. Section 60 of the New York Stock Corporation Law clearly authorizes the directors to remove corporate officers without cause.³⁵ This court, taking the position that the court in the *Dodge* case had not distinguished the *McQuade* case on the ground that there was no unanimity of agreement among the stockholders in the latter case, reasoned that: "If an agreement that directors are to continue a person as officer as long as he shall be faithful, efficient and competent is legal and valid, it must follow that a by-law that directors are not to remove a person from office without cause is likewise legal and valid as an equally harmless and slight infringement upon the provisions of section 27 of the General Corporation Law and section 60 of the Stock Corporation Law. The agreement to continue the plaintiff in the *Clark* case . . . in office as long as he should be faithful, efficient and competent in effect prohibited

33. 269 N. Y. 410, 417, 199 N. E. 641, 643 (1936). *But cf.* the lower court decision in *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*, 188 Misc. 793, 66 N. Y. S. 2d 165 (Sup. Ct. 1947), and *Matter of Buckley*, 183 Misc. 189, 50 N. Y. S. 2d (Sup. Ct. 1944) (see text accompanying notes 34-38 *infra*). As to the provision in the *Dodge* case that no unreasonable salaries were to be paid to other officers and agents, that provision, had it not been expressed, would probably have been present by implication. As to the provision that defendant would vote his stock so as to continue plaintiff as director, agreements whereby stockholders pledge themselves to vote for certain persons as directors are by the clear weight of authority legal and enforceable if, without fraud, the stockholders seek to accomplish that which they might have accomplished without the agreement. *Morris v. The Broadview*, 328 Ill. App. 314, 65 N. E. 2d 605 (1946); *Brightman v. Bates*, 175 Mass. 105, 111, 55 N. E. 809, 811 (1900). In the words of Holmes, C. J., speaking for the court in the last cited case: "If stockholders want to make their power felt, they must unite." See Wormser, *The Legality of Corporate Voting Trusts and Pooling Agreements*, 18 COL. L. REV. 123 (1918). *Contra*: *Harney v. Linville Improvement Co.*, 118 N. C. 693, 24 S. E. 489 (1896); *Creed v. Copps*, 103 Vt. 164, 152 Atl. 369 (1930); see *Trumbo v. Bank of Berkeley*, 77 Cal. App. 2d 704, 709, 176 P. 2d 376, 379 (1947); *Cummins v. McCoy*, 22 Tenn. App. 681, 125 S. W. 2d 509, 513 (1938). In New York voting trusts have been expressly authorized by statute. N. Y. STOCK CORP. LAW § 50.

34. 183 Misc. 189, 50 N. Y. S. 2d 54 (Sup. Ct. 1944). See also the lower court decision in *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*, 188 Misc. 793, 66 N. Y. S. 2d 165 (Sup. Ct. 1947).

35. "The directors . . . may remove him [officer, agent or employee] at pleasure."

the directors from removing him at their pleasure and thus is legally equivalent to the by-law in the case at bar which forbids the directors from removing the Chairman of the Board without cause."³⁶

While it must be conceded that the Court of Appeals in the *Dodge* case did not *in so many words* distinguish the *McQuade* case on the ground of lack of unanimity of agreement among the stockholders in the latter, the facts remain that: (1) the court spent a considerable portion of its opinion in citing, discussing and quoting from cases wherein the stockholders' agreements had been unanimous; (2) the *dictum*³⁷ from the *Manson* case (which was cited along with the *McQuade* case for the proposition that in those cases the boards of directors had been sterilized) was quoted expressly to point out that the stockholders' agreement in the *Manson* case had not been unanimous; and (3) there *was* unanimity of agreement among the stockholders in the *Dodge* case.

It is submitted, therefore, that even if it be conceded that in the *Buckley* case the impingement upon Section 60 of the Stock Corporation Law was slight, the absence of a unanimous agreement of all the stockholders would seem to render the decision therein an unwarranted extension of *Clark v. Dodge*.³⁸

The warning that all the stockholders of a corporation, even of a close corporation, may not, in disregard of seemingly mandatory statutory requirements, determine for themselves the manner in which a corporation may be managed and directed was sounded in *Benintendi v. Kenton Hotel*.³⁹ In that case the stockholders agreed to, and later did, vote for by-laws which required that: (1) no action be taken by the stockholders except by the unanimous vote of all; (2) directors could be elected only by unanimous vote of all the shareholders; and (3) no action could be taken by the board of directors except it be the unanimous act of all.⁴⁰ The minority stockholder sued for a judgment declaring the validity of the by-laws and an injunction restraining the defendant from doing anything inconsistent with them. The majority of the Court of Appeals declared the by-laws to be invalid and denied the injunction, three judges dissenting as to the third by-law. The court, in reaching its conclusion, once again emphasized the special position occupied by corporations in our law when it said: "The State, granting to individuals the privilege of limiting their individual liabilities for business debts by forming themselves into an entity separate and distinct from the persons who own it, demands in turn that the entity take a prescribed form and conduct, pro-

36. 183 Misc. 189, 194, 50 N. Y. S. 2d 54, 58 (Sup. Ct. 1944).

37. See text accompanying note 17 *supra*.

38. *But see* Note, 23 N. Y. U. L. Q. Rev. 150, 154 (1948).

39. 294 N. Y. 112, 60 N. E. 2d 829 (1945); *cf.* *Tompkins v. Hale*, 284 N. Y. 675, 30 N. E. 2d 721 (1940); *Ripin v. United States Woven Label Co.*, 205 N. Y. 442, 98 N. E. 855 (1912). See note 42 *infra*.

40. A fourth by-law requiring unanimous action for amending the by-laws was upheld by the court.

cedurally, according to fixed rules."⁴¹ And, further on: "The State has an interest in seeing to it that such 'private laws' or by-laws as the corporation adopts are not inconsistent with the public law and not such as will turn the corporation into some other kind of entity."⁴²

The very recently decided case of *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*⁴³ presents the interesting and less common problem of the validity of an agreement entered into by *all* the stockholders of a large as distinguished from a close corporation as the latter type of corporation is traditionally understood.⁴⁴ There, a stockholder of Trenton-New Brunswick Theatres Company, a New Jersey corporation,⁴⁵ brought what eventually turned into an action to have determined the validity of an agreement entered into by all the stockholders of the latter corporation with B. F. Keith Corporation for the management of the theatres owned by Trenton. The latter corporation's 1000 shares of stock were divided into four equal classes designated A-1, A-2, B and C, respectively, each of which classes was given the sole and exclusive right to name one of the four directors. Classes A-1 and A-2 were owned by Keith, Class B by plaintiff and Class C by a third corporation. The agreement provided that for its term of nineteen years⁴⁶ the management was

41. 294 N. Y. 112, 118, 60 N. E. 2d 829, 831 (1945).

42. *Id.* at 121, 60 N. E. 2d at 832. See also *Jackson v. Hooper*, 76 N. J. Eq. 592, 599, 75 Atl. 568, 571 (Ct. Err. & App. 1910). In striking down the by-law which required unanimous stock vote for the election of directors, the court in the *Benintendi* case relied upon *Matter of Boulevard Theatre & Realty Co.*, 195 App. Div. 518, 186 N. Y. Supp. 430 (1st Dep't 1921), *aff'd without opinion*, 231 N. Y. 615, 132 N. E. 910 (1921), wherein a provision similar to the just mentioned by-law was found in the certificate of incorporation. The Appellate Division held that such a provision contravened § 55 of the Stock Corporation Law. A provision in a certificate of incorporation requiring the unanimous consent of all the stockholders in order to effect a change in the number of directors was held valid in *Ripin v. United States Woven Label Co.*, 205 N. Y. 442, 98 N. E. 855 (1912), the applicable statute being deemed permissive rather than mandatory. *Winer, Proposing A New York "Close Corporation Law,"* 28 CORN. L. Q. 313, 316 n.11 (1943), has this to say of the *Ripin* case: "The distinction between preserving the number of and the identical directors may be a substantial one. The ground in the opinion, however, that the statute says the number of directors 'may' be increased, but directors 'shall' be elected by a plurality, is not convincing, as neither thought could have been expressed the other way. See N. Y. STOCK CORPORATION LAW §§ 35, 55." Section 14 of the New York General Corporation Law provides that "Every corporation as such has power, though not specified in the law under which it is incorporated: 5. To make by-laws, *not inconsistent with law. . .*" (Italics supplied.)

43. 297 N. Y. 174, 77 N. E. 2d 633 (1948).

44. Although in the *Long Park* case the stockholders were three in number they were all corporations some of which presumably had stockholders of their own. In this Comment the discussion proceeds on the assumption that such a corporation is not a "close" corporation as that term is usually understood. ". . . when a single corporation with 1000 stockholders is the sole stockholder in a subsidiary, the latter is not a close corporation." *Winer, supra* note 42, at 315.

45. See note 50 *infra*.

46. Justice Peck, dissenting in the Appellate Division, 272 App. Div. 902, 904, 71 N. Y. S.

to be designated by the holders of the Class A-1 and Class A-2 stock unless changed as otherwise provided in the agreement. The only provision for changing the management was that the holders of a majority of the B stock and a majority of the C stock jointly could submit to the American Arbitration Association the question whether there should be a change in management.⁴⁷ In other words, the management was at all times to be designated by half the stockholders, the remaining stockholders and, most importantly, the directors, to have nothing to say about the important question of management.

The trial court entered a judgment for the defendant, basing its decision upon what it quite candidly characterized as the "dictum" in *Clark v. Dodge*.⁴⁸ The majority of the Appellate Division affirmed without opinion, Justice Peck voicing a strong and articulate dissent.⁴⁹ The Court of Appeals reversed, one judge dissenting,⁵⁰ and contented itself with distinguishing the *Dodge* case⁵¹ and holding that "the powers of the directors . . . were completely ster-

2d 369, 372 (1st Dep't 1947), speaks of the term of the agreement as follows: ". . . this is no contract for management by Keith or any other designated person for any period of time. It is a contract for designation of the management from time to time by whoever happens to be from time to time the holders of certain classes of stock—that is Keith today, but maybe someone else tomorrow, and someone else the next day—the right to designate the management running with the particular classes of stock which happen to have the privilege that year."

47. There was a further qualification that after the first change in management no other could be made within one year from the effective date of the last change in management.

48. "Public policy, the intention of the Legislature, detriment to the corporation, are phrases which in this connection mean little. Possible harm to *bona fide* purchasers of stock or to creditors or to stockholding minorities have more substance; but such harms are absent in many instances. 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.'" 188 Misc. 793, 795, 66 N. Y. S. 2d 165, 166 (Sup. Ct. 1947).

49. 272 App. Div. 902, 71 N. Y. S. 2d 369 (1st Dep't 1947).

50. Judge Fuld, although indicating that he "might" were the court "dealing with a corporation organized and operating in this State," agree with the majority that the agreement violated the statute, dissented on the ground that since the "declaration granted goes to the very heart" of the affairs of a foreign corporation the New York courts should refuse to entertain jurisdiction. This despite the fact that the applicable New Jersey statute (see note 2 *supra*) is almost identical to that of New York and, it might be added, has been at least as strictly construed.

51. In speaking of *Clark v. Dodge* the court said simply: "We think these restrictions and limitations went far beyond the agreement in *Clark v. Dodge* (269 N. Y. 410). We are not confronted with a slight impingement or innocuous variance from the statutory norm, but rather with the deprivation of all the powers of the board insofar as the selection and supervision of the management of the corporation's theatres, including the manner and policy of their operation, are concerned." 297 N. Y. 174, 179, 77 N. E. 2d 633, 635 (1948).

ilized,⁵² citing the *Benintendi*, *McQuade* and *Manson* cases. Students of corporation law and practitioners must resign themselves to a case by case development of this most important phase of the law. It seems needless to point out that generalizations from the decisions extant are to be made cautiously.

Conclusion

In corporations with many stockholders, especially where their interests may be conflicting, the statutory norm is undoubtedly a necessary one.⁵³ It furnishes protection against abuse of corporate power and control. Yet where there is unanimity among the stockholders,⁵⁴ those primarily to be protected, and the general public or creditors are not concerned, what interest has the state in insisting on the observance of the letter of the statutory mandate? *Clark v. Dodge*, which may have intimated the disinterestedness of the state on such observance, has unquestionably been limited almost strictly to its facts by the *Benintendi* and *Long Park* cases.

Will the New York Court of Appeals follow the decision in the *Dodge* case only in cases involving close corporations or will unanimous agreements of stockholders, even of large corporations, be held valid provided that there is only a "slight impingement" on Section 27 and an absence of damage to anyone? There seems to be no valid reason why the court should not, at least in such cases, disregard the artificial and highly unsatisfactory distinction which apparently continues to be drawn between close and large corporations. It seems to be time to harken to realities and to give legal recognition to the fact that contracts such as that involved in the *Long Park* case afford a practical solution for many problems of corporate management.⁵⁵

52. 297 N. Y. 174, 179, 77 N. E. 2d 633, 634-35 (1948).

53. In the words of Judge Lehman, concurring in *McQuade v. Stoneham*, 263 N. Y. 323, 333, 336, 189 N. E. 234, 238, 239 (1934), "In truth the board of directors may check the arbitrary will of those who would otherwise completely control the corporation, but cannot indefinitely thwart their will. A contract which destroys this check contravenes 'express charter or statutory provisions' and is, therefore, illegal." That the courts will be astute to protect the interests of non-assenting stockholders is well illustrated by the case of *Odman v. Oleson*, 319 Mass. 24, 64 N. E. 2d 439 (1946). Therein the contract entered into between four of the five stockholders was held invalid, the court saying (*id.* at 25, 64 N. E. 2d at 440): "There was one stockholder not a party to the contract who might be injuriously affected by it. . . . The contract was not restricted as to time. . . . The contract by its terms purported to control the conduct of some of the parties as directors, in which capacity they were in all respects fiduciaries for the corporation. . . ." See *Odell v. Wells*, 183 App. Div. 242, 247, 171 N. Y. Supp. 345, 349 (4th Dep't 1918).

54. See note 24 *supra*. In addition to the *Dodge* case see the leading Massachusetts case of *Hayden v. Beane*, 293 Mass. 347, 199 N. E. 755 (1936), discussed at length in *Meck*, *supra* note 26, at 1091-92. Cf. *Hellier v. Achorn*, 255 Mass. 273, 151 N. E. 305 (1926). See note 18 *supra*.

55. "In conclusion it should be emphasized that in the situation of the corporation with a single majority stockholder there seems to be no justification for an arbitrary rule invalidating all contracts of the type under consideration. Within the confines of that situation, the cases involving tangible injury to anyone should be handled on the basis of

There is, of course, no disputing the fact that prior adjudications in this state completely support the decision of the Court of Appeals in this most recent case. Certainly the abandonment of the entire management to persons other than directors was a clear violation of the well-established proposition that "the law does not permit the stockholders to create a sterilized board of directors,"⁵⁶ and failed to conform to the principle which upholds the validity of an agreement "though it impinges slightly upon the broad provision of Section 27."⁵⁷ In fact the agreement went even further and in a certain contingency permitted a person not even a stockholder or director, but a complete stranger, to designate the management. Even under a more liberal construction of stockholders' agreements it might well be contended that the provision for arbitration might in itself be sufficient to render the agreement invalid.⁵⁸

It must be conceded that the strict view taken towards stockholders' agreements has now become too strongly entrenched in the law of this state for one reasonably to expect any considerable change by way of decision. Legislative modification or repeal of Section 27 of the General Corporation Law seems to offer the only solution if there is to be any departure from the inflexible and unrealistic rule which now obtains.⁵⁹

their own particular facts . . . whatever the rule of law may be, the reasonable use of such contracts achieves a very practical end. As such, no doubt lawyers will continue to draw them, and if the tendency of the New York court in *Clark v. Dodge* and that of the Massachusetts court in *Hayden v. Beane* and *Mansfield v. Lang* continues to grow, it would seem that eventually such contracts will be legally acceptable everywhere." Meck, *supra* note 26, at 1098. "Besides, such agreements . . . even if regarded as open to the objection that they pledge in advance the action of officers or stockholders, may be sustained on the ground of the practical necessity that it would be impossible to organize a corporation if its proper management were not assured." *Mansfield v. Lang*, 293 Mass. 386, 391, 200 N. E. 110, 113 (1936).

56. *Manson v. Curtis*, 223 N. Y. 313, 323, 119 N. E. 559, 562 (1918). *But cf.* Meck, *supra* note 26, at 1093 n. 33.

57. *Clark v. Dodge*, 269 N. Y. 410, 415, 199 N. E. 641, 642 (1936).

58. *But cf.* *Ringling v. Ringling Bros.-Barnum & Bailey Combined Shows, Inc.*, 53 A. 2d 441 (Del. Ch. 1947), 60 HARV. L. REV. 651. Therein the court granted specific performance of a voting agreement which provided that in case the parties thereto disagreed as to how they should vote they would vote as a named arbitrator would decide.

59. Pursuant to recommendation by the Law Revision Commission (See LEG. DOC. No. 65 (K) 1948)) a new section, now before the Governor for approval, has been recommended for adoption as an amendment to the New York Stock Corporation Law. The section permits, upon compliance with certain conditions, a certificate of incorporation, as originally filed or as amended, to include provisions requiring more than the statutory majority or plurality for a quorum, vote or consent of directors or shareholders. The section will, if adopted, overrule the Court of Appeals' holding in the *Benintendi* case only with respect to the first (unanimous stockholder action) and third (unanimous director action) by-laws adopted by the parties to the action therein. The court's invalidation of the second by-law, which provided that directors could be elected only by unanimous vote of all the stockholders, would seem to remain unaffected by the proposed statute. See also Winer, *supra* note 42, at 335 *et seq.*, especially §§ 36, 37 and 39 of Mr. Winer's proposed "Close Corporation Law." (The Governor approved the bill on April 6, 1948, effective September 1, 1948. N. Y. Laws 1948, c. 862.)

TAXPAYER'S ACTION AGAINST STATE OFFICIALS TO PREVENT ALLEGED UNCONSTITUTIONAL USE OF STATE FUNDS

A recent case in New York raises again the question of the right of a taxpayer to maintain against state officials an action to restrain an alleged unconstitutional use of state funds.¹ Acting under the authority of a statute, a state board allocated state funds to a college operated by a religious corporation, for the enlargement of its facilities in order to meet problems of increased enrollment of veterans as students. Plaintiff, as a citizen and taxpayer, brought an action against members of the board, the college and the contractor employed by it. He asked for judgment declaring the projected use of state funds unconstitutional as involving a grant of public funds to a denominational educational institution and for an injunction restraining the board from paying out any funds for work done on the project. The complaint was dismissed on the ground that plaintiff had not shown sufficient interest to entitle him to maintain his action.

Seemingly well established principles have long closed the door to such actions in New York. Other states have seen the problem differently. Plaintiff urged a review of the New York position and the adoption of reasoning advanced elsewhere in support of his action.

The Basis of the New York Position

Long before the enactment of a special statute² allowing "taxpayers' actions" against municipalities, the New York courts had held that an individual taxpayer had no right to bring suit to enjoin alleged illegal expenditures of either state or municipal funds.³ The New York courts, after the enactment of the statute referred to, repeatedly held that it could not be construed as giving the taxpayer a right of action against the state or state officials.⁴ So far as such actions are concerned, the view announced long ago has been often restated, that the plaintiff must show something more than a mere status as a taxpayer or citizen "to challenge the public officers to meet him in the courts of justice to defend their official acts."⁵ He must show more than zeal for the purity of the constitution. No person or group of persons can assume to be the guardians of the community. Incumbent on the plaintiff is the duty of showing that he has an interest in the action distinguishable from one which he has in common with the general body of the state's citizens.

1. *Bull v. Stitchman*, 72 N. Y. S. 2d 488 (Sup. Ct. 1947) (Appeal now pending, Appellate Division, Fourth Department); *Bull v. Stitchman*, 72 N. Y. S. 2d 202 (Sup. Ct. 1947).

2. N. Y. GEN. MUNIC. LAW § 51.

3. *Reynolds v. Mayor of Albany*, 8 Barb. 597, 599 (N. Y. 1850); *Butler v. Kent*, 19 Johns. 223, 225 (N. Y. 1821).

4. *Goldstein v. State Commission of Correction*, 182 Misc. 695, 45 N. Y. S. 2d 476 (Sup. Ct. 1943); *New York League for Separation of Church & State v. Graves*, 170 Misc. 196, 10 N. Y. S. 2d 142 (Sup. Ct. 1939); *Schieffelin v. Komfort*, 212 N. Y. 520, 106 N. E. 675 (1914).

5. *Doolittle v. Supervisors of Broome County*, 18 N. Y. 155, 163 (1858).