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INTRODUCTION

Undivided loyalty is demanded of those who occupy a fiduciary relationship toward a corporation.[1] Thus, the directors and other officers of a corporation cannot, in any transaction in which they are under a duty to guard the interests of the corporation, acquire any personal benefit or advantage in opposition to those corporate interests.[2] The doctrine of "corporate opportunity" is the particular application of this broad, general rule.[3] It specifies that a director ". . . may not for personal gain divert unto himself the opportunities which in equity and fairness belong to his corporation."[4] Equity will impose a constructive trust on the property which is the product of such an appropriation.[5] However, not all business opportunities which may come to a director's attention will be "corporate opportunities." Those which do *not* in equity and fairness belong to the corporation are within the legitimate sphere of a director's individual business activity. The courts have been hard pressed for a rule accurately distinguishing between those opportunities which are, and those which are not, "corporate opportunities."

BROAD SCOPE OF DOCTRINE

The general rule is that directors are prohibited from acquiring any property in which the corporation has an existing right or interest, or a tangible expectancy.[6] Thus, where a director or other corporate officer purchases property in which the corporation has a leasehold interest, the courts have held that the corporate interest in or expectancy of renewing the lease is such as to make it an opportunity belonging solely to the corporation.[7] However, where the corporation has been denied renewal of the lease the expectancy is destroyed, and a director may procure it without subjecting himself to liability.[8]

Decisions limiting the obligation of loyalty to instances where the corpora-

1. Meinhard v. Salmon, 249 N.Y. 458, 464, 164 N.E. 545, 546 (1928).

2. Gilbert v. Finch, 173 N.Y. 455, 66 N.E. 133 (1903); Bosworth v. Allen, 168 N.Y. 157, 61 N.E. 163 (1901); McClure v. Law, 161 N.Y. 78, 55 N.E. 388 (1899); 3 Fletcher, Corporations § 884 (perm. ed. rev. vol. 1947); 13 Am. Jur., Corporations § 998 (1939); Ballantine, Corporations § 79 (rev. ed. 1946); Stevens, Corporations § 147 (2d ed. 1949).

3. 3 Fletcher, op. cit. supra note 2, § 861.1.

4. Litwin v. Allen, 25 N.Y.S.2d 667, 677 (Sup. Ct. 1940).

5. Equity Corp. v. Groves, 294 N.Y. 8, 60 N.E.2d 19 (1945); Beatty v. Guggenheim Exploration Co., 225 N.Y. 380, 386, 122 N.E. 378, 380 (1919); Bosworth v. Allen, 168 N.Y. 157, 61 N.E. 163 (1901).

6. Blaustein v. Pan Am. Petroleum & Transp. Co., 263 App. Div. 97, 31 N.Y.S.2d 934 (1st Dep't 1941), aff'd, 293 N.Y. 281, 56 N.E.2d 705 (1944); Litwin v. Allen, 25 N.Y.S.2d 667 (Sup. Ct. 1940); 3 Fletcher, op. cit. supra note 2, § 861.1.

7. Robinson v. Jewett, 116 N.Y. 40, 22 N.E. 224 (1889); Gildener v. Lynch, 184 Misc. 427, 54 N.Y.S.2d 823 (Sup. Ct. 1945).

8. Crittenden & Cowles Co. v. Cowles, 66 App. Div. 95, 72 N.Y. Supp. 701 (3d Dep't 1901).

tion has a right, property interest or expectancy, have been properly criticized as unduly narrow.[9] The doctrine is but a phase of the rule requiring undivided loyalty of fiduciaries. It is the violation of this duty, as revealed by the particular facts of each case, which is the basis of the doctrine. Thus in the lease cases it is the blatant disloyalty of the fiduciary, rather than the mere existence of any expectancy, which requires application of the corporate opportunity rule.

For a proper application of the general rule, the terms "right, interest or expectancy" must be broad enough to include any element which makes the particular opportunity one which in justice should belong to the corporation.[10] In *Litwin v. Allen,* Justice Shientag stated the key to a proper determination of corporate opportunity cases most succinctly—"To put it quite simply, the question to be determined is, have the directors profited at the expense of their corporation; have they gained because of disloyalty to its interests and welfare?"[11]

It is obvious then, that the outcome of each case will depend upon its own peculiar factual situation. While there can be no simple formula, certain facts and circumstances have come to be decisive.

Pre-Existing Corporate Rights or Interests

In general, a favorable business deal which comes to the attention of a corporate director is his to accept unless his company may be for some reason regarded as having a prior claim or reasonable expectancy.[12] In *News-Journal Corp. v. Gore,*[13] a director purchased a lot of real estate upon which a building leased by his corporation was situated, and also purchased a second lot used rent-free by his corporation. He thereafter increased the rental of the first lot and commenced charging rent for the second. It can readily be seen that a director who takes advantage of such an opportunity, without first offering it to his corporation, is violating his fiduciary obligations. The corporation had an existing interest in the property before the transaction was consummated. The court therefore concluded that the director held the land as trustee for the corporation.

The corporate opportunity doctrine ". . . is not satisfied by proof that after the property is appropriated it occurs that it would have been useful in the

9. Ballantine, op. cit. supra note 2, § 79, at 204-05.

10. In Litwin v. Allen, 25 N.Y.S.2d 667, 686 (Sup. Ct. 1940), Justice Shientag illustrated the broad scope of these terms stating, "This corporate right or expectancy, this mandate upon directors to act for the corporation, may arise from various circumstances; such as, for example, the fact that directors had undertaken to negotiate in the field on behalf of the corporation, or that the corporation was in need of the particular business opportunity to the knowledge of the directors, or that the business opportunity was seized and developed at the expense, and with the facilities of the corporation."

11. Ibid.

12. Ballantine, op. cit. supra note 2, § 79.

13. 147 Fla. 217, 2 So. 2d 741 (1941).

corporation's business."[14] The opportunity must be one in which the corporation clearly had an interest, such as was present in the *News-Journal* case. Nor is it sufficient to show from hindsight that it would have been a very profitable corporate undertaking. Thus in *Turner v. American Metal Co.*,[15] a corporation which dealt primarily in the basic metals was limited by directors to only 7 per cent of a venture involving a special alloy steel. The directors made personal investments and subsequently reaped large profits from the undertaking. The court, after considering the facts as they existed when the decision was made in the latter part of 1917, concluded that this was a legitimate exercise of good business judgment rather than a breach of fiduciary duty. This opportunity was, in contrast to the *News-Journal* case, speculative in nature and therefore not something to which the corporation had a true prior claim.

The fact that the opportunity is essential to the continued existence of the corporation is sufficient to give the corporation a prior claim to the opportunity. In *Averill v. Barber*,[16] the corporate opportunity doctrine was invoked against directors where a corporation was formed for the purpose of doing certain work, for which the directors had personally purchased the patent rights. The same is generally true in any case where the director's acquisition of the opportunity would substantially interfere with the corporation in effecting the purposes of its creation.[17]

Perhaps the clearest application of the rule is the case where a director acquires for himself property he was authorized to purchase for the corporation. A fairly recent federal decision, *Central Ry. Signal Co. v. Longden*,[18] illustrates this proposition. There the directors, aware of an opportunity to contract with the United States Navy, authorized the president and certain of his associates to approach the Government concerning the matter. Instead the president created a new corporation through which he, in effect, secured the contract for himself. In such a case liability to account for profits may be grounded on either the violation of his fiduciary duty,[19] or the laws of agency.[20] It is equally clear that a director may not appropriate for his own benefit a business opportunity first offered to the corporation.[21] As in the case where the director is also an agent, the pre-existing corporate interest may be found in the fact that the opportunity was intended in first instance for the corporation.

14. Blaustein v. Pan Am. Petroleum & Transp. Co., 293 N.Y. 281, 300, 56 N.E.2d 705, 713 (1944). See also Guth v. Loft, Inc., 23 Del. Ch. 255, 5 A.2d 503 (Sup. Ct. 1939); Hauben v. Morris, 281 N.Y. 652, 22 N.E.2d 482 (1939); Seymour v. Spring Forest Cemetery Ass'n, 144 N.Y. 333, 39 N.E. 365 (1895).

15. 286 App. Div. 239, 50 N.Y.S.2d 800 (1st Dep't 1944).

16. 6 N.Y. Supp. 255 (Sup. Ct., Gen. T. 1889).

17. 3 Fletcher, op. cit. supra note 2, § 861.

18. 194 F.2d 310 (7th Cir. 1952).

19. Albert A. Volk Co. v. Fleschner Bros., Inc., 60 N.Y.S.2d 244 (Sup. Ct. 1945).

20. 1 Mechem, Agency § 1224 (2d ed. 1914).

21. McClure v. Law, 161 N.Y. 78, 55 N.E. 388 (1899), reversing 20 App. Div. 459, 47 N.Y. Supp. 84 (1st Dep't 1897).

As noted, there is a tangible expectancy attending a corporate lease, and a director who obtains a renewal of the lease for himself is liable to the corporation. This same principle may be applied in a host of situations. Thus recovery will be had: (1) where directors of a railroad corporation purchase rights of way along the projected route of the railroad;[22] (2) where directors cancel a corporate contract and then obtain it for themselves;[23] or, (3) where directors purchase patent rights necessary for the corporation to operate.[24] In all these cases the action is grounded not on the presence of a legal right, interest or expectancy in the corporation, but on the breach of duty on the part of the director in acting against his corporation's best interests.

Use of Corporate Facilities

On occasion a director will use the facilities of his corporation in developing a business opportunity for his own profit.[25] It has been said that such cases are separate and distinct from, although closely related to, ordinary corporate opportunity cases.[26] Those who favor this view argue that the corporation might be totally unaware of the existence of any opportunity, and further, that it might be wholly unrelated to the corporation's business. Thus the corporation cannot be said to have any true right, interest or expectancy in the opportunity.

The better view, however, is to find the corporate interest in the fact that its funds or other facilities were used to develop the opportunity. A liberal construction of the "right, interest or expectancy" prerequisite so as to embrace this factual situation is not unwarranted. The corporation, having become involved in the venture, whether knowingly or not, due to the directors' breach of duty, should have the right to any benefits which may result from the transaction. The courts have apparently accepted this latter view. In *Guth v. Loft, Inc.*,[27] Guth, the president of Loft, Inc., purchased the formula and rights to "Pepsi-Cola" with knowledge that his corporation was in need of such a beverage. He then used the funds, credit, employees and other facilities of Loft, Inc., in order to create a new corporation capable of producing the beverage. The Delaware court said Guth was estopped from denying he had acted for the corporation and not for himself, on grounds that ". . . Guth's appropriation of the Pepsi-Cola opportunity to himself placed him in a competitive position with Loft with respect to a commodity essential to it . . . and this situation was accomplished, not openly and with his own resources, but secretly and with the money and facilities of the corporation which was committed to his protection."[28] Thus, the essential nature of the opportunity and the use of corporate facilities gave rise to the necessary cor-

22. Blake v. Buffalo Creek R.R., 56 N.Y. 485 (1874).
23. Sialkot Importing Corp. v. Berlin, 295 N.Y. 482, 68 N.E.2d 501 (1946).
24. See note 16 supra.
25. Guth v. Loft, Inc., 23 Del. Ch. 255, 5 A.2d 503 (Sup. Ct. 1939).
26. Note, 39 Colum. L. Rev. 219, 227-30 (1939).
27. 23 Del. Ch. 255, 5 A.2d 503 (Sup. Ct. 1939).
28. Id. at 281-82, 5 A.2d at 515.

porate interest. The interest or expectancy can be found in the use of corporate facilities alone, be it funds, credit, property, or even information gained[29] or influence asserted on the corporation,[30] by virtue of directorship or other office.

Purchase of Securities by Director

Not infrequently, the question of corporate opportunity has been raised in cases involving the purchase of stock by a director in his own corporation, or in a subsidiary or foreign corporation.[31] Ordinarily, there is no prohibition against a director buying securities in his own corporation.[32] In *Hauben v. Morris*,[33] the New York Appellate Division, in deciding a case of this nature, declared that directors have a right to buy shares for themselves ". . . unless the circumstances imposed upon them a 'mandate' to buy for the corporation."[34] In the *Hauben* case the court cited as authority *Bisbee v. Midland Linseed Products Co.*, where the federal court said, "No trust duty rests upon the directors . . . with respect to dealings between them in buying or selling stock in the corporation, unless some situation exists which makes it inequitable for such officer to buy the stock in question."[35] In other words, a corporate right, interest or expectancy is the "mandate" that must be found in order to impose liability upon the directors who purchase stock in their own corporations.[36]

The same would seem to apply to stock purchases in foreign corporations.[37] A director will not be denied the right to purchase securities in another corporation unless his corporation has an interest in the purchase which imposes upon the director a duty to notify his corporation of the opportunity. Such an interest would be present, for example, if the directors had been authorized to purchase the shares for the corporation, or if the stock had been first offered to the corporation, or if corporate funds had been used by the directors in making a personal purchase. Thus in the *Bisbee* case the court stated "it would undoubtedly be a breach of duty for an officer to buy stock for himself, when

29. Duane Jones Co. v. Burke, 306 N.Y. 172, 117 N.E.2d 237 (1954) (usurped customers and employees); Gast Furriers Supplies, Inc. v. Winter, 247 App. Div. 135, 286 N.Y. Supp. 749 (1st Dep't 1936) (customers from customer lists); Asphalt Constr. Co. v. Bouker, 150 App. Div. 691, 135 N.Y. Supp. 714 (1st Dep't 1912).

30. Globe Woolen Co. v. Utica Gas & Elec. Co., 224 N.Y. 483, 121 N.E. 378 (1918) (contract made under dominating influence of director).

31. Litwin v. Allen, 25 N.Y.S.2d 667 (Sup. Ct. 1940); Gallin v. National City Bank, 152 Misc. 679, 273 N.Y. Supp. 87 (Sup. Ct. 1934). See also Colorado & Utah Coal Co. v. Harris, 97 Colo. 309, 49 P.2d 429 (1935).

32. Lewin v. New York Ambassador Inc., 61 N.Y.S.2d 492 (Sup. Ct. 1946), aff'd, 271 App. Div. 927, 67 N.Y.S.2d 706 (1st Dep't 1947).

33. 255 App. Div. 35, 5 N.Y.S.2d 721 (1st Dep't 1938), aff'd, 281 N.Y. 652, 22 N.E.2d 482 (1939).

34. 255 App. Div. at 46, 5 N.Y.S.2d at 730.

35. 19 F.2d 24, 27 (8th Cir. 1927).

36. See note 10 supra. Cf. DuPont v. DuPont, 256 Fed. 129, 133 (3d Cir. 1919).

37. See note 4 supra.

he had been employed by the corporation to buy it for the corporation."[38] In the absence of such circumstances, however, a director may without fear of liability purchase shares in his own or any other corporation without first offering them to his corporation.

Other Considerations

Where a director, mindful of his potential liability, acquires the opportunity openly, the corporate opportunity doctrine may nevertheless be applied against him.[39] In considering the over-all factual situation to determine whether or not he violated his fiduciary duty, the disclosure, however, is a strong factor in his favor. More important perhaps is the fact that a recovery may be barred by laches or ratification in an open, but not in a secret transaction.[40]

Further, it is immaterial for an application of the doctrine that the corporation was not damaged by the transaction.[41] The cause of action arises when the director usurps the opportunity in violation of his duty to his corporation. The recovery is not for corporate losses suffered, but for the individual gains unjustly acquired. Thus where the wrongful preemption of a corporate opportunity is established the wrongdoer is liable to the corporation for the profits he has made.

Limitations and Exceptions

The test of a director's right to obtain a profit or benefit for himself in a given venture, is whether or not he owed a duty to the corporation inconsistent with his obtaining the advantage.[42] In the absence of such a duty a director may acquire outside interests although they are well within the scope of his corporation's business.[43] Thus, where a director seeks to enforce a valid claim against the corporation, or where the corporate business is under court supervision and thereby protected from the director's self-interest, no duty prevents the director from acting for himself.[44] A director's transactions for private profit will be equally unassailable where the corporation as a matter of business policy did not engage in the particular activity,[45] or where the opportunity had already been rejected by the management of the corporation.[46]

38. 19 F.2d at 28.

39. 3 Fletcher, op. cit. supra note 2, § 887, at 287.

40. Ibid. See Pouzzner v. Westerly Theatre Operating Co., 67 F. Supp. 874 (D.R.I. 1946), where a director secretly leased corporate property in his own name for a period of 17 years and was compelled to account for all the profits.

41. Fleishhacker v. Blum, 109 F.2d 543 (9th Cir. 1940); Guth v. Loft, Inc., 23 Del. Ch. 255, 5 A.2d 503 (Sup. Ct. 1939); Broderick v. Blanton, 59 N.Y.S.2d 136 (Sup. Ct. 1945).

42. 3 Fletcher, op. cit. supra note 2, § 885, at 283.

43. New York Automobile Co. v. Franklin, 49 Misc. 8, 97 N.Y. Supp. 731 (Sup. Ct. 1905).

44. Stevens, op. cit. supra note 2, § 147, at 671.

45. Broderick v. Blanton, 59 N.Y.S.2d 136 (Sup. Ct. 1945). See also Lancaster Loose Leaf Tobacco Co. v. Robinson, 199 Ky. 313, 250 S.W. 997 (1923).

46. Cowell v. McMillen, 177 Fed. 25 (9th Cir. 1910). The rejection would be no defense, if it was induced by fraud or misrepresentation. Kelly v. 74 & 76 W. Tremont Ave. Corp., 4 Misc. 2d 533, 151 N.Y.S.2d 900 (Sup. Ct. 1956).