Contracts by Outsiders to Influence Directors' Action

Follow this and additional works at: http://www.repository.law.indiana.edu/ilj

Part of the Business Organizations Law Commons, Contracts Commons, and the Securities Law Commons

Recommended Citation

This Note is brought to you for free and open access by the Law School Journals at Digital Repository @ Maurer Law. It has been accepted for inclusion in Indiana Law Journal by an authorized editor of Digital Repository @ Maurer Law. For more information, please contact wattn@indiana.edu.
of and the necessity for an assessment.\textsuperscript{10} Here the Georgia court did not deny the conclusiveness of the decree of the New York court, although it did fail to use the law of New York to determine the contract questions involved.\textsuperscript{11}

Thus by application of the Georgia contract law, the policy holders were held not to be members of the New York mutual insurance company\textsuperscript{12} and obviously the decree was not binding on those who were not members. The case seems justifiable, for it is highly probable that the same result would have been attained if the correct law, namely that of the domicile of the corporation, had been applied.\textsuperscript{13}

**CORPORATIONS**

**CONTRACT BY OUTSIDERS TO INFLUENCE DIRECTORS' ACTION**

Plaintiff seeks damages for breach of agreement by influential business men. The defendants for a good consideration promised to present plaintiff's name to the Board of Directors of Reo Motor Corporation and urge that he be offered a position as manager. None of the parties to the contract was alleged to be a stockholder in the corporation. It was alleged that the plan was in the best interests of the corporation and that because of defendant's breach, plaintiff was not offered a position. Held, demurrer overruled. The contract is not against public policy.\textsuperscript{1}

As alleged, the defendants possessed sufficient influence to control the directors in exercising their judgment on corporate matters. Logically, public policy toward their contracts would be the same as that governing validity of directors' contracts. As a general rule directors owe a duty to the corporation to exercise individually and at the appointed time their best and impartial judgment on behalf of the corporation.\textsuperscript{2} Stockholders likewise are not permitted to bind the directors in the exercise of this duty.\textsuperscript{3} After acknowledging such a duty, the court asserts that it is not here in question as the defendants were not directors or stockholders. The court then analogizes the contract in the principal case to those made by directors

\textsuperscript{10} Chandler v. Peketz, 297 U. S. 609 (1936); Selig v. Hamilton, 234 U. S. 652 (1914); Swing v. Humbird, 94 Minn. 1, 101 N. W. 938 (1904); Stone v. Penn Yan, K. P. & B. Ry., 197 N. Y. 279, 90 N. E. 843 (1910). However, personal defenses may be asserted, if not in the nature of a collateral attack.


\textsuperscript{12} The somewhat questionable rule employed by the court was expressed in \textit{WHARTON, CONFLICT OF LAWS} (3d ed. 1905) § 401.


\textsuperscript{1} Miller v. Vanderlip, 285 N.Y. 116, 33 N.E. (2d) 51 (1941).

\textsuperscript{2} West v. Camden, 135 U.S. 507 (1890); 6 WILLISTON, CONTRACTS (Rev. ed. 1938) §1737; 2 FLETCHER, CORPORATIONS (Perm. ed. 1931) §229.

\textsuperscript{3} McQuade v. Stoneham, 263 N.Y. 323, 189 N.E. 234 (1934), (1935) 44 YALE L.J. 873.
and stockholders, implying that it would not have been contrary to public policy if the defendants had been stockholders or directors.  

The voting trust has been expressly sanctioned in New York. But a contract to influence directors is not "an agreement among a minority in number but a majority in shares for the purpose of obtaining control of the corporation by the election of particular directors." The contract is rather an attempt to create a "passive directorate." Such contracts are not voting trusts and therefore remain invalid as against public policy.

In the case of Clark v. Dodge, the same court held that where the contract of a director is alleged to be beneficial and there is nothing on the face of the contract which might be harmful to the corporation, it is such a slight infringement of the directors' duty that public policy does not require that it be invalidated. It is to be noted, however, that this test has been openly enunciated only in cases where a small "close" or "private" corporation was involved. In such a corporation the sole owners are typically two or three stockholders who are also directors. It would seem that the courts, or preferably, the legislature should recognize this distinction and limit the test of possible harm to the corporation to such cases while retaining the stricter standard when dealing with a corporation having a large and diversified ownership as Reo Motor Corporation.

While the courts are becoming more lenient in upholding contracts made by the stockholders and directors, the contract in the principal case does not fall within either of the exceptions to the general rule discussed by the majority of the court. Therefore, the argument of Justice Lehman dissenting would seem to be the better interpretation of public policy. "A disappointed seeker of corporate office should not be allowed to recover damages...for the profits which he would have received if the men...who had influence sufficient to induce the board of directors to elect him had thereafter chosen to present and advocate a different plan for corporate action."

It would seem to be contradictory and useless to forbid directors

4 See Brightman v. Bates, 175 Mass. 105, 55 N.E. 809 (1900) (voting trust not against public policy); Clark v. Dodge, 269 N.Y. 410, 199 N.E. 641 (1936) (no injury to the corporation apparent on the face of contract therefore valid).
5 NEW YORK STOCK CORPORATION LAW §50.
6 6 WILLISTON, CONTRACTS (Rev. ed. 1938) §1736.
7 Note (1935) 44 YALE L.J. 873, 875.
9 269 N.Y. 410, 199 N.E. 641 (1936).
12 See note 4 supra.
to contract away their judgment on corporate matters and then permit a group having enough influence to control the directors to do that very thing, possibly against their better judgment. Although the plaintiff is left without remedy, public policy should discourage the formation of any such contracts by refusing to enforce them.

LABOR LAW

"LABOR DISPUTE" AND UNEMPLOYMENT COMPENSATION

Coal miners filed claims for benefits under the Kentucky Unemployment Compensation Act for a period when they did not work because of failure of mine operators and union representatives to agree on a new contract, the existing contract having expired. The Kentucky statute excluded from benefits those employees who left employment because of strike or other bona fide labor dispute. The trial court reversed the decision of the Commission and directed it to pay unemployment compensation. Held, reversed. A "labor dispute" existed within the meaning and intent of the statute.1

As the term "labor dispute" in the Kentucky Unemployment Compensation Act was not defined, the court used the definition found in the Norris-LaGuardia Act. The term "labor dispute" includes any controversy concerning terms or conditions or employment, or concerning the association or representation of persons in negotiating, fixing, maintaining, changing, or seeking to arrange terms or conditions of employment.2 An almost identical definition is found in the National Labor Relations Act.3

The Labor Relations Acts were passed for the declared purpose of encouraging the "friendly adjustments of industrial disputes" and of eliminating "forms of industrial strife and unrest" which result from the refusal of employers to accept the procedure of collective bargaining, because of obstructing interstate commerce by impairing the flow of raw materials into the channel of commerce.4 Its theory is to give free opportunity for negotiation between employer and employee which is likely to promote industrial peace and bring about agreements which the act in itself did not attempt to compel.5 The public policy of the Norris-LaGuardia Act declared it is necessary

1 Barnes v. Hall, 285 Ky. 160, 146 S.W. (2d) 929 (1940), cert. dened, 10 U.S.L. Week 3119. To the same effect see Ex parte Pesnell, 240 Ala. 457, 199 So. 726 (1941).
2 "The entire subject is in its infancy. We may, however, hope for further clarification of the meaning of the term "labor dispute" in connection with unemployment insurance legislation. The increasing number of cases involving contested rights to unemployment insurance benefits have revealed remarkable generalities in present legislation and the need for more careful terminology in the light of the many novel situations." TELLER, LABOR DISPUTES AND COLLECTIVE BARGAINING (1940) §44, p. 107.
3 47 STAT. 70, 29 U.S.C.A. §113 (c) (1932).
5 Id. at §151.
6 NLRB v. Jones & Laughlin Steel Corp. 301 U.S. 1, 45 (1937); see Jefferey-De Witt Insulator Co. v. NLRB, 91 F. (2d) 189 (C.C.A. 4th, 1937).