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CORPORATIONS-STOCKHOLDER'S DERIVATIVE SUIT-LIABILITY OF DIRRECTORS FOR ACTS IN LABOR DISPUTE

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CORPORATIONS—STOCKHOLDER'S DERIVATIVE SUIT—LIABILITY OF DIRECTORS FOR ACTS IN LABOR DISPUTE—Plaintiff, for himself and all other stockholders of *R* corporation similarly situated, brought action against the directors of the corporation, alleging that they had caused the dismantling and removal of corporate factories and the curtailment of production, that great loss to the corporation had been caused thereby, and that these things were done solely to discourage and punish the corporation's employees by removing hope of re-employment. Defendants moved to dismiss the complaint for failure to state a cause of action. The trial court denied the motion. The appellate division reversed, stating that the complaint showed only a reasonable exercise of business judgment.[1] On appeal, *held*, reversed. The alleged acts amount to actionable breaches of duty by the directors. *Abrams v. Allen*, 297 N.Y. 52, 74 N.E. (2d) 305 (1947).

The court simply states that the alleged facts may fall into one of several categories of acts for which directors may be liable, because contrary to the public policy of New York and the United States.[2] It is well established that directors may be liable for mismanagement through negligence or to serve their own interests,[3] but the 'business judgment' rule has been invoked by the courts as a bar to actions in which the stockholder merely desires the court to act as arbiter of the wisdom of the directors' acts.[4] The court's opinion may well be interpreted as meaning that in leading the corporation into a path which was opposed to the public policy of the state and nation, as expressed in their statutes, the directors risked personal liability, regardless of having exercised sound business judgment.[5] Courts have found liability without regard for good faith where a state insurance law was violated by the directors,[6] and where their acts were prohibited by a state banking law.[7] In both of these decisions, however, the statutes were designed for the protection of the stockholders and creditors of the corporation. Much the same language was used, however, in a case involving the breach by directors of a statute intended for the public

[1] Abrams v. Allen, 271 App. Div. 326, 65 N.Y.S. (2d) 421 (1946).

[2] 30 N.Y. Consol. Laws (McKinney, 1940) § 704; 29 U.S.C. (1940) § 158 (National Labor Relations Act); the Taft-Hartley Act contains language which is almost identical to this provision of the N.L.R.A.; Labor-Management Relations Act, § 8, Public Law 101, 80th Cong., 1st sess., c. 120, § 8 (1947). As a result of this same labor dispute, the corporation had been ordered to desist from its unfair labor practice in refusing to bargain collectively with its employees. N.L.R.B. v. Remington Rand, Inc., (C.C.A. 2d, 1938) 94 F. (2d) 862.

[3] STEVENS, PRIVATE CORPORATIONS, § 147 (1936); BALLANTINE, CORPORATIONS, § 63 (1946).

[4] Everett v. Phillips, 288 N.Y. 227, 43 N.E. (2d) 18 (1942), where the court said that errors of judgment do not indicate a lack of fidelity, even though so gross that they demonstrate the unfitness of the director. Helfman v. American Light & Traction Co., 121 N.J. Eq. 1, 187 A. 540 (1936); Henry v. Wellington Tel. Co., 76 Ohio App. 77, 63 N.E. (2d) 233 (1945); Rous v. Carlisle, 261 App. Div. 432, 26 N.Y.S. (2d) 197 (1941). See Carson, "Further Phases of Derivative Actions Against Directors," 29 CORN. L. Q. 431 (1944).

[5] 3 FLETCHER, CYC. CORP., § 1024 (1947).

[6] Van Schaick v. Carr, 170 Misc. 539, 10 N.Y.S. (2d) 567 (1938).

[7] Broderick v. Marcus, 152 Misc. 413, 272 N.Y.S. 455 (1934).

benefit.[8] It would be understandable that any willful breach of a statute should result in liability per se for the directors, where such a violation would result in criminal prosecution and a fine against the corporation. But where, as in the principal case, the maximum risk is a cease and desist order from a federal court, with the alternative possibility of frustrating the union's demand for higher wages, business judgment might well calculate the risk to be worth taking. Support for this view is found in another recent New York decision, where it was held that submission by the directors to an illegal exaction of money by union officers was not necessarily a ground for liability, but rather a situation for the exercise of business judgment. The court repudiated as the basis of liability the theory that the acts of the directors were contrary to public policy,[9] but one consideration of policy is probably the most rational explanation of the decision in the principal case: the court is simply anxious to discourage trifling with the legislature's labor policy,[10] even though such insubordination might be a good business risk. This decision may have important ramifications by furnishing an added weapon to stockholding union employees.[11]

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[8] Simon v. Socony-Vacuum Oil Co., 179 Misc. 202, 38 N.Y.S. (2d) 270 (1942), affirmed without opinion, 267 App. Div. 890, 47 N.Y.S. (2d) 589 (1944). The court found no liability for a violation of the Sherman Act, placing its decision largely on the ground that the directors could not reasonably have known that their acts violated the statute.

[9] Hornstein v. Paramount Pictures, Inc., (N.Y. Co. S.Ct. 1942) 37 N.Y.S. (2d) 404; affirmed, 292 N.Y. 468, 55 N.E. (2d) 740 (1944). But see also, Roth v. Robertson, 64 Misc. 343, 118 N.Y.S. 351 (1909), where liability for paying an illegal bribe was upheld on grounds of public policy.

[10] See especially 30 N.Y. Consol. Laws (McKinney, 1940) § 704, ¶ 10, designating as an unfair labor practice interfering with or coercing employees in the exercise of any of their guaranteed rights.

[11] 46 YALE L. J. 1424 (1937), discussing Pipelow v. Lindemann & Haverson Co., (Cir. Ct. of Milwaukee County, Wis., Dec. 24, 1936). The action, very similar to the principal case, unfortunately was never carried beyond the trial stage.