

New Jersey Court of Errors and Appeals.

Between

RICHARD SIEGMAN,
Complainant-Appellant,

and

ELECTRIC VEHICLE COMPANY

Defendant-Appellee.

*On Appeal from
Final Decree in
Chancery.*

BRIEF FOR APPELLEE ELECTRIC VEHICLE COMPANY.

The bill of complaint sets up a claim in favor of the Electric Vehicle Company against Rudolph H. Kissel and other former directors of that Company, amounting to \$324,800 arising out of the declaration and payment of sundry dividends in the year 1899, aggregating that amount.

The bill alleges that in August, 1901, the complainant brought suit on behalf of the Vehicle Company against its former directors to recover said dividends but failed because complainant had not previously requested the board of directors of the Company to bring the suit. It says that such a demand was made, however, in September, 1903, and that in the latter part of that year the complainant received a letter from the president of the Vehicle Company enclosing

a resolution of the board of directors refusing the demand.

The bill further declared that at the time of such refusal to sue, the directors well knew that said dividends had been unlawfully declared and paid out and that there was no valid reason why the Vehicle Company should not sue for the same, and that in refusing to sue the directors did not act or intend to act for the benefit of the Vehicle Company but were acting and intending to act for the benefit of the directors who had participated in the declaration of the unlawful dividends, and that the refusal of the directors to sue was unlawful and in violation of their duty to the corporation.

To this bill the Electric Vehicle Company filed a plea setting up that at the time the complainant's demand of September, 1903, was received, no member of the board of directors who had participated in the alleged illegal dividends was in office; that the board referred the demand to a committee for investigation and report; that the committee employed independent counsel and made a thorough investigation and reported that the claim of the complainant as to the illegality in the declaration of the dividends complained of was without substance, and that in the judgment of the committee no action should be brought by the Company or in its behalf to recover back said dividends. The committee stated that in their opinion such an action could not be maintained and that if it could it would be unfair to the directors and detrimental to the best interests of the Company.

The plea further sets up that the directors examined this report of the committee and the documents, accounts and statements showing the history and

affairs of the Company, and being satisfied from such examination that the dividends complained of were reasonably made in the light of what was known and believed at the time they were declared, that they were declared fairly and in good faith, and that it was not for the interest of the Company that suit should be brought, thereupon resolved that complainant's demand be refused *unless and until such suit shall be ordered by a majority in interest of the stockholders other than the former directors, and that unless so ordered no suit should be brought by the Company or on its behalf to recover said dividends.*

The plea further sets up that on a subsequent request by the complainant the directors called a meeting of the stockholders and submitted to them the question of whether or not the suit should be brought; that at said stockholders' meeting the stock of the former directors was excluded from voting and that of the stock actually voted 124,759 shares were voted against bringing suit while only 650 shares (or about one-half of one per cent) were voted in favor of it.

To this plea the Vehicle Company annexed an answer specifically denying the charges of fraud, collusion and bad faith contained in the bill.

The complainant has filed no replication to this plea and answer but has elected to go to hearing upon a record which admits the truth of all the facts which are properly pleaded as well those contained in the plea as those found in the answer.

Gaskill v. Sine, 2 Beas. 130.

Davison's Executors v. Johnson, 1 C. E. Gr. 112.

Bogardus v. Trinity Church, 4 Paige, 178.

Beach on Modern Equity Practice, Vol. 1, Sections 298, 326.

The question, therefore, is whether or not taking the plea and answer to be true, the complainant has a right to prosecute this suit.

That he has no such right without showing a demand upon and a wrongful refusal by the Company to bring the suit, is familiar law and has already been decided in a suit between some of the same parties in the Court of Errors and Appeals.

Siegman v. Maloney, 20 Dick. 372.

The complainant has now shown a demand and refusal and this leaves only the question remaining whether or not the refusal was wrongful. It cannot be said to be wrongful because done in bad faith inasmuch as the charge that it was so done, contained in the bill, is explicitly denied in both plea and answer, and as shown above, such denial takes this allegation out of the case. Does, then, the mere allegation that a cause of action exists and that the corporation refuses to bring it entitle the complainant stockholder to sue? Or rather, is it a good answer to a demand upon the corporation to sue, that the directors have investigated the claim and found it to be without foundation and one that it would be prejudicial to the Company to attempt to enforce?

It will be observed that no question of *ultra vires* arises with respect either to the original act of declaring dividends or to the act of the present directors in refusing to sue.

The declaration of dividends is within the power of business corporations. Indeed it may be said to be the principal end of their existence. It is true that dividends are not to be declared except out of net earnings or surplus but it is for the directors to determine whether such net earnings or surplus exists, and

if in making such determination they reach a wrong conclusion, either innocently or fraudulently, their act cannot be said to be *ultra vires*.

But if the declaration of unearned dividends could be said to be *ultra vires*, that mere fact would not make it the duty of the corporation to bring the action demanded by the complainant in September, 1903. While an *ultra vires* act cannot be ratified, and while a single stockholder may, upon the refusal of the corporation to act, be heard on an application to enjoin it or set it aside, no such request was made here, for what the complainant in this case demanded was not the refusal to pay an illegal dividend or the failure of a bill to set the declaration of the same aside and recover back the money from the stockholders to whom it was paid, but an action for damages sustained by the corporation on account of such declaration. Such a demand, therefore, presented only the ordinary questions of right and expediency which arise in every case where action is contemplated for the recovery of damages for an injury sustained.

As to the action of the present board in refusing to bring suit, of course no question of *ultra vires* arises since the bringing of actions to redress injuries to the corporation is a part of the internal management of corporations and is peculiarly the province of the directors.

Must, then, a corporation bring suit to recover damages alleged by a stockholder to have been sustained by it notwithstanding the directors, after a fair, full and honest investigation, conclude that the action will not lie and that if it would lie it would not be expedient to bring it? Or rather we should say, must a corporation bring such a suit upon such a de-

mand after such an investigation and conclusion and after, at the request of the stockholder, it has submitted to the whole body of stockholders the question of whether or not the suit shall be brought and 99½ per cent. of the stockholders have voted that it should not be brought? To answer this question in the affirmative would be to declare that the judgment of the chosen directors of the corporation may at any time be dethroned by a single stockholder with regard to any question of business policy and the will or whim of a single stockholder substituted in its place; for if a single stockholder may overrule the judgment of the directors, although concurred in by nearly all the stockholders with respect to bringing suits for damages against A, B, C or D, against whom such stockholder may happen to think a cause of action exists, why may he not enjoin the making of any particular contract by the corporation although similarly concurred in if he thinks it inimical to the best interests of the corporation? Or why may he not file a bill to set aside any and every contract made by his corporation upon the ground that it was not to the interests of the corporation that it should be made, although the directors and all his fellow stockholders have approved it and do approve it?

It is respectfully submitted that there is no authority in the world for such a proposition; that the action of corporate directors in refusing to bring suit to enforce alleged claims of the corporation is binding upon all the stockholders except in case of fraud, and that independent of the denials of fraud in this case, the resolution passed by the directors is, on the face of it, conclusive of their good faith, as it contained an offer to bring the suit if the stockholders

voted to do it, and an offer to call the stockholders together for that purpose whenever the complainant should request them. For the complainant, after accepting this offer and submitting his plea to the stockholders, to now claim that the stockholders and directors acted fraudulently simply because they disagreed with him, is too preposterous to receive serious consideration. That the directors fully and patiently investigated every item of the complainant's claim is shown by the report of their committee and by the recitals of the resolution which they adopted on the coming in of such report. That they erred in judgment in concluding that the dividends were earned and properly paid may be the case. Whether they did or not is of no account on the present inquiry as no appeal lies to any court from the judgment of a board of directors honestly reached on such a question. The only appeal is to the stockholders to elect a different board.

But even if the directors had concluded that the dividends, or some of them, were improperly declared they may well have thought, as their resolution states, that it was not for the interest of the Company that suit should be brought. The report of the committee states that the Company was then doing a prosperous and steadily increasing business, and it is not difficult to understand the action of the directors and the great body of the stockholders in accepting the view of the committee that the true interests of the Company lay in the prosecution and development of that business rather than in the prosecution of a law suit, which all of them thought would be likely to do the Company more harm than good.

It is apparent that a judicial inquiry into the-

question as to whether or not the dividends paid in 1899 had been really earned, would involve an exposure of the Company's business to an extent and in a manner which might injure its credit and check its present prosperity and in that way injure it to a greater extent than the recovery of the \$324,800 which the complainant demanded could benefit it. The conclusion of the directors on this point was the determination of a question of policy, of corporate management, peculiarly committed to them, and with respect to which their determination bound every stockholder.

And to this effect are all the authorities.

TEXT BOOKS.

In *Clark and Marshall on Corporations*, at Section 544, it is said:

"The doctrine that a stockholder may sue in equity to redress or prevent wrongs on the part of the directors or majority of the stockholders, or to obtain redress on behalf of the corporation for injuries by strangers, where he cannot obtain relief through the corporation, does not give a stockholder the right to maintain such a bill where the act complained of, or the refusal of the directors or majority of the stockholders to sue, is properly within the discretionary power with respect to the internal affairs of the corporation, vested in them by charter. So long as they act, not fraudulently, illegally or oppressively, but in good faith, in the exercise of their discretion, and for what they deem to be the best interests of the company, a court of equity has no jurisdiction to interfere at the suit of a dissenting stockholder, or a dissenting minority of the stockholders. Such a suit cannot be maintained

by showing a mere mistake or error of judgment on the part of the directors or majority of the stockholders. Their conduct must be *ultra vires*, illegal, fraudulent, or oppressive."

At section 544 (c) of the same work, it is said:

"The mere fact that a corporation has a cause of action for an injury does not always make it incumbent upon it to sue, any more than in the case of an individual. If, in the opinion of the directors or a majority of the stockholders, the best interests of the company do not require it to sue, it need not do so. The matter is within their discretion, and if they act in good faith, their refusal to sue violates no right of dissenting stockholders, so as to entitle them to maintain a suit in their own behalf."

In *Morawetz on Corporations*, Section 2441, it is said:

"It is often a matter involving the exercise of much judgment, whether or not it be expedient, in a given case, to begin a litigation on account of an actionable injury. It is not the duty of the managing agents of a corporation to go to law immediately, whenever a wrong has been done to the corporation. The advisability of suing for redress, and the time and manner of proceeding, are largely intrusted to their judgment; and it is their duty to give the corporation the benefit of their best judgment in this respect. The refusal of the agents of a corporation to institute proceedings on its behalf, even when requested by its shareholders, may possibly be a judicious exercise of the discretion which was conferred upon them by the charter. The discretionary power confided to the agents of a corporation cannot be usurped by its shareholders; and therefore the courts will not interfere at the suit of a shareholder to redress an injury suffered by the corporation, merely because its managing

agents have in good faith refused to begin a suit in the name of the corporation."

In *Cook on Stock and Stockholders*, at Sec. 750, it is said:

"The discretion of the directors in refusing to institute or to defend an action involving corporate interests is not generally interfered with. It frequently happens that the corporation has a cause of action against a third party which the directors think best not to press, or that the corporation is sued and the directors think best not to defend, or, where an action is pending, the directors decide to compromise the matter. The judgment of the directors may, in the opinion of a stockholder, be erroneous, and yet it cannot be controlled or changed by the stockholders except by refusing to re-elect the directors to office. The stockholder cannot go into court and attempt to change the policy of the directors as regards the management of the suit. In general a corporation represents and binds the shareholders in bringing and defending suits which involve the rights and obligations of the corporation, and binds them as fully as in the making of contracts."

In *Taylor on Corporations*, at Sec. 140, it is said:

"It must be shown in the complaint that the refusal of the directors is a breach of trust on their part, and not a mere error of judgment in a matter properly within their discretion."

To the same effect is *Thompson on Corporations*, Vol. 4, Sec. 4487.

ENGLISH CASES.

In *Lord v. Copper Mining Co.*, 2 Phillips, 740, Lord Cottenham said:

"I find all the complaints made by the indi-

vidual shareholders to consist of acts within the powers of the corporation, and all sanctioned by general meetings of shareholders, and no allegation raising any case for the interference of a court of equity. A court of equity could not assume jurisdiction without opening its doors to all parties interested in corporations, who, although a small minority, may wish to interfere in the conduct of the majority."

In *McDougall v. Gardiner*, 1 Chan, Div. 14, James, L. J., said:

"Nothing connected with internal disputes between the shareholders is to be made subject of a bill by one shareholder, unless there is something illegal, oppressive, or fraudulent, and unless there is something *ultra vires* on the part of the company, or on the part of the majority, so that they are not fit persons to determine it; but that every litigation must be in the name of the company, if the company really desire it; because there may be a great many wrongs committed in a company; there may be claims against directors; there may be claims against officers; there may be claims against debtors; there may be a great variety of things which the Company may be well entitled to complain of, but which, as a matter of good sense, they do not think it right to make a subject of litigation."

In *Burland v. Earle*, Law Rep., App. Cas., 1902, p. 83, the Court said at p. 93:

"It is an elementary principle of the law relating to joint stock companies, that the court will not interfere with the internal management of companies acting within their powers and in fact has no jurisdiction to do so. Again, it is clear law that in order to redress a wrong done to the Company or to recover money or damages alleged to be due to the company, the action

should *prima facie* be brought by the company itself. These cardinal principles are laid down in the well known cases of *Foss v. Harbottle* and *Mosley v. Alston*, and in numerous later cases which it is unnecessary to cite. But an exception is made to the second rule where the persons against whom the relief is sought, themselves hold and control a majority of the shares in the Company, and do not permit action to be brought in the name of the company. In that case the courts allow the shareholders complaining to bring an action in their own names. This, however, is mere matter of procedure in order to give a remedy for a wrong which would otherwise escape redress, and it is obvious that in such an action the plaintiffs cannot have a larger right to relief than the Company itself would have if it were plaintiff, and cannot complain of acts which are valid if approved by a majority of the shareholders, or are capable of being confirmed by a majority. The cases in which the minority can maintain such an action are, therefore, confined to those in which the acts complained of are of a fraudulent character, or beyond the powers of the Company."

AMERICAN STATE CASES.

In *Benedict v. Columbus Construction Company*, 4 Dick. 23, 36, Chancellor McGill said:

"If stockholders in a corporation disapprove of the company's management, which is conducted without fraud, or by action *ultra vires*, or in gross abuse of trust, or shall consider their speculation a bad one, their remedy is to elect new officers or sell their shares and withdraw. Where the question is one of mere discretion in the management of corporate business by directors, or of doubtful event in the undertaking in which the corporation

has embarked, remedy cannot be had by application to a court of equity."

In *Ellerman v. Chicago Junction Railways Co.*, 4 Dick. 217, Vice Chancellor Green said:

"Individual stockholders cannot question in judicial proceedings, the corporate acts of directors, if the same are within the powers of the corporation and in furtherance of its purposes, are not unlawful or against good morals and are done in good faith and in the exercise of an honest judgment. Questions of policy of management, of expediency of contracts or actions, of adequacy of consideration not grossly disproportionate, of lawful appropriation of corporate funds to advance corporate interests, are left solely to the honest decision of the directors if their powers are without limitation and free from restraint. To hold otherwise would be to substitute the judgment and discretion of others in the place of those determined on by the scheme of incorporation."

In *Edison v. Edison United Phonograph Co.*, 7 Dick. 620, Vice Chancellor Van Fleet said:

"No rule of law is better settled than that which declares that, so long as the directors of a corporation keep within the scope of their powers and act in good faith and with honest motives, their acts are not subject to judicial control or revision. Perhaps no better statement of this principle can be found than that which Vice Chancellor Green made in *Ellerman v. Chicago Junction Co.*, 4 Dick. Ch. Rep. 217, 232."

The rule announced in these cases was approved by the New Jersey Court of Errors and Appeals in

Berger v. United States Steel Corporation, 18 Dick. 829.

Hodge v. United States Steel Corporation, 19 Dick. 817.

In *Rathbone v. Parkersburg Gas Co.*, (Sup. Ct. W. Va., 1888) 8 S. E. Rep. 570, it is said:

“Ordinarily the directors of a corporation have complete power to control its action, and to decide whether it shall enter into litigation or not. The shareholder, therefore, cannot obtain the interposition of the courts without showing that the directors are either unwilling or unable to bring suit on behalf of the corporation. And, even where the directors or the ordinary managing officers are at fault, it does not necessarily follow that the corporation is disabled from procuring justice for itself; for the majority of the shareholders in corporate meeting have supreme authority under the charter to manage the corporate affairs, whenever it is possible to obtain justice by calling a meeting of the shareholders and removing the offending officers and electing new ones, this remedy must be pursued. In such case a shareholder cannot sue in equity, since the ground for relief fails, namely, that the corporation, his trustee, is unable to protect the trust. *Hawes v. Oakland*, 104 U. S. 450, 460. The managing agents of an ordinary private corporation are invested with wide discretionary powers. It is often a matter involving the exercise of much judgment whether or not it is expedient in a given case, to begin litigation on account of an actionable injury. It is not always the duty of the managing agents of a corporation to go to law immediately, whenever a wrong has been done to the corporation. The advisability of suing for redress, and the time and manner of proceeding are largely intrusted to their judgment; and it is their duty to give the corporation the benefit of their best judgment in this respect. The refusal of the agents to institute legal proceedings on behalf of the corporation even when requested by its shareholders, may possibly be a

judicious exercise of the discretion conferred upon them. This discretionary power confided to the agents cannot be usurped by the shareholders, and therefore the courts will not interfere at the suit of a shareholder to redress an injury suffered by the corporation, merely because its managing agents have in good faith refused to begin a suit. In order to entitle a shareholder to sue he must show, either that the managing agents are themselves the authors of the wrong, or that their refusal to bring suit in the name of the corporation is an act of bad faith, or an abuse of the discretionary power vested in them. Even this rule is subject to this qualification: The directors and agents of the corporation are inferior to and under the control of a majority of the shareholders. Consequently, when the directors refuse to discharge their duty, they may be removed or controlled by a majority of the shareholders. Thus, in order to confer upon a shareholder the right to sue, in a case in which the primary right is in the corporation, he must not only show that the directors are in default or wrongfully refuse to sue, but he must show that a majority of the shareholders have been appealed to, and that they are also guilty of misconduct, or willfully and wrongfully refuse to act in the matter."

In *Gamble v. Q. C. W. Co.*, 123 N. Y. 91, the court said:

"To warrant the interposition of the court in favor of the minority shareholders in a corporation or joint stock association as against the contemplated action of the majority, where such action is within the corporate powers, a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influ-

enced by any honest desire to secure such interests, but that he must have acted with an intent to subserve some outside purpose regardless of the consequences to the company, and in a manner inconsistent with its interests."

In *Leslie v. Lorillard*, 110 N. Y. 519, it is said:

"In actions by stockholders which assail the acts of their directors or trustees, courts will not interfere unless the powers have been illegally or unconscientiously executed, or unless it be made to appear that the acts were fraudulent or collusive and destructive of the rights of the stockholders. Mere errors of judgment are not sufficient as grounds for equity interference, for the powers of those entrusted with corporate management are largely discretionary."

In *Dudley v. Kentucky High School*, 9 Bush, 576, it is said:

"Each and every stockholder contracts that the will of the majority shall govern in all matters coming within the limits of the act of incorporation, and in cases involving no breach of trust but only error or mistake of judgment upon the part of the directors who represent the company, individual stockholders have no right to appeal to the courts to dictate the line of policy to be pursued by the corporation."

In *Dunphy v. Travellers Newspaper Assn.*, 146 Mass. 495, it is said:

"It would be contrary to the fundamental principals of corporate organization to hold that a single shareholder can at any time launch the corporation into litigation to obtain from another what he deems to be due to it, or to prevent methods of management which he thinks unwise. Intelligent and honest men differ upon questions of a business policy. It is not always best to in-

sist upon all one's rights; and a corporation acting by its directors or by vote of its members may properly refuse to bring a suit which one of its stockholders believes should be prosecuted. In such a case the will of the majority must control."

UNITED STATES COURT CASES.

Dodge v. Woolsey, 18 How. 331, is the oldest case in the Supreme Court bearing upon the question now under consideration, and it is usually relied upon to support such actions as the present. We submit, however, that it does not do so.

It appeared in the *Dodge* case that in 1845 an act had been passed by the Legislature of Ohio to incorporate the Ohio State Bank and other banking companies, and that the Commercial Bank of Cleveland was a corporation, being a branch of the State Bank of Ohio. The act of incorporation stated that the bank should semi-annually pay to the state six per cent. of its net profits, which should be in lieu of all taxation to which the banking company or its stockholders might otherwise be subject. It also appeared that the banking company semi-annually had complied with the requirement of its charter in respect to taxation; that on the first of September, 1851, a new constitution had been adopted in Ohio which provided that the Legislature should pass laws taxing by uniform rule all moneys, credits, investments, etc., and should provide for taxing the notes and bills discounted, or purchased, money loaned and all other property, effects or dues whatever without distinction, of all existing banks and banks to be thereafter created, and of all bankers so that all property

employed in banking should always bear a burden of taxation equal to that imposed on the property of individuals. It was further provided in the new constitution that the property of corporations then existing, or thereafter created, should be subject to taxation as the property of individuals.

It further appeared that in the year 1852 the Legislature of Ohio had passed an act designed to carry out the direction of the constitution in respect to taxation of the stock and assets of banks and apparently provided a severe penalty in case of failure of officers of the banks to make the proper returns in order that the taxing act might be completely administered.

It also appeared that the president and cashier of the Commercial Bank "fearing the penalty imposed by the act for a refusal or neglect to make a return according to the act, did in the month of May, 1852, make a return protesting against the right of the state to assess taxes on the bank other than that which was provided for in the charter of its incorporation on the 24th of February, 1845." In pursuance of that return a tax had been imposed upon the stock of the bank for ten thousand one hundred and ninety-seven dollars and fifty-five cents, exceeding by seven thousand five hundred and twenty-six dollars and seventy-two cents, the amount of taxes for which the bank was liable under its charter. It was also shown by the bill that there had been another entry of taxation against the bank for the year 1853 of more than fourteen thousand seven hundred dollars, which was also largely in excess of the taxation to which the bank was liable under its charter. Pages 338, 339.

Woolsey, a resident of Connecticut and a holder of stock of the bank, had, by his attorney, addressed a

letter to the bank requesting it "to institute proper proceedings to prevent the collection of the taxes by Dodge (the tax collector) in the same manner as had been done by the attorney of a stockholder in the Canal Bank of Cleveland" for a tax assessed under the same act and that the action of the board of directors of the Commercial Bank, in answer to Woolsey's application, was the same as had been given by the directors of the Canal Bank. Their resolution was as follows:

"Resolved that we fully concur in the views expressed in said letter as to the illegality of the tax therein named, and believe it to be in no way binding on the bank; but in consideration of the many obstacles in the way of testing the law in the courts of the state we cannot consent to take the action which we are called upon to take, but must leave the said Klemens (probably a stockholder in the Canal Bank) to pursue such measures as he may deem best in the premises." p. 340.

The court, in characterizing the action of the directors in refusing to bring the suit, said:

"That they refused to do so, accompanying, however, their refusal with the declaration that they fully concurred with Woolsey in his views as to the illegality of the tax; that they believed it to be in no way binding upon the bank, but that in consideration of the many obstacles in the way of resisting the collection of the tax in the courts of the state, they could not consent to take legal measures for testing it. Besides this refusal the papers in the case disclosed the fact that the directors had previously made two protests against the imposition of the tax because it was repugnant to the constitution of the United States, and to that of Ohio also, both concluding with a resolution that they would not, as then

assessed, pay the taxes unless compelled by law to do so, and that they were determined to rely upon the constitutional and legal rights of the bank under its charter." p. 345.

The opinion thereupon proceeds:

"Now, in our view the refusal on the part of the directors, by their own showing, partakes more of a disregard of duty than an error of judgment. It was a non-performance of a confessed official obligation, amounting to what the law considers a breach of trust, though it may not involve intentional moral delinquency. It was a mistake, it is true, of what their duty required from them according to their own sense of it, but, being a duty by their own confession, their refusal was an act outside of the obligation which the charter imposed upon them to protect what they conscientiously believed to be the franchise of the bank. A sense of duty and their conduct contrary to it is not an error of judgment merely and cannot be so called in any case. It amounted to an illegal application of the profits due to the stockholders of the bank, into which a court of equity will enquire to prevent it being made. Thinking, as we do, that the action of the board of directors was not 'an error of judgment merely,' but a breach of duty, it is our opinion that they were properly made parties to the bill and that the jurisdiction of a court of equity reaches such a case and gives such a remedy as the circumstances may require." p. 345.

It is clear, therefore, that in the case of *Dodge v. Woolsey*, the directors willfully refused to exercise a duty which they fully recognized and appreciated.

In considering the right of *Woolsey* to bring the suit, the court said, at page 343:

"The result of the cases is well stated in *Angell and Ames*, paragraphs 391-393: 'In cases where

the legal remedy against a corporation is inadequate, a court of equity will interfere, is well settled and there are cases in which a bill of equity will lie against a corporation by one of its members. * * * Though the result of the authorities clearly is that in a corporation, when acting within the scope of and in obedience to the provisions of its constitution, the will of a majority, duly expressed at a legally constituted meeting, must govern; yet beyond the limits of the act of incorporation, the will of the majority cannot make an act valid, and the powers of a court of equity may be put in motion at the instance of a single shareholder, if he can show that the corporation are employing their statutory powers for the accomplishment of purposes not within the scope of their constitution. Yet it is to be observed that there is an important distinction between this class of cases and those in which there is no breach of trust, but only error and misapprehension, or simple negligence on the part of the directors."

This case of *Dodge v. Woolsey* was carefully examined in the subsequent cases of *Hawes v. Oakland*, 104 U. S. 450, decided in 1881, see pages 457-460, and its application restricted. The court said, p. 460,

"The examination of *Dodge v. Woolsey* satisfies us that it does not establish, nor was it intended to establish a doctrine on this subject different in any material respect from that found in cases in the English and other American courts, and that the recent legislation of Congress referred to leaves no reason for any expansion of the rule in that case beyond its fair interpretation.

"We understand that doctrine to be that to enable a stockholder in a corporation to sustain in a court of equity, in his own name, suit

founded on a right of action existing in the corporation itself, and in which the corporation itself is the appropriate plaintiff, there must exist as the foundation of the suit, some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred upon it by their charter or other source of organization;

“Or such a fraudulent transaction completed or contemplated by the acting managers in connection with some other party or among themselves, or with other shareholders as will result in serious injury to the corporation or to the interests of the other shareholders;

“Or when a board of directors, or a majority of them, are acting for their own interests in a manner destructive of the corporation itself or toward the right of other shareholders;

“Or when the majority of shareholders themselves are oppressively and illegally pursuing a course in the name of the corporation which is in violation of the rights of other shareholders, and which can only be restrained by the aid of a court of equity.”

It will be observed that the present case does not come within any of the subdivisions of the rule as stated above.

The rule as declared in *Hawes v. Oakland* was reiterated and applied in *Corbus v. Alaska Treadwell Gold Mining Co.* (1902) 187 U. S. 455. This was a case in some respects like *Dodge v. Woolsey*. The stockholder brought an action in equity to restrain his corporation from the payment of an Alaskan license tax. The bill of complaint was evidently framed on the complaint in *Dodge v. Woolsey*, setting up a request to the officers and agents of the company to refrain from paying the tax, that such agents doubted

the constitutionality of the law imposing the same but from fear of incurring the pains and penalties imposed for the omission to pay the tax, refused the stockholder's request. On demurrer the bill was dismissed and the stockholder appealed. The court, after quoting from *Hawes v. Oakland* as to the cases in which a stockholder might sue in the right of the corporation, proceeded as follows:

"But, in addition to the existence of grievances which call for this kind of relief, it is equally important that, before the shareholder is permitted in his own name to institute and conduct a litigation which usually belongs to the corporation, he should show to the satisfaction of the court that he has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances, or action in conformity to his wishes. He must make an earnest, not a stimulated, effort, with the managing body of the corporation, to induce remedial action on their part, and this must be made apparent to the court. If time permits, or has permitted, he must show, if he fails with the directors, that he has made an honest effort to obtain action by the stockholders as a body, in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it.

" * * * * * The directors represent all the stockholders, and are presumed to act honestly and according to their best judgment for the interests of all. Their judgment as to any matter lawfully confided to their discretion may not lightly be challenged by any stockholder or at his instance submitted for review to a court of equity. The directors may sometimes properly waive a legal right vested in the corporation in the belief

that its best interests will be promoted by not insisting on such right. They may regard the expense of enforcing the right or the furtherance of the general business of the corporation in determining whether to waive or insist upon the right. And a court of equity may not be called upon at the appeal of any single stockholder to compel the directors or the corporation to enforce every right which it may possess, irrespective of other considerations. It is not a trifling thing for a stockholder to attempt to coerce the directors of a corporation to an act which their judgment does not approve, or to substitute his judgment for theirs. As said in *Dodge v. Woolsey*, 18 How. 344, 15, L. ed. 406: 'The circumstances of each case must determine the jurisdiction of a court of equity to give the relief sought.' "

The court made in this case the point which is significant in the present case, that it did not appear from the bill that any other stockholder shares with the plaintiff his belief in the illegality of the tax or objected to its payment by the corporation.

In *Kessler & Co. v. Ensley*, 129, the Circuit Court for Alabama said:

"While the mere refusal of the governing body of a corporation to bring suit to redress a fraud committed against it is not a ratification of such fraud, and does not in itself constitute a fraud against the corporation, yet where the refusal is from proper motives, and in the interest of the corporation, it is neither illegal nor immoral, it being the duty of such body in general to act for pecuniary interest of the corporation; and where its action has been fairly approved by a disinterested majority of the stockholders it is binding on the minority, who cannot, in such case, maintain in their own name, on behalf of the corporation, the suit which the majority have deter-

mined to be against its interest as to a purely *intra vires* matter."

Applying the rule laid down in these various cases to the present situation, it is to be noted that, although the dividends in question were declared and paid in 1899, no stockholder, except the complainant, has up to this time demanded that suit should be brought to recover the same, and, although the complainant brought his first suit in 1901 and his second suit in August, 1904, no other stockholder has joined him up to the present time, although in both bills he invited all other stockholders to do so.

It may well be said, therefore, as Justice Brewer said in the *Corbus* case, that it does not appear that any other stockholder shares with the complainant his opinion that the dividends were illegally declared, or at least his opinion that the present directors had wrongfully refused to commence an action for their recovery.

It is also to be noted that several annual elections of directors have been held since the complainant discovered that the corporation was not disposed to bring suit to recover the alleged illegal dividends, and that he has either not attempted to procure the election of a board who would bring such suits, or, if he has so attempted, he has failed in the attempt.

It is likewise to be noted that the directors disclosed to the complainant a willingness to bring the suit if a majority of the stockholders should so direct, and that they offered to call the stockholders together to pass upon the question if the complainant or any other stockholder should so request; that the complainant, after taking three months for reflection, made the request and that at the meeting of stockholders so called

together the complainant was present by his attorney, and after full consideration over 99 per cent. of the stockholders voted that the action should not be brought.

The foregoing argument was presented to the learned Vice Chancellor who advised the decree appealed from in this case and was rejected by him for the reasons given in his opinion printed on page 30 of the case. We submit that he has altogether failed to meet the argument. He says that the bill shows a clear cause of action against the defendant Kissel for \$324,000 and that all the plea sets up in excuse or justification for not bringing suit is "that the present directors and a large number of the stockholders now think that no just ground exists therefor and that it is not for the interest of the company to prosecute; in other words, admitting that, under the statute, Kissel is liable to refund the money, it is not thought fair to him or expedient for the company to enforce the liability." And again he says: "We must, as the pleadings stand, regard the right of recovery against Kissel to be clear for, as I have said, it is expressly averred in the bill that he knew that the dividends were all paid out of capital, and notwithstanding this knowledge voted for their payment. This makes a perfectly clear case against him, however the matter may stand as to the others. The fact that a committee of the directors may have thought that as to the liability of the directors generally in office when the dividends were declared there might be some doubt or question is immaterial; for taking the facts to be as alleged by the bill, and not denied by the plea, this doubt does not extend to Kissel. Then, the only other ground assigned for not suing is found in the bare statement

that suit is inexpedient. But if the circumstances of each case are to determine the question of jurisdiction, then, the right being clear, it ought to appear why it is inexpedient. If Kissel be solvent (and there is no intimation of insolvency), and if the right to recover so large a sum (\$324,000) be undoubted, some good reason should be given for not suing. But no reason whatever is given."

We submit that this reasoning totally misapprehends the language, office and effect of the plea. With all due respect we insist that it is a perversion of the plea to say that it admits that Kissel is liable but sets up that notwithstanding such liability the directors think that it is not fair to him or expedient for the company to enforce the liability. The plea sets up not the present sentiment or opinion of the directors but their formal and deliberate judgment. And that judgment as pleaded finds not that a cause of action exists which it is unfair to enforce but that no cause of action in fact exists. The judgment further finds that it is not to the interest of the company to bring the suit and approves a report of a committee of the board declaring that if an action against the directors could be sustained it would be detrimental to the best interests of the company to bring it. The theory of the plea is that the judgment of a board of directors, honestly arrived at after full and fair investigation, binds the stockholder as effectually as the judgment of a court of record; and that, too, whether the board finds that no cause of action exists or that, a cause of action existing, it is not to the interest of the company to enforce it. Under these circumstances it is quite as illogical, as it seems to us, to say that the plea admits the cause of action as it would

be to say the same thing of a plea setting up the judgment of a court of record. And equally illogical is it to say that the evidence in support of the judgment of the board ought to be set out; that if no cause of action exists the directors should show why it does not exist, or if they think it inexpedient to bring suit they should show why it is inexpedient. This would be to waive the whole force and effect of the judgment and to submit to the court questions which the law submits to the directors and with respect to which the judgment of the directors is final. As well might it be said that a defendant pleading the judgment of a court or record must set forth the facts upon which such judgment is founded and justify the finding by his pleading and evidence.

No greater force or finality is given to the judgment of any court than the cases both in this country and in England have for a century given to the judgment of corporate directors acting within the scope of their authority and acting honestly.

So late as 1902 the House of Lords declared in *Burland v. Earle*, *supra*, that it is an elementary principle of law relating to joint stock companies that the court will not interfere with the internal management of companies acting within their powers; that indeed it has no jurisdiction to do so and that the cases in which the minority can maintain a stockholder's action are confined to those in which the acts complained of are of a fraudulent character or beyond the powers of the company. And to precisely the same effect was the judgment of this court in *Berger v. The Steel Corporation* pronounced in the same year at the June Term of this court and repeated in *Hodge v. The Steel Corporation* at the succeeding term.

The learned Vice Chancellor in observing what was admitted in favor of the complainant by the form which the pleadings took seems to have quite overlooked the admissions in favor of the defendant. For instance the defendant answered in support of the plea denying the charges of fraud and collusion contained in the bill and in the plea averred the good faith of the directors not only but that they had fully and patiently investigated the claim of the complainant before rejecting it. By failing to file a replication to this plea and answer the complainant admits its truth. The case stands, therefore, with the charge of fraud against the present board eliminated without which the complaint would be demurrable. It also stands with the allegation admitted that the directors made a full and careful investigation and reached the conclusion that suit should not be brought upon the double ground, 1st that it would not lie, and 2nd, that if it would lie it would not be to the interest of the company to bring it.

We respectfully submit that such a plea is sufficient on its face; that as a matter of pleading the defendant who sets up the judgment of a board of directors upon a question within its jurisdiction is no more bound to plead the evidence upon which such judgment was founded or to justify it with facts or circumstances than is one who pleads the final judgment of this court. Fraud will avoid the judgment of a court as well as the judgment of a board of directors, but when the judgment of either is impeached for fraud and the fraud is denied, the complainant must join issue on the denial and go to hearing on the merits.

As to the suggestion that Kissel may be in a different situation from that of the board of directors as a whole and that therefore the conclusion of the present board that an action will not lie against the old board is no answer to a suit against Kissel, it is enough to say, 1st that the board placed its refusal upon grounds which apply to all the directors, and 2nd that no demand was made by the complainant that suit should be brought against Kissel alone. If the complainant thought Kissel's situation was different from that of the other directors and that a suit would lie against him even if one would not lie against the others, he should have framed his demand accordingly or made a new demand.

The learned Vice Chancellor cites only one case in support of his judgment, namely, *Dodge v. Woolsey* to which we have already called attention. The conclusion which he draws from the decision in that case we think cannot be supported. He says that "Although the case was devoid of any element of *ultra vires*, *fraud* or oppression the Supreme Court held that the suit was maintainable; in other words, the constitutional right to protection against the imposition of a further tax being adjudged, the stockholder was permitted, as the representative of the company, to override the *judgment* of the directors on the question of expediency of testing the right in the courts." (The italics are ours). As we read this case, instead of its being devoid of any element of fraud, the Supreme Court found that there was fraud and placed its judgment on that finding, and instead of the court holding that the stockholder was permitted to override the judgment of the directors on the question of ex-

pediency it held that the directors had exercised no judgment whatever.

It will be noted that this case arose upon final hearing and not upon a plea demurred to. The bank itself did not answer the bill of complaint but Dodge, the tax collector, did and averred that no demand had been made upon the directors to bring suit. A replication was filed and a formal demand upon the directors to bring suit was put in evidence, together with a resolution passed by the directors in response to such demand in which the directors stated that they fully concurred in the views expressed in the demand as to the illegality of the tax and believed that it was in no way binding upon the bank but that in consideration of the many obstacles in the way of testing the law in the courts of the State they could not consent to take the action called for. The Supreme Court admitted that the judgment of a board of directors upon a matter *intra vires* could not, in the absence of fraud, be reviewed or set aside by the courts even where it was believed to be erroneous, but held that the action of the board in that case partook "more of a disregard of duty than an error of judgment" and that "it was a non-performance of a confessed official obligation amounting to what the law considers a breach of trust;" that being a duty by their own confession the refusal of the board was an act outside of the obligation which the charter imposed upon them to protect what they conscientiously believed to be the franchises of the bank and added "A sense of duty and their conduct contrary to it is not an error of judgment merely and cannot be so called in any case." The court also pointed out that if there were obstacles in the way of testing the law in the courts of the State

a writ of error would lie from the judgment of the State Court to the Supreme Court of the United States.

As heretofore remarked, it has been held in England and in this country for a century that the judgment of a board of directors upon the question as to whether it is expedient to do or not to do some *intra vires* act cannot be overridden by the stockholders or the courts, and it would be a matter of astonishment to find in *Dodge v. Woolsey* anything to the contrary of this doctrine. That nothing to the contrary of it was intended is clearly shown by the judgment of the same court in *Hawes v. Oakland* which soon followed *Dodge v. Woolsey*. There the court took pains to point out the several grounds upon which a stockholder's action may be founded, no one of which includes the review of the judgment of a board of directors on a question within their discretion, and in order that no false impression might be perpetuated with regard to the decision in *Dodge v. Woolsey* the court said:

"The examination of *Dodge v. Woolsey* satisfies us that it does not establish, nor was it intended to establish a doctrine on this subject different in any material respect from that found in cases in the English and other American courts."

As was said in *Corbus v. Alaska Treadwell Gold Mining Company, supra*, "It is not a trifling thing for a stockholder to attempt to coerce the directors of a corporation to an act which their judgment does not approve, or to substitute his opinion for theirs." If any appeal should lie from the judgment of a board of directors with regard to a question of corporate man-

agement, it would seem that it ought to lie to the stockholders. Such an appeal was taken by the complainant in this case and was overruled by a vote of over 99% of the disinterested stockholders, after the complainant was fully heard. Upon what principle of law or morals he can now ask the court to substitute either his or its judgment for that of the directors and majority stockholders on such a question, we are quite at a loss to understand.

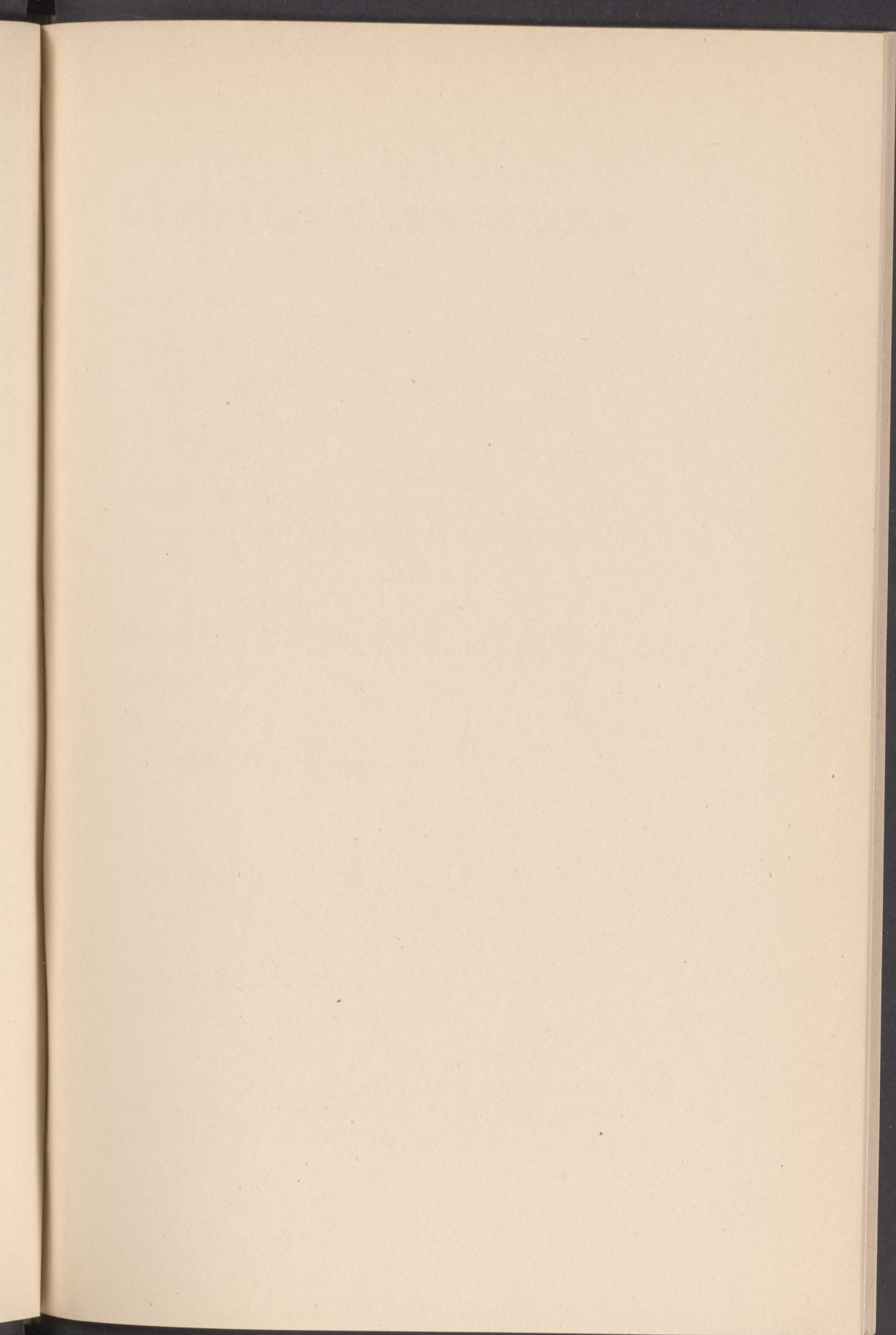
We respectfully submit that the decree appealed from finds no support in any American or English case decided in a court of last resort; that it is contrary to the principles of corporate management and equity pleading which have come to be considered as elementary, and that it should be reversed and the plea of the defendant sustained.

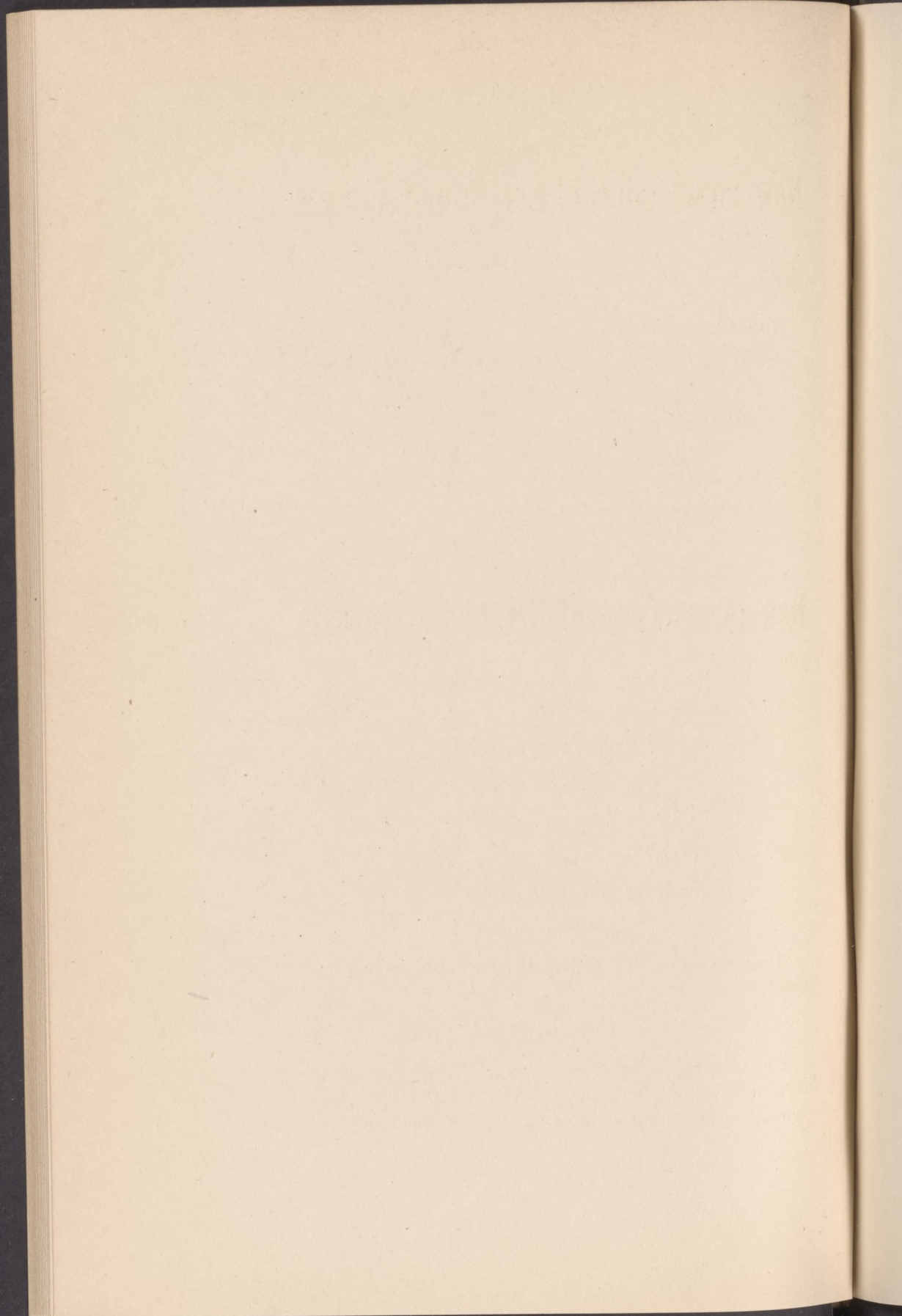
Respectfully submitted,

R. V. LINDABURY.

WM. H. PAGE, JR.

June Term 1906.





New Jersey Court of Errors and Appeals

Between

RICHARD SIEGMAN,

Complainant and Respondent,

and

NORMAN HENDERSON *et al*,

Defendants and Appellant.

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New Jersey Court of Errors and Appeals 20

Between

RICHARD SIEGMAN,

Complainant and Respondent,

and

RUDOLPH H. KISSEL *et al*,

Defendants and Appellant.

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Brief of James E. Howell for Complainant (Respondent).

THE BILLS.

The bills in these cases are filed by Richard Seigman, a stockholder of the Electric Vehicle Company, against (1) Henderson and (2) Kissel and the 40

Electric Vehicle Company, to compel the payment by them to that Company of a large amount of money which was paid out by the company in the form of a dividend, it being claimed that the same was paid out of the capital and not out of the earnings.

The suit is under Section 30 of the Corporation Act of 1896, which was dealt with by the Court of Appeals in *Appleton v. American Malting Company*, 20 Dick.
10 375.

Mr. Siegman is the owner of Two hundred (200) shares of the preferred stock and Two hundred (200) shares of the common stock of the Electric Vehicle Company, which he has held since the year 1899.

The defendants Henderson and Kissel were elected directors of the Company in September, 1898, and
20 held their offices until September, 1899, during which period three dividends were declared.

On April 1, 1899, the Board declared two dividends; one on the preferred stock aggregating Eighty-four thousand eight hundred dollars (\$84,800), and one on the common stock aggregating One hundred thousand dollars (\$100,000). Both Kissel and Henderson were members of the Board of Directors when these two dividends were declared. On June 30, 1899,
30 the Board of Directors declared a further dividend of two (2) per cent. on the common stock which amounted to One hundred and forty thousand dollars (\$140,000). At the time of the declaration of this dividend Mr. Henderson had ceased to be a member of the Board but Mr. Kissel was still a member. The claim in the Henderson bill is for One hundred and eighty-four thousand dollars (\$184,000), and in the Kissel bill for Three hundred and twenty-four thousand
40 and dollars \$324,00). The bill alleges that Mr.

Henderson and Mr. Kissel were large stockholders in this corporation. That they attended at the meeting of the Board of Directors at which these dividends were declared and voted for them, and that the dividends were not declared and paid out of surplus or net profits of the corporation, but were declared out of the capital, and that Mr. Henderson and Mr. Kissel knew that they were unlawful and that they were paid out of the capital, and that they represented it to be the fact at the time the dividends were declared that they were declared out of the profits. 10

In September, 1903, the complainant served a notice upon the persons who were then the directors of the Company, in which they were notified of the fact that these unlawful dividends had been paid, and they were requested to bring suit. The directors declined to bring any such suit. There is an allegation that at the time the directors so refused they knew that the dividends had been unlawfully declared and paid, and that there was no valid reason why the Company should not sue for the amounts so paid out, and that these directors were acting not for the benefit of the Company but for the benefit of the former directors who had dissipated its funds, and that they passed upon this question of a demand for suit in a perfunctory and informal way and without any knowledge of the facts. 20

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The eleventh paragraph of the bills shows one manner in which the directors made up a surplus for the declaration of these dividends. The company had stock in other corporations and they inflated the value of these stocks by a mere valuation for the purpose of making it appear that there was a surplus, and then they declared dividends out of this fictitious surplus. There is a further allegation that no such surplus ever existed and that these stocks never had any value that 40

might be considered. There is a prayer for answer and discovery and for a declaration of liability against the individual defendants as parties who jointly and severally are liable for what was done. The principal authorities for this course are—

Dodge v. Woolsey, 18 How. 331.

Hawkes v. Oakland, 104 U. S. 450.

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Appleton v. American Malting Co. 20 Dick. 375.

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THE PLEA.

The Electric Vehicle Company pleads—

(1) That the dividends complained of were declared in good faith, and—

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(2) That the refusal of the directors to bring suit, when requested so to do by Mr. Siegman, was also in good faith.

Here are two defences attempted to be set up by a single plea. Duplicity in pleading in equity is quite as objectionable as at common law. A plea must set up a single fact, which if true in point of fact and sufficiently pleaded or admitted, will end the contro- 20
versey.

This plea admits the principal allegations of the bill, namely, that the dividends were paid out of the capital, which of course was illegal, but it attempts to palliate the offence by asserting that they were paid in good faith. The most obvious thing about the plea is its lack of facts. It states conclusions of fact and conclusions of law, but it omits to state facts from which these conclusions can be drawn. 30

I may say at the outset, that the precise point argued in this brief has been recently twice heard and decided, first, by the United States Circuit Court for the District of New Jersey and secondly by our Court of Chancery.

Siegman v. Electric Vehicle Co. 140 F. R. 117

August, 1905;

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That case arose on bill and plea. The bill and plea were identical with the bill and plea in the case at bar.

Judge Lanning overruled the plea, upon the ground that the matters therein set out did not show that the directors of the Electric Vehicle Company acted in good faith in declaring the dividend, or in refusing to bring suit to recover back the money unlawfully paid.

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In *Groel* against the *United Electric Company*, 61 Atl. R. 1061, Oct., 1905, Vice Chancellor Garrison overruled a similar plea holding that the complainant had set out a cause of action and that the defendant's plea that the corporation deemed it inexpedient to bring a suit for the cause of action was unjustifiable and expressing a grave doubt as to whether a defendant corporation, circumstanced as that one was, should be permitted to raise the issue of the right of a complainant to bring a suit in behalf of the corporation by filing a plea or answer denying that right.

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The plea admits Siegman's demand in September, 1903. This demand was laid before the directors on September 15, 1903. The directors appointed a committee to examine and report, which they did on Sept. 29, 1903, a copy of this report is annexed to the plea as Exhibit B., and it is this report as a basis on which the board of directors passed its resolution Exhibit 6, and all the facts which are set up in the plea are referable to this report alone. It contains all the facts which are alleged as a ground of defence to the suit. It starts it by reporting that the committee has examined the accounts, statements and records of the Company at the time the dividends were declared, and has also inquired into the history of the company's affairs from its organization until the last dividend was paid, but it does not report these ac-

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counts, statements and records to the directors and, so far as the report shows, the directors had that document only before them.

It is true that the resolution Exhibit C. states that the board of directors had examined documents, accounts and statements but there is no allegation anywhere to show what documents, accounts and statements were so examined.

But to return to the facts which are alleged in the report. The first dividends amounted to \$184,800. The facts upon which that dividend was based are stated in the report as follows: "Business was carried on in 1898 with success, and the prospect seemed very good. In February 1899, a sale was made of a plant, constructed by the company, in New York City for the manufacture and operation of electric vehicles in that city. This sale was made to a new company called The New York Transportation Company for a large sum of money, which was paid in cash, and as a part of the transaction a contract was made by this company with that company, assuring this company a large income from the business of the New York Company if successful, and soon after like contracts were made with several other companies with large capital operating in defined territories in other parts of the country. On March 7, 1899, there were outstanding preferred shares amounting to One million and sixty thousand dollars (\$1,060,000) and common Five million dollars (\$5,000,000), and a dividend was declared on that date of eight (8) per cent. on preferred stock for the year 1899 and two (2) per cent. on common, amounting to \$184,800. This dividend was fully warranted by the surplus accumulated."

It will be noticed that while the company made a sale of property in New York for a large sum of

money, there is no statement as to the amount received, or whether it had any relation whatever to surplus out of which dividends could be paid, or anything to show whether it was a large sum of money or not. A part of the bargain with that other company was a contract made between the two companies by which this company was assured a large income from the business of the New York company
 10 *in case the New York Company was successful.* This likewise seems to have no relation whatever to a solid, substantial surplus out of which dividends could be paid. In fact, the words indicate that if the New York company was not successful some other disposition of the matter might have been necessary. Apparently what they did was to declare a dividend on a mere business venture. There are no facts stated, no
 20 figures given, no information opened to the board of directors by this report, from which any of the members of the board could determine independently for himself whether this dividend had been earned and was fully warranted by the surplus accumulated, or whether there was in fact any surplus.

The above quotation is the only excuse which the company gives for the dissipation of \$184,800. The remainder of the report, which is annexed to the plea,
 30 relates to other dividends declared by the corporation in which Mr. Henderson and Mr. Kissel had no hand, because at the time they were declared these gentlemen were not members of the board and hence cannot be charged. But it is instructive to examine the remainder of this report because it throws a strong light on the loose, if not fraudulent, methods adopted by this board of directors for the purpose of booming their stock.

Take for instance the declaration of the last dividend on March 20, 1900, which amounted to \$100,000
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and this is the excuse—"At that time the market value of the shares of the Transportation Company held by this company had depreciated. There were, however, large orders for vehicles placed by this company with the Columbia Electric Vehicle Company, exceeding in amount \$3,000,000. The interest of this company in the Columbia Electric Vehicle Company, which had cost one million dollars, was supposed to be of much greater value. The stock of that company was not on the market and could not be tested by sales. The vehicles were still in demand, the orders being larger than ever, and a large profit on them seemed assured. That was a confident expectation that the batteries would be improved, and this has since been realized, although not in time for the machines built in 1900. It cannot be said that the dividend of one hundred thousand dollars declared on preferred stock on March 17, 1900, was not properly declared in view of what appeared at that time. *It is now known that the whole enterprise upon which the company was embarked was unsound, but that was not suspected at that time.* The confidence of the stockholders and directors in their enterprise during the year 1899 is evidenced by the market price of their stocks. The direct- such when the experience of the year 1900 demonstrates that the enterprise as originally projected was a failure."

This is a fair sample of the so-called facts set up by the plea, and if this latter means anything at all it means that this company converted its orders, which had never been filled, in a surplus out of which it paid One hundred thousand dollars (\$100,000) in dividends; and notwithstanding the fact that there is no pretense that any surplus existed, it is claimed that it cannot be said that the dividend of One hundred

thousand dollars declared at this time was not properly declared, in view of what appeared at that time. This is not only a suppression of facts and clear evasion of the issue, but it is a positively absurd statement and its absurdity is demonstrated by the statement that follows it, namely: "That it is now known that the whole enterprise was unsound, but that its unsoundness was not suspected at the time the dividends were declared."

Anyone who reads this report would know that the whole enterprise was always unsound, but how this latter-day omniscient committee could know that its unsoundness was not suspected by the negligent or fraudulent directors at the time the dividends were declared is more than I can imagine.

The report winds up with another statement that the directors who were in office when the dividends were declared were large stockholders and continued to be such when the experience of the year 1900 demonstrated that the enterprise as originally projected was a failure. It is fair to suppose that the hold their stock yet but only because they have not been able to sell it out to the unsuspecting public.

This report was intended to bolster up the action of the board of directors in their refusal to bring suit, but it contains no facts whatever suitable for that purpose. Whatever facts are stated in the plea are facts which were known to the directors in 1899, and they demonstrate now, not in the light of past events but on their face, the fact that there never was any surplus out of which these dividends could have been declared. How can they say that their refusal was in good faith?

This report was approved by the board of directors and Mr. Siegman's request denied. In order to give

this fact and fraudulent affair the appearance of fairness, the board called a meeting of the stockholders who resolved by a large majority to approve the action of the board of directors and that no suit should be brought by the company, or on its behalf, to recover these unlawful dividends or any damages or penalties on account thereof.

The action of the stockholders has no force or effect whatever. The law of New Jersey commits the 10
conduct of the affairs of a corporation to the directors and to them only, and they are not bound by any action of the stockholders, nor need they follow the advice of that body. Upon the coming in of this report it is interesting to observe what the stockholders did. Having no knowledge of the matters complained of, except what was contained in the report which was before them, they recited in their resolution—(1)
“that it appears that no just ground exists for a suit 20
against the former directors of the company, on account of the declaration of the dividends complained of; (2) “It appears that it is not expedient nor for the interest of the company that a suit on that account should be brought against the former directors.”
And they resolve that they ratify and approve the action of the directors, and also resolve that no suit shall be brought against the former directors either for dividends or for any damages or penalties on account of the declaration of dividends. 30

It will be observed that there has been no release of the cause of action, nor any binding covenant not to sue. The cause of action subsists, and indeed, its release would be a palpable fraud. The directors may at any time rescind this resolution and resume their right to bring suit; and in case the company should be thrown into insolvency or bankruptcy this resolution of the board of directors would not bind the Receiver or Trustee; notwithstanding it he could sue. 40

The point of asking directors to bring a suit of this character is merely to have the suit brought by the corporation and in its name for mere convenience, regularity and conformity. If they refuse, the right of the stockholder to act at once attaches. The refusal does not touch the cause of action or the right of action, it merely regulates the parties, complainant and defendant, it does not release or in any way interfere with the cause of action.

And so with the resolution of the stockholders. While we claim that it is not efficient for any purpose, still if it has any pertinency it is merely another refusal giving the individual stockholder a still stronger right to sue.

But it is said that it does not lie with the court to say whether any suit shall be brought or not, and that it lies wholly with the board of directors, and that in case the board of directors refuse and in their refusal state the conclusion of fact that they acted in good faith nobody can inquire into the matter any further, and that there is no appeal from the board of directors to any court whatever.

This does not seem to be the result of leading New Jersey cases.

Knoop v. Bomrich, 4 Dick. 82, S. C. on appeal, 5 Dick. 485.

Appleton v. Am. Malting Co., 20 Dick. 375.

In those cases the directors who were sued were the persons who had committed the fraud. It was, therefore, unnecessary to request the directors to sue. In cases of that character no preliminary question as to permitting a suit to be brought has ever arisen or can arise. The suit is brought and if the stockholder can

show a cause of action he recovers for his company. The court has no control over the right to sue, it must permit the stockholder to sue, and whether the cause of action exists or not is determined on the final hearing. If it does exist the court will make a decree on it, and if it does not exist the court will dismiss the bill. But it is claimed that in a case where a new board of directors has taken the place of the fraudulent ones, so that a request to sue is necessary, there the court will examine the whole case as a preliminary question to determine whether the right to sue should be exercised. Indeed, that is an expression that is found in the case of *Willoughby v. Chicago Junction Railway Co.*, 5 Dick. at page 667, where these words are used: "A stockholder has no standing in the court to prosecute such an action except on the refusal of the directors, either actually or presumptive, to prosecute, but such refusal of the directors to prosecute must be an unjustifiable refusal. If their reason for not so doing is a valid one the individual stockholder cannot from such refusal derive a right to prosecute in his own name. It would not be reasonable or unjustifiable for a board of directors to refuse to prosecute on the application of a stockholder when there had been an adjudication on the point, which he seeks to have passed upon, which is conclusive upon the company." In that case the directors refused to bring a suit for the reason that the point of law in issue had already been decided against the right of action. In that case Ellerman had brought a suit which decided the point.

Ellerman v. Chicago Junction Ry. 4 Dick. 217.

It was very properly held that the excuse which the directors gave was a good one, but no such excuse is given in this case, nor, indeed, is any excuse given except that everybody acted in good faith, a very simple statement but quite bare of facts.

In the Willoughby case the facts were before the court on bill, supplemental bill, answers and affidavits, and a subsequent stipulation that the cause should be disposed of as if it were heard on final hearing. The defendant pleaded a fact, not a mere inference or conclusion of fact, or a conclusion of law. The fact was that the real point in issue had already been determined and that was, of course, a sufficient reason to excuse the directors from bringing a suit. And the quotation that I have made from the Willoughby case (*Supra*) shows that the Vice Chancellor was dealing with the case in which all the facts were disclosed and upon final hearing. And the same view was taken by the Supreme Court of the United States in *Corbus v. Gold Mining Co.*, 187 U. S. at page 463, from which I quote:

“It must not be understood that a mere technical
 “compliance with the foregoing rule (Rule 94) is
 “sufficient and precludes all inquiry as to the right
 “of a stockholder to maintain a bill against the
 “corporation. This court will examine the bill in
 “its entirety and determine whether under all cir-
 “cumstances the plaintiff has made such a showing
 “of wrong on the part of the corporation, or its
 “officers, and injury to himself as will justify the
 “suit.”

But how can the court examine “all the circumstances” unless “all the circumstances” are disclosed fully, openly and fairly. And the same comment was made by the same court in *Dodge vs. Woolsey*, 18 Howard 344, where it is said “the circumstances of each case must determine the jurisdiction of the Court of Equity to give the relief sought.”

Judge Jones of the N. D. of Alabama, in the case of *Kessler v. Ensley Co.*, 129 F. R. 397, attempted to draw such a distinction but he expressly limits the rule to acts of the board of directors which are *intra vires*.

In that case the Judge prefaces his argument by the statement: "The transaction here complained is wholly *intra vires* and involves private not public wrong." "The corporation may hold them (the officers) to such transactions unless the thing done is forbidden by law or condoning it is contrary to public policy. If the transaction in which the officer defrauding the corporation is one into which it might enter in the first instance, it is not contrary to public policy for the corporation to condone the fraudulent contract and insist upon its performance on sufficient consideration and motives. The wrong here is a private wrong and a private person may condone a private wrong and the rights of the public and strangers are not involved." 10 20

"All cases admit that the persons defrauded, if *sui juris*, can ratify the fraud. The corporation is certainly *sui juris* as to matters *intra vires*."

(Earlier report of the same case, 123 F. R. 546).

We may here state at this point that the unlawful declaration of dividends is actually forbidden by the statute under which this suit is brought. The whole thing is not only *ultra vires* the corporation, but it is against the well settled and positively declared public policy of the State. It is a transaction in which the State has an interest and is such a violation of the charter of the company as would undoubtedly justify the Attorney-General in taking *quo warranto* proceedings to dissolve the corporation. This is an offence 30 40

against the State which the board of directors cannot ratify or in any manner make good.

The corporation may declare dividends and such act is *intra vires*, but it may not impair its capital wilfully or negligently; such an act is *ultra vires*.

The same distinction between acts *intra vires* and acts *ultra vires* was made by Judge Blatchford in
 10 *Heath vs. Erie Ry. Co.*, 8 Blatchford 847, Fed Case 6306.

“Now so far as the bill sets out acts *ultra vires*
 “in issuing stock and breaches of trust, which are
 “frauds on the stockholders, such acts and breaches
 “of trust are beyond the power of the corporation or
 “its directors to affirm or sanction or make good,
 20 “and in such case the authorities agree that the
 “reason of the rule for an application to the corpo-
 “ration or its board of directors to bring the suit
 “does not exist. Such reason is that while the
 “stockholder is prosecuting his suit the corpora-
 “tion through its board of directors may affirm and
 “make good the acts complained of, but the rule
 30 “ceases when the reason ceases. The bill, therefore,
 “is clearly maintainable in respect to the acts *ultra*
 “*vires* which it sets forth and the preventive relief
 “it seeks founded thereon without reference to any-
 “thing else contained in it.”

In closing this point I may say, that it is not suffi-
 cient for this company to answer that its directors
 acted in good faith, even though they set out the nec-
 40 essary facts to show it, they should likewise set out

sufficient facts to convince the court that they did not act negligently or carelessly, or without that prudence which is required of the ordinary careful individual. Have they shown that they exercised that caution and discrimination, and care and investigation, and good judgment and prudence which they exercise in

It is monstrous to say that this company can stop their own lines of business? Assuredly not.

It is monstrous to say that this company can stop this investigation into its affairs and stop the complainant from collecting a debt for it by merely saying "good faith" and that there is no appeal from that unsupported assertion to any court. The facts appearing on the face of this bill and plea, meager as the defence is, would convince an ordinary jury without further proof that the whole scheme was either fraudulent or negligent.

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AN INEQUITABLE DEFENCE.

Will a plea by this company, even though proper in form and sufficient in facts, lie in a case like the present? The best interests of this company would be subserved by placing money in its treasury. It is absurd to say otherwise. The company should feel grateful to Siegman for bringing the suit and fighting its battles, and should aid him to the uttermost of its power and should not stand in his way. I can easily see how Henderson and Kissel and any other of the directors who might be sued might consistently interpose this defence, which at the best is purely technical, but how can the company with any degree of good faith decline to receive the money which the complainant may recover.

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In the first report of *Kessler v. Ensley*, 123 F. R. 546, the counsel for the company answered submitting the company to the judgment of the court, a very 40

proper proceeding. It was there left to the persons who were accused of having defrauded the company to set up the technical inequitable defence by which they hoped they might escape the consequences of their fraudulent acts.

See opinion of Garrison V. C., Oct. 2, 1905, in *Groel v. M. E. Co.*, 61 atl. Rep. 1061.

10 The most salient point in all these pleadings is that a board of directors should have the hardihood to allege that in refusing to bring a suit for nearly a million dollars they acted in good faith and for the best interests of the company, and for this reason stood between Siegman and the fraudulent board of directors.

20 The plea practically confesses that the former directors of this company in paying these dividends acted upon what turned out to be entirely false premises, a confession of their negligence. It is at least a confession that the charge of the bill that the dividends were paid out of the capital is true. The mere recital of the board of directors in their resolution that no just ground exists for a suit is no answer and it, therefore, appears that this company has a claim for nearly half a million dollars which it declines for some undisclosed cause to prosecute.

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Another declaration is that it is not expedient or for the interests of the company to bring suit, and while these allegations are not sustained by any fact, still if the fact existed it would hardly be an excuse for this company to stand in the way of receiving this large amount of money. It merely shows that the present board of directors are not acting in good faith, that they are interposing an inequitable and fraudulent defence for the purpose of saving the former di-

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rectors from the consequences of their fraud or negligence.

If the claim had been for \$500 instead of the large amount mentioned the present absurd plea of good faith and expediency might have some weight. It might cost more to recover the claim than the claim was worth. Mr. Henderson and Mr. Kissel might have some business relations with the corporation which might be terminated to the disadvantage of the company, in case the claim was prosecuted and he became its enemy instead of its friend. There might have been some previous decision of some court as there was in the Willoughby case, which might have been interposed as a defence as a reason for refusing to sue. None of these things appeared and there is no fact that goes to the argument *ab inconvenienti*. 10

Shortly before the filing of the bill in this case a similar bill was filed in this court against Martin Maloney, to which bill precisely the same plea was interposed. The only difference between the cases in hand and the Maloney case being that Maloney was sued for all the dividends that were declared, while Henderson and Kissel are sued for only a portion of them. The plea was set down for argument before the United States Circuit Court and after consideration was overruled for reasons set out in the opinion of Judge Lanning, a copy of which is annexed hereto. 20 30

JAMES E. HOWELL,

Of Counsel

140 Fed. Rep.
117.

In Chancery of New Jersey.

To the Honorable William J. Magie, Chancellor of the State of New Jersey.

In Chancery complaining shows unto your Honor your orator Richard Siegman, of the City, County and State of New York, who sues, not only for himself but for all the other stockholders of the Electric Vehicle Company who are similarly situated with him and who may apply to be admitted to this suit and contribute to the expense thereof; 10

1. That the Electric Vehicle Company was incorporated under the laws of New Jersey on the 29th day of September, 1897, with a capital stock of \$10,000,000, which was afterwards increased from time to time to \$18,800,000, divided into shares of the par value of \$100 each, and also divided into common stock and preferred stock; the holders of which preferred stock are entitled to an eight per cent preferential dividend to be paid out of the surplus earning or profits of the said company. 20

2. That on or about the 15th day of February, 1899 your orator purchased 200 shares of the preferred stock of the said Electric Vehicle Company and has been at all times since and now is the owner and holder of the said shares and that the same are registered on the books of the said corporation, and that on or about the 10th day of October, 1899, he purchased 200 shares of the common stock of the said company and that he has been at all times since and now is the owner and holder of the same, and that the same is registered in his name on the books of the said company. 30

3. That the annual meeting of the stockholders of the said company for the election of directors thereof, according to its by-laws, is held in the month of September of each year, and that on the 20th day of Sep- 40

tember 1898, Rudolph H. Kissel was elected a director of the said corporation, and that he held his office of director until the 19th day of September, 1899, so that the said Rudolph H. Kissel held and exercised the office of director of the said corporation continuously during the time of the committing of the grievances by him, hereinafter more particularly set out.

10 4. That on the 1st day of April, 1899, the Board of Directors of the said corporation declared a dividend of eight per cent on the preferred stock of the said corporation which was then outstanding, which dividend aggregated the sum of \$84,800, and that on the same day the said Board of Directors of the said corporation declared a dividend of two per cent upon the out-
 20 standing common stock of the said corporation, which dividend aggregated the sum of \$100,000, and that these dividends, amounting in the whole to the sum of \$184,800, were actually paid by the said corporation and its Board of Directors to its stockholders and that
 on the 30th day of June, 1899, the Board of Directors of the said corporation declared a further dividend of two per cent upon the 700,000 shares of the stock of the said Electric Vehicle Company then issued and outstanding, for the quarter ending on said 30th day of June, 1899, which dividend aggregated the sum of \$140,000, which was also actually paid by the said corporation and its Board of Directors to its stock-
 holders.

30 5. That the said Rudolph H. Kissel during the period which the dividends were paid was a prominent and active director of the said corporation and that he held and now holds, as your orator is informed and believes and charges the truth to be, a very large amount of the capital stock of the said corporation; that your orator is informed and believes it to be true and charges the truth to be that the said Rudolph H. Kissel attended the meetings of the Board of Directors at which the above mentioned dividends were
 40 declared and that he voted at the meetings of the said

Board for the declaration of the said dividends and that when the said dividends were paid those which were declared upon the stock held by him were paid to and received by him.

6. That your orator is informed and believes it to be true and charges the truth to be that the said dividends hereinabove specifically mentioned were not declared and paid out of the surplus or net profits arising from the business of the said corporation and that at neither of the times hereinbefore stated, when such dividends were declared, and paid, had the said corporation sufficient surplus or net profits out of which to pay any such dividends or any dividends at all, and that the said dividends were declared and paid out of the capital of the said corporation unlawfully and contrary to the laws of this State and that the said Rudolph H. Kissel knew that such dividends so voted for him and so declared and paid by the said Board of Directors were unlawful and were not paid out of the surplus or net profits of the business of the said company but were paid out of the capital of the company, and that in so declaring and paying the said dividends they unlawfully impaired the capital of the said company and divided, withdrew and paid to its stockholders a portion of its capital stock and reduced its capital stock contrary to the laws of this State, and that the said Rudolph H. Kissel thereby made himself liable under the statute to the said corporation to the full amount of the dividends so made and capital stock so divided, withdrawn, paid out and reduced, with interest on the same from the time such liability accrued.

7. That at the time the said dividends were declared the Board of Directors which was concerned therein, included the said Rudolph H. Kissel, openly stated and represented it to be a fact that the dividends thus declared and paid were duly and lawfully declared and paid out of the net earnings and profits made by the said company in the course of its business and that

your orator believed the said statements and accepted the dividends which were declared in his favor on his said stock, and that he did not learn of the facts which he now presents to the court until the month of August, 1901, or thereabouts, in which month your orator brought a suit in this court against the said Board of Directors which was concerned in the declaration of the said dividends; that in said suit your orator alleged the unlawful payment of dividends as herein-
 10 above set out and prayed that the directors who were in office at the time the said dividends were declared might be made jointly and severally liable for the amount of the moneys so wrongfully paid out by their direction, but that this court dismissed the bill in the said suit upon the ground that your orator had not requested the Board of Directors of the said company who were in office at the time the said suit was brought to bring suit or suits in respect to the matters set out in the said bills and the declaration of the said divi-
 20 dends and your orator shows that the final decree in the said suit was subsequently affirmed by the Court of Errors and Appeals in the spring or early summer of the year 1903.

8. That in the month of September, 1903, at the time of the service of the notice hereinafter mentioned, George H. Day, M. Toscan Bennett, N. J. Budlong, Philip T. Dodge, John Hone, A. D. Newton, Albert A. Pope, Isaac L. Rice and Fred. Vieweg were the directors of the Electric Vehicle Company and that
 30 since that time the said company has not filed in the office of the Secretary of State any report giving a list of its officers and directors, as required by law, and your orator therefore charges the truth to be that the said persons were then and hitherto have been and now are the directors of the said corporation.

That in the month of September, 1903, your orator served upon the said Electric Vehicle Company and upon the persons who were then its directors a notice
 40 in and by which your orator notified the said Board of

Directors of the facts hereinabove stated in relation to the unlawful declaration of dividends out of the capital of the said corporation, and that in said notice your orator demanded that the said corporation, its officers and directors, should forthwith take such proceedings as might be necessary, or as they might be advised, to charge the said directors who declared the said dividends jointly and severally as their liability might appear with the amount so divided, withdrawn and paid out, with interest, and to collect the same by lawful proceedings for the benefit of the said corporation and to collect also such damages in addition thereto as might have accrued to the said corporation by reason of the illegal payments of the said dividends and that your orator therein and thereby requested that a meeting of the then Board of Directors of the said corporation should be called immediately to consider his demand and to direct action to be taken upon it, and that in and by the said notice your orator called the attention of the Board to the fact that he had previously brought suits in this court in respect to the matters now complained of, to which suits some of the then directors of the said corporation were parties, and that in response thereto your orator in the latter part of the year 1903 received from the President of the said corporation a letter enclosing a resolution of the Board of Directors of the said corporation, certified to by the secretary thereof, in and by which it was resolved that the demand of your orator that suit be brought against the former directors of the said company to recover said dividends was thereby denied.

9. That at the time when said Board of Directors so refused to sue for the moneys so unlawfully paid out as dividends they well knew that said dividends had been unlawfully declared and paid out and that there was no valid reason why said Electric Vehicle Company should not sue for said moneys so unlawfully paid out and that in refusing so to sue said Board of Directors did not act or intend to act for the benefit

of the said Electric Vehicle Company but were acting and intended to act for the benefit of said directors who had participated in the declaration of said unlawful dividends and that their refusal so to sue was unlawful and in violation of their duty to the said corporation.

10 10. That your orator is informed and believes it to be true and charges the truth to be, that the declaration and payment of the said dividend was a wanton disregard of the law of this State and of the rights of the said corporation and its stockholders; that your orator is likewise informed and believes it to be true and charges the truth to be that there was never placed before the Board of Directors of the said corporation any statement of the accounts of the said corporation or of its financial condition which showed that it had made any profits which would warrant the payment of the said dividends, and that the said Rudolph H. Kissel as one of the directors of the said corporation, 20 never inquired into its financial condition and voted blindly for the declaration of the said dividends without knowing anything whatever of the financial condition of the said corporation; that there was nothing in the nature of its assets nor in the character of the business in which it was engaged which would justify the said Rudolph H. Kissel, or any of the directors of the said corporation in believing that their said corporation had earned and had in its possession any surplus or net profits out of which lawful dividends 30 might be paid.

11. That your orator had been informed and believes and charges the truth to be that the said Rudolph H. Kissel and the directors of the said corporation who voted for the said dividends claim that in valuing the assets of the said corporation for the purpose of ascertaining whether there was a surplus or net profit out of which dividends could be lawfully declared, they valued the stocks of certain corporations held by the Electric Vehicle Company or 40

in which the Electric Vehicle Company was interested, at a large amount, but your orator shows that the stocks of the companies then owned by the Electric Vehicle Company never had any such value as the said directors then placed thereon and that this fact was well known to the said Rudolph H. Kissel and to the other directors of the said corporation when they declared and paid the said dividends; that there was never any fair and honest valuation made of the assets of the said corporation by the said directors for the purpose of ascertaining whether it had a surplus or net profit enabling it to pay dividends under the law, and that there never was any such surplus or net profit applicable to the payment of dividends and that the payment of said dividends was a fraudulent act for which said directors, including the said Rudolph H. Kissel, are by law jointly and severally liable to said corporation; that prior to the declaration of said dividends the business had never been carried on with a profit, as was well known to the said Rudolph H. Kissel and the other directors.

12 And your orator further shows that such surplus as is pretended by the said Rudolph H. Kissel and the other directors to have existed were arbitrarily and ficticiously made to appear by placing upon the stocks of companies owned by the Electric Vehicle Company a forced and unwarranted valuation; that said stocks were at certain periods during the time of the declaration of said dividends quoted in the market at prices many times their actual value and that said quotations were purely speculative and temporary as was well known to the said Rudolph H. Kissel and the other directors, and that none of the said stocks owned by said corporation were ever sold by it at said prices or any other prices and that the prices of said stock as quoted in the market have since the declaration of the first of the said dividends violently declined, and have for many years stood at a figure which would show an enormous loss to the said Electric Vehicle Company on its investment therein.

13. That none of the companies whose stock was thus owned by the Electric Vehicle Company had at the time of the declaration of said dividends or ever since earned any profits or surplus, and never offered any prospect of earning such profits, but on the contrary thereof the business carried on by said companies was of no importance or extent whatsoever, and that in fact some of said companies have since been entirely dissolved because of their utter lack of business or earning capacity.

14. And your orator shows that the pretense of a high valuation of the stocks of the said companies as indicating a surplus or profits accruing to the Electric Vehicle Company was a purely fraudulent and unwarranted device resorted to by the said directors, including Rudolph H. Kissel.

WHEREFORE, Inasmuch as your orator is without remedy by the rules of the common law, he prays:

1. That the said Rudolph H. Kissel and the said Electric Vehicle Company may true, full and perfect answer make, but without oath, to all and singular the premises, and that they or such of them as have knowledge thereof may set forth and discover when the Electric Vehicle Company was organized and what was its then authorized capital stock, and how divided into common and preferred stock and at what times and on what dates its authorized capital stock was increased and the amounts of money and property received upon the issue and sale of said stock, and the dates when so received, and what business the Electric Vehicle Company has been engaged in from the date of its organization down to the present time, and the manner in which the same has been carried on, and the character and extent of its business, and the number of vehicles it has manufactured and sold, and what profits have been made by the Electric Vehicle Company from its organization down to the time of the declaration of the last dividend herein above referred

to and whether it ever had any surplus at that time and if so the amount thereof; and from what source the same was derived and the manner in which such profits and surplus are entered in its books of account, and that they may state each and every source of revenue and profit from which the revenues or profits of the said company have been derived since the organization of the said company, out of which the said dividends could be lawfully paid, and the several amounts of such revenues or profits, and that they, or such of them as have knowledge thereof, may set out and discover what dividends were paid upon the capital stock of the said corporation, common and preferred, and the dates when the same were respectively declared and made payable and paid, and that they may likewise set out and discover the funds from which the said dividends were paid and the source or sources from which the said funds were derived, and that they may set forth and discover what statements, balance sheets, reports or other documents were made or compiled from time to time by the said corporation for the use of the Board of Directors in ascertaining whether the profits had been made or not out of which the above mentioned dividends were declared and that they may set out and discover what losses had been incurred by the said corporation from the date of its organization down to the time of the declaration of the last of the said two dividends hereinabove mentioned, and in what way such losses were incurred and the amounts thereof, and when the same accrued and whether the same had been entered in their books of account or not, and if so, what entries were made in relation thereto and when; and that the said defendants or such of them as have knowledge of the same may set forth and discover the names of all corporations in which the Electric Vehicle Company was a stockholder at the time of the declaration of the said dividends and the number of shares of stock in such companies respectively held by the Electric Vehicle

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Company, and so far as they have knowledge, information and belief in regard to the same, that they may set out and discover what the assets of such corporations severally were and at what valuation the stocks therein held by the Electric Vehicle Company were valued by the Electric Vehicle Company or its Board of Directors from time to time for the purpose of the declaration of the dividends hereinabove mentioned.

- 10 And that the Electric Vehicle Company may set out and discover all the information it had in relation to the value of the said stocks at the time the said dividends were declared and the manner in which such information was given to it, and that they, or such of them as have knowledge of the same, may set out and discover what assets the said corporation, in which the Electric Vehicle Company held stock as aforesaid, owned at the time the above mentioned dividends were declared, and the value of the same and the amount
- 20 of the liabilities of the said corporations.

2. That it may be declared by the decree of this court that the dividends which were made and declared by the said corporation and voted for by the said Rudolph H. Kissel, as hereinabove stated, at the time and on the days hereinabove set out in that behalf, were not declared and paid out of the surplus and net profits of the business of the said corporation but that the same were declared and paid out of the
- 30 capital thereof; and that the said Rudolph H. Kissel may be decreed to account for the amount of the said illegal dividends and that the amount thereof may be ascertained by the decree of this court and the said Rudolph H. Kissel be decreed to pay to the Electric Vehicle Company the amount so ascertained.

3. That your orator may have his costs in this suit to be taxed, and such other and further relief as the nature of his case requires and as shall be agreeable to
- 40 equity.

May it please your Honor to grant unto your orator the State's writ of subpoena, directed to the said Rudolph H. Kissel, and the Electric Vehicle Company, commanding them to appear in court to answer the premises and abide such decree as shall be made against them.

COULT, HOWELL & TEN EYCK,
Solicitors for and of Counsel with Complainant.

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IN CHANCERY OF NEW JERSEY.

Between

RICHARD SIEGMAN,

Complainant,

and

ELECTRIC VEHICLE COMPANY

and RUDOLPH H. KISSEL,

*Defendants.**On Bill, etc.*

10

PLEA.

The plea of the Electric Vehicle Company, one of the defendants, to the Bill of Complaint of Richard Siegman in the above entitled cause

20 This defendant by protestation, not confessing or acknowledging all or any of the matters and things in the said bill to be true, in manner and form as the same are therein set forth and alleged, for plea to all the relief sought by said bill, and also to all the discovery thereby sought, says:

30 In the month of September, nineteen hundred and three, the complainant, Richard Siegman, made a demand in writing upon this defendant and its directors and officers that they should take legal proceedings against the former directors of this defendant to recover the dividends declared by them and paid to stockholders. (A copy of said demand, dated September one, nineteen hundred and three, is annexed hereto marked as "Exhibit A" and forms part of this plea.) The said demand was laid before the directors of this defendant at a meeting held by them September fifteenth, nineteen hundred and three. No one of the directors who were in office at that time, or who have been in office at any time since, was a director or officer of this defendant at the time of the declaration of dividends by the company in the years eighteen hundred and ninety-nine and nineteen hundred, or

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was in any manner concerned therein. The directors at their said meeting appointed a committee to examine and report upon the application of the complainant with the aid and advice of counsel, and the committee of the company thereupon made their report to the Board of Directors at a meeting held by the directors on the twenty-ninth day of September, nineteen hundred and three. (A copy of said report is annexed hereto as "Exhibit B" and forms part of this plea.) Thereupon the Board of Directors examined the accounts, documents and statements showing the history and affairs of the company in the years eighteen hundred and ninety-nine and nineteen hundred, and procured the advice of Hon. Robert H. McCarter, special counsel employed in this matter, not previously concerned in the business of the company; and being satisfied that the report of their committee was correct, approved the same and adopted resolutions on said twenty-ninth day of September, nineteen hundred and three (a copy of which marked as "Exhibit C" is annexed to and forms part of this plea), whereby it was determined by the said Board of Directors that no suit should be brought by the company or on its behalf to recover from its former directors any of the dividends declared, unless a majority in interest of the stockholders, other than the former directors, should so order. A copy of said resolutions was on the same day sent to the complainant, and no action was taken by him or by any other of the stockholders until the thirteenth day of January, nineteen hundred and four, when a demand was made on behalf of the complainant for the calling of such a meeting. (A copy of said demand, dated January twelfth, nineteen hundred and four, is annexed hereto as "Exhibit D" and forms part of this plea.)

Pursuant to said demand the president of this defendant called a special meeting of the directors, and thereupon, by resolution; at a meeting held by them February third, nineteen hundred and four, called a

special meeting of the stockholders to consider the said demand of the complainant. Formal notice was given to all the stockholders of the company of a special meeting of stockholders, to be held at the company's office February twenty-fourth, nineteen hundred and four, at eleven A. M., to consider and act upon the said demand of the complainant, and the said notice contained a copy of the said notice given to this defendant by the complainant dated September 10 first, nineteen hundred and three, and of the said report of the committee and of the resolutions adopted thereon, and a copy of said notice given on the part of the complainant requesting that such meeting should be called; of all which copies are hereto annexed and form part of this plea.

Pursuant to said notice, a meeting of stockholders was held accordingly at the office of the company, at which meeting there were present in person or by proxy stockholders holding one hundred and twenty-five thousand four hundred and nine (125,409) shares (being more than a majority of all the shares), none of which were owned by any of the former directors of the company, by whom the dividends referred to in the bill had been voted. The complainant was represented at said meeting by counsel holding a proxy to vote on his shares. The notice for the meeting was read to the stockholders, which notice contained the complainant's demand that suit should be brought, the action of the directors, the report of the committee thereon, and the complainant's call for a 30 meeting of stockholders (copies of which are annexed to and form part of this plea), and thereupon the following resolution was adopted, the total number of votes for the adoption thereof being one hundred and twenty-four thousand, seven hundred and fifty-nine (124,759), and the total number of votes against the adoption thereof being six hundred and fifty (650), of which number four hundred (400) were voted by the complainant, and no votes on the adop-

tion of said resolution were cast on the shares held by any of the former directors, by whom said dividends were voted:

"WHEREAS it appears that no just ground exists for a suit against the former directors of the company on account of the declaration by them of dividends in the years 1899 and 1900; and it further appears that it is not expedient nor for the interest of the company that a suit on that account should be brought against the said former directors.

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"THEREFORE RESOLVED, That the action of the Board of Directors in refusing to bring suit against the former directors of the company to recover dividends declared by them in the years 1899 and 1900 be approved and ratified;

"RESOLVED, That no suit shall be brought by the company or on its behalf to recover from the former directors of the company any of the said dividends declared by them, or to recover any damages or penalties on account of such declaration of dividends."

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And this defendant says that its directors and stockholders, in refusing to bring suit to recover the dividends declared by its former directors in the years eighteen hundred and ninety-nine and nineteen hundred, and in deciding that no suit should be brought by the company or on its behalf to recover from said former directors any of the dividends so declared, or to recover any damages or penalties on account of such declaration of dividends, acted in good faith and according to their best judgment for the benefit of this defendant, and did not act, and did not intend to act, for the benefit of said former directors who participated in the declaration of said dividends for the years eighteen hundred and ninety-nine and nineteen hundred, and that the refusal of the said directors to bring said suit and of the said stockholders to order and direct that the same should be brought was lawful and not in violation of the duty of either the said directors or stockholders to this defendant.

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ALL of which matters and things this defendant does aver to be true and does plead the same in bar of complainant's bill of complaint.

And this defendant, answering unto such parts of the complainant's bill as charged, that in the month of September, 1903, the complainant served upon this defendant and upon the persons who were then its directors a demand that this defendant, its officers and directors, take such proceedings as might be necessary to charge its former directors who declared the dividends in said bill complained of jointly and severally with the amounts so divided, withdrawn and paid out, and that this defendant, its officers and directors, refused the said demand, and that there was no valid reason why this defendant should not bring such suit, and that, in refusing to sue, its directors did not act or intend to act for the benefit of this defendant, but were acting and intended to act for the benefit of the said directors who had participated in the declaration of said dividends, and that such refusal to sue was unlawful and in violaton of the duty of the said directors of this defendant, says that a demand to bring suit against its former directors was in fact served by the complainant upon this defendant in September, 1903, a copy of which is hereto annexed as Exhibit A. That the Board of Directors of this defendant, consisting of M. J. Budlong, Philip T. Dodge, H. H. Vreeland, W. G. Henderson, Albert Taylor, Grant B. Schley, Jr., M. Gavin, 2d, W. O. Knudsen and H. W. Kyte, none of whom were in office at the time of the declaration of the dividends complained of, considered the said demand and referred the same to a committee of its members for investigation, which committee made a report thereon, a copy of which is hereto annexed as Exhibit B; that upon the coming in of said report the Board of Directors of this defendant examined the accounts, documents and statements showing the history and affairs of the company

in the years 1899 and 1900, and procured the advice of Robert H. McCarter, special counsel employed in said matter, not previously concerned in the business of the company; that, being satisfied that the report of the said committee was correct, said directors, acting in good faith and according to their best judgment for the best interests of this defendant, approved the same and adopted resolutions on the 29th day of September, 1903, a copy of which, marked Exhibit C, is annexed hereto; that a copy of said resolutions was thereupon transmitted to the complainant, and that the complainant, in January, 1904, addressed a demand to this defendant that it call a meeting of its stockholders pursuant to the provisions of said resolutions of September 29th, 1903, a copy of which demand is annexed hereto as Exhibit D; that thereupon said directors called a meeting of stockholders to consider complainant's said demand, at which meeting resolutions were passed, a copy of which is embodied in the foregoing plea. And this defendant says that its directors and stockholders, in refusing to bring suit to recover the dividends declared by its former directors in the years 1899 and 1900, and in deciding that no suit should be brought by the company or on its behalf to recover from said former directors any of the dividends so declared, or to recover any damages or penalties on account of such declaration of dividends, acted in good faith and for the benefit of this defendant, and denies that, either at the time when said directors refused to bring said suit, or at any other time, said directors knew that said dividends had been unlawfully declared and paid, or that there was no valid reason why this defendant should not bring suit to recover said dividends, and denies that, in refusing to bring such suit, the directors of this defendant acted and intended to act for the benefit of the directors who participated in the declaration of such dividends and not for the benefit of this defendant, and denies that the refusal of said directors

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to sue was unlawful or in violation of their duty to this defendant.

And this defendant prays the judgment of this court whether it ought to be compelled to make any further or other answer to said bill, and prays to be hence dismissed with its costs.

M. J. BUDLONG,
President.

[SEAL]

Attest:

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H. W. KYTE,
Secretary.

LINDABURY, DEPUE & FAULKS,
*Solicitors for and of Counsel with
Defendant Electric Vehicle Company.*

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STATE OF NEW YORK, }
COUNTY OF NEW YORK. } ss.:

The plea of the defendant Electric Vehicle Company was taken this fourth day of May, in the year one thousand nine hundred and five before me, a Master in Chancery of the State of New Jersey, under the common seal of the said corporation, as by its said seal hereto affixed appears.

LUTHER V. STRYKER, 10
Master in Chancery of New Jersey.

STATE OF NEW YORK, }
COUNTY OF NEW YORK. } ss.:

M. J. BUDLONG, of full age, being duly sworn, according to law, on his oath says that he is the president of Electric Vehicle Company, one of the defendants in the above entitled cause, which is about to file the foregoing plea, and that he is the agent of said company in this suit. Deponent further says that 20
the said plea is true in point of fact and is not interposed for delay, but in good faith.

M. J. BUDLONG.

Sworn and subscribed before me,
this 4th day of May, A. D., 1905.

LUTHER V. STRYKER,

Master in Chancery of New Jersey.

I certify that I have perused the complainant's bill 30
in the above stated cause, and that the foregoing plea about to be filed on behalf of the defendant Electric Vehicle Company is well founded in point of law.

R. V. LINDABURY,
Of Counsel.

EXHIBIT A.

To The Electric Vehicle Company:

George H. Day, President of the Electric Vehicle Company, and George H. Day, M. Toscan Bennett, M. J. Budlong, Philip T. Dodge, John Hone, A. D. Newton, Albert A. Pope, Isaac L. Rice and Fred Viewig, Directors of the Electric Vehicle Company—

10 THIS IS TO NOTIFY YOU, That the Board of Directors of the Electric Vehicle Company on the first day of April, eighteen hundred and ninety-nine, declared and thereafter paid a dividend on the outstanding preferred stock of the said company aggregating eighty-four thousand eight hundred dollars (\$84,800), and on the same day declared and thereafter paid a dividend on the outstanding common stock aggregating one hundred thousand dollars (\$100,000).

20 And that on the thirtieth day of June, eighteen hundred and ninety-nine, the directors of the said company then in office declared and thereafter paid a dividend on the outstanding common stock of the said corporation aggregating the sum of one hundred and forty thousand dollars (\$140,000).

30 And that on the thirtieth day of September, eighteen hundred and ninety-nine, the directors of the said corporation then in office declared and thereafter paid a dividend on the outstanding common stock of the said corporation aggregating the sum of one hundred and forty thousand dollars (\$140,000).

And that on the thirtieth day of December, eighteen hundred and ninety-nine, the directors of the said corporation then in office declared and thereafter paid a dividend on the outstanding common stock of the said corporation aggregating the sum of one hundred and forty thousand dollars (\$140,000).

40 And that on the fifteenth day of April, nineteen hundred, the directors of the said corporation then in office declared and thereafter paid a dividend on the

outstanding preferred stock of the said corporation aggregating one hundred thousand dollars (\$100,000).

THIS IS TO FURTHER NOTIFY YOU, That the dividends so paid by the said Board of Directors aggregating the sum of seven hundred and four thousand eight hundred dollars (\$704,800) were paid out of the capital of the said corporation, and not out of its surplus or net profits arising from its business. And that by the payment thereof the directors did divide, withdraw and pay to its stockholders a portion of its capital stock, and did reduce its capital stock in violation of the General Corporation Law of the State of New Jersey and the Stock Corporation Law of the State of New York, and of their duty as such directors. 10

THIS IS TO FURTHER NOTIFY YOU, That the directors in paying said dividends out of the capital of said company caused the company to borrow large sums of money and issue a large amount of bonds and pledge the company's property therefor, at a great loss to the company; that it would not have been necessary for the company to do this had it not been for the depletion of its capital caused by the payment of said dividends out of the company's capital, and the company has been damaged thereby in a large amount. 20

THIS IS TO FURTHER NOTIFY YOU, That I am the holder of two hundred shares of the preferred stock of the said corporation, and am likewise the holder of two hundred shares of the common stock thereof, and that the same stands in my name on the books of the said company. 30

I hereby demand that the said corporation, its officers and directors, shall forthwith take such proceedings as may be necessary, or as they may be advised, to charge the said directors who declared the said dividends, jointly and severally, as their liability may appear, with the amounts so divided, withdrawn and paid out, with interest, and collect the same by legal proceedings for the benefit of the said corpora- 40

tion, and also such damage in addition as may have accrued to said corporation by reason of the illegal payment of the said dividends.

I request that a meeting of the present Board of Directors of the said corporation be called immediately to consider my demand and to direct action to be taken upon it.

10 It is proper that I should call your attention to the fact that on August thirtieth, nineteen hundred and one, nearly two years ago, I brought suits in the Court of Chancery of New Jersey for an accounting in respect to the matters now complained of. To these suits the Electric Vehicle Company and some of its present directors were parties. These suits were dismissed, as you know, because I had not sufficiently excused myself from first demanding that your company bring the suits. I think I am justified in assuming that during these two years your company has
20 investigated the serious charges then and now made and that you will be prepared to give me an immediate reply to my present demand.

Dated, September 1, 1903.

RICHARD SIEGMAN,
Care Coult, Howell & Ten Eyck,
Prudential Building, Newark, N. J.,

or

McELHENY & BENNETT,
15 William St., New York City.

EXHIBIT B.

TO THE DIRECTORS OF THE ELECTRIC VEHICLE COMPANY:

Your committee appointed to report upon the application of Richard Siegman that suit be brought by your company against the former directors to recover the amount paid in dividends, report that they have examined the accounts, statements and records of the company at the time of the dividends and have inquired into the history of the affairs of the company from its organization until April, 1900, when the last dividend was paid. 10

The company was organized in New Jersey, September 27, 1897, to manufacture and sell vehicles propelled by electric storage batteries and as part of the plan purchased the stock, property and business of the Electric Carriage and Wagon Company, which was doing a profitable business. The price paid was \$5,000,000 in common stock and \$60,000 in preferred stock. The rest of the preferred stock, which, in all, was \$5,000,000, was afterwards sold from time to time for cash. An essential part of this purchase was a contract held by the said carriage company with the Electric Storage Battery Company, whereby this company obtained the right to use storage batteries under the Brush and other patents, which were essential to the business. 20

Business was carried on in 1898 with success, and the prospects seemed very good. In February, 1899, a sale was made of a plant constructed by the company in New York City for the manufacture and operation of electric vehicles in that city. This sale was made to a new company called The New York Transportation Company for a large sum of money, which was paid in cash, and as a part of the transaction a contract was made by this company with that company, assuring to this company a large income 30 40

from the business of the New York company, if successful, and soon after like contracts were made with several other companies with large capital operating in defined territories in other parts of the country. On March 7th, 1899, there were outstanding preferred shares amounting to one million and sixty thousand dollars, and common five million dollars, and a dividend was declared on that date of eight per cent. on preferred stock for the year 1899 and two per cent. on common, amounting to \$184,800. This dividend was fully warranted by the surplus accumulated. Soon after this competition was threatened by the Columbia Automobile Company, which was licensed by the battery company, and this led to a combination of the interests of the three companies whereby this company obtained exclusive advantages in the use of the patented battery, and received in cash from the battery company \$2,000,000, for which it issued to that company \$2,000,000 of its preferred stock, and also \$2,000,000 of its common stock, which was increased by that amount for the purpose.

This was in May, 1899, and in June following the company, to all appearances, was highly prosperous. It had purchased and then held 53,000 shares of the stock of the three transportation companies, each having a substantial capital, whose stock was selling readily at high and increasing prices. All these companies were dependent on this company for vehicles to be operated by them, which they were to purchase from this company by agreement. The stocks in these three companies represented an investment by this company of \$415,000, but were then worth at market rate about \$1,000,000. On the basis of the condition of the company then apparent, a dividend of two per cent. on common stock was voted June 13, 1899, and was fully warranted.

The business of manufacture was turned over to a new company called The Columbia and Electric Vehicle Company under an agreement whereby that company was guaranteed twenty per cent. profit above

cost of manufacture, and this company was given the exclusive right to its output. This company held half of its stock for which originally it was paid \$600,000, and afterwards the capital being increased to \$2,000,000, this company purchased \$400,000 more. This company, thus holding half the stock, was entitled to half the profits on all the orders.

The third and fourth dividends were declared September 16th and December 16th, 1899, each two per cent. on common stock, and on each of these dates it appeared that on a fair valuation of assets at that time there was a surplus sufficient to warrant the dividends. The last dividend was declared on March 20, 1900, and was of two per cent. on preferred stock, and amounted to one hundred thousand dollars. At that time the market value of the shares of the transportation companies held by this company had depreciated. There were, however, still large orders for vehicles placed by this company with the Columbia Electric Vehicle Company, exceeding in amount three millions of dollars. The interest of this company in the Columbia Electric Vehicle Company, which had cost one million dollars, was supposed to be of much greater value. The stock of that company was not on the market, and could not be tested by sales. The vehicles were still in demand, the orders being larger than ever, and a large profit on them seemed assured. There was a confident expectation that the batteries would be improved, and this has since been realized, although not in time for the machines built in 1900. It cannot be said that the dividend of one hundred thousand dollars declared on preferred stock on March 17, 1900, was not properly declared in view of what appeared at that time. It is now known that the whole enterprise upon which the company was embarked was unsound, but that was not suspected at that time. The confidence of the stockholders and directors in their enterprise during the year 1899 is evidenced by the market price of their stocks. The directors who were

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in office when the dividends were declared were large stockholders and continued to be such when the experience of the year 1900 demonstrated that the enterprise as originally projected was a failure. They still hold most of the stock they held then. There is no ground for the charge that dividends were declared to swell the price of shares, or for any improper purpose.

We report that in our judgment no action should be brought by the company, or on its behalf, against
 10 its former directors to recover back the dividends declared by them. Such an action, we think, could not be sustained, and if it could we think it would be unfair to said directors and detrimental to the best interests of the company. The company is now doing a prosperous, steadily increasing business along new and better lines, and its true interests lie in the prosecution and development of that business, rather than in the prosecution of lawsuits that would be likely to
 20 do it more harm than good.

M. J. BUDLONG,
 PHILIP T. DODGE.
 M. GAVIN, 2D.

EXHIBIT C.

The Board of Directors having examined the report of the committee appointed to consider the application of RICHARD SIEGMAN, and having heard the statements made by the committee, and having examined documents, accounts and statements showing the history and affairs of the company in the years eighteen hundred and ninety-nine and nineteen hundred; and the Board being satisfied from its examination that the dividends declared in these years were reasonably made in the light of what was known and believed at the time, and that the said dividends were declared fairly and in good faith, and that it is not for the interest of the company that suit should be brought against the Directors to recover said dividends, and the advice of counsel having been taken regarding the power and duty of this Board;

RESOLVED, That the demand of RICHARD SIEGMAN that suit shall be brought against the former directors of the company to recover the dividends declared by them in the years eighteen hundred and ninety-nine and nineteen hundred, be and the same hereby is denied, unless and until such suit shall be ordered by a majority, in interest of the stockholders, other than the said former directors, and that unless so ordered no suit shall be brought by the company or on its behalf to recover from the said former directors any of the dividends declared.

RESOLVED, That on the written demand of RICHARD SIEGMAN or of any other stockholder, the president shall call a special meeting of stockholders to consider the application of said Siegman, or of such other stockholders, for the bringing of such suit.

EXHIBIT D.

January 12, 1904.

TO THE BOARD OF DIRECTORS OF THE ELECTRIC VEHICLE
COMPANY.

10 Gentlemen:—We acknowledge receipt of the letter
from your president, dated September 29th, 1903, and
have been unable to reply earlier because of the neces-
sity of communicating with Mr. Siegman, who is in
Europe.

20 We note the offer of your Board to call a special
meeting of the stockholders to consider Mr. Siegman's
demand. While we believe that the body of the stock-
holders have no directive or advisory authority in the
matters which Mr. Siegman complains of, yet now, on
his behalf, we request that you call a meeting of the
stockholders to consider the demand made by him on
your Board. You will kindly send Mr. Siegman's
notice of the meeting to us.

Yours very truly,

COULT, HOWELL & TEN EYCK,
J. E. H.

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IN CHANCERY OF NEW JERSEY.

Between

RICHARD SIEGMAN,

Complainant,

and

RUDOLPH H. KISSEL ET ALS.,

*Defendants.**Order
Overruling
Plea.*

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This cause coming on to be heard on bill and plea, in the presence of James E. Howell, of counsel with the complainant, and Richard V. Lindabury, of counsel with the defendant, The Electric Vehicle Company, and the court having heard the arguments of counsel of the respective parties and being of opinion that the said plea is not good:

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IT IS, THEREUPON, on this fourteenth day of February, nineteen hundred and six, ordered that the said plea be and the same hereby is overruled with costs.

It is further ordered that the said defendant, The Electric Vehicle Company, shall file its answer to the complainant's bill in twenty days from this date, and if it fail to do so, the said bill shall be taken as confessed as against The Electric Vehicle Company.

Respectfully advised,

FREDERIC W. STEVENS,
V. C.

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IN CHANCERY OF NEW JERSEY.

Between

RICHARD SIEGMAN,

Complainant,

and

RUDOLPH H. KISSEL ET ALS.,

Defendants.

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Mr. Lindabury, for complainant.

Mr. Howell, for defendants.

STEVENS, V. C.

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The question raised by the plea has been very recently twice considered: first, by Vice Chancellor Garrison in *Groel v. United Electric Company* and then by Judge Lanning, in *Siegmán v. Electric Vehicle Company*. In both cases the plea was overruled. The case in the United States Circuit Court is identical with the one in hand. Were it not that an appeal is to be taken, I should not think it necessary to write an opinion. As it is, I shall state, as briefly as possible, the ground upon which I think the suit is sustainable.

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The complainant bases his case upon Section 30 of the Corporation Act, which provides that no corporation shall make dividends except from the surplus or net profits arising from its business, and that in case of a violation of the provision the directors under whose administration the same may happen "shall be jointly and severally liable at any time within six years after paying such dividend to the corporation and to its creditors in the event of its dissolution or

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insolvency." In *Appleton v. American Malting Co.*, 20 Dick., 375, the Court of Appeals construed this provision and held that it gave a remedy, not only in cases of insolvency or dissolution, but also in cases where the company was going and solvent.

The bill alleges that on April 1, 1889, the Board of Directors of the Electric Vehicle Company declared a dividend of eight per cent. on the preferred stock and two per cent. on the common stock, and that these dividends aggregated \$184,800, and that on June 30, 1899, they declared a further dividend of \$140,000. It then alleges that the defendant, Rudolph H. Kissel, a director of the company, at meetings of its directors, voted to declare said dividends, and that the same, to the knowledge of Kissel, were declared and paid, not out of the surplus or net profits, but out of capital. Under the decision above cited, Kissel thus became liable to make them good. Now the plea does not deny these allegations. What it sets up and all that it sets up is this: that after the declaration and payment of these dividends an entirely new board of directors was chosen; that such Board, after being requested to sue, appointed a committee to examine and report upon the matter; that the committee reported against bringing suit, and that the Board, after examination, approved the report and adopted a resolution that the company should not sue unless a majority in interest of the stockholders, other than the former directors so ordered; that at the demand of complainant a meeting of stockholders was called, at which complainant was represented, and that by a vote of 124,759 to 650 it was resolved by them that no just ground for suit against the former directors existed, and that, it not being expedient or for the interest of the company to bring suit, the action of the directors in refusing to do so was ratified and approved.

This plea does not deny that the dividends in question were declared and paid out of capital and that Kissel knew that they were, consequently, it does not

deny that there was a clear cause of action against Kissel for \$324,800. All that it sets up in excuse or justification for not bringing suit is that the present directors and a large majority of the stockholders now think that no just ground exists therefore and that it is not for the interest of the company to prosecute; in other words, admitting that, under the statute, Kissel is liable to refund the money, it is not thought fair to him or expedient for the company to enforce the liability. Now, as I understand the decisions, and as Judge Lanning, on an identical state of facts, decided, neither of these reasons is good as against dissenting stockholders.

In *Dunphy v. Travellers Newspaper Association*, 146 Mass, 495, the court said that it is not always best to insist upon all one's rights; that a corporation acting by its directors or by vote of its members may properly refuse to bring a suit which one of its stockholders believes should be prosecuted, and that in such case the will of the majority must control; but they add, "The court cannot interfere with the management of corporations in matters which are properly within their discretion, so long as their discretion is fairly exercised."

In *Corbus v. Alaska Treadwell Gold Mining Co.*, 187, U. S., 455, Mr. Justice Brewer says: "This court will examine the bill in its entirety and determine whether under all the circumstances the plaintiff has made such a showing of wrong on the part of the corporation or its officers and injury to himself as will justify the suit. The directors represent all the stockholders and are presumed to act honestly and according to their best judgment for the interest of all. Their judgment as to any matter lawfully confided to their discretion may not lightly be challenged by any stockholder or, at his instance, submitted for review to a court of equity. The directors may sometimes properly waive a legal right vested in the corporation in the belief that its best interests will be prompted by

not insisting on such right. They may regard the expense of enforcing the right or the furtherance of the general business of the corporation in determining whether to waive or insist upon the right. As said in *Dodge v. Woolsey*, 18 Howard, 344, "the circumstances of each case must determine the jurisdiction of a court of equity to give the relief sought."

In the *Corbus* case the relief was denied; in the *Dodge-Woolsey* case it was granted under the following circumstances: Woolsey was a shareholder in the Branch Bank of Cleveland. The bank was incorporated under an act of the State of Ohio, which provided that it should be taxed in a certain mode. It was subsequently sought to impose a greater tax. The contention on behalf of the bank was that the first act constituted a contract on the subject of taxation which the subsequent legislation impaired, and such was the view taken by the Supreme Court. The directors, it was alleged in the bill, had been requested by Woolsey to take measures by suit or otherwise to assert the franchises of the bank against the collection of the unconstitutional tax, and, while admitting the illegality of the tax, had refused, "because of the many obstacles in the way of testing the law in the courts of the State." Although the case was devoid of any element of *ultra vires*, fraud or oppression, the Supreme Court held that the suit was maintainable; in other words, the constitutional right to protection against the imposition of a further tax being adjudged, the stockholder was permitted, as the representative of the company, to override the judgment of the directors on the question of the expediency of testing the right in the courts.

This case appears to me to control the decision of the case in hand. We must, as the pleadings stand, regard the right of recovery against Kissel to be clear, for, as I have said, it is expressly averred in the bill that he knew that the dividends were all paid out of capital, and notwithstanding this knowledge, voted

for their payment. This makes a perfectly clear case against him, however the matter may stand as to the others. The fact that a committee of the directors may have thought that as to the liability of the directors generally in office when the dividends were declared there might be some doubt or question is immaterial; for taking the facts to be as alleged by the bill, and not denied by the plea, this doubt does not extend to Kissel. Then, the only other ground assigned for
 10 not suing is found in the bare statement that suit is inexpedient. But if the circumstances of each case are to determine the question of jurisdiction, then, the right being clear, it ought to appear why it is inexpedient. If Kissel be solvent (and there is no intimation of insolvency), and if the right to recover so large a sum (\$324,000) be undoubted, some good reason should be given for not suing. But no reason
 20 whatever is given. The case, therefore, as it now stands, must be regarded as falling rather within the ruling of *Dodge v. Woolsey*, 18 How. (U. S.), 344, than within that of *Hawes v. Oakland*, 104, U. S., 450, and *Corbus v. Mining Co.*, 187, U. S., 455.

IN CHANCERY OF NEW JERSEY.

Between

RICHARD SIEGMAN,

Complainant,

ELECTRIC VEHICLE COMPANY

and RUDOLPH H. KISSEL,

*Defendants.**On Bill, &c.*

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NOTICE OF APPEAL FROM ORDER OVER-
RULING PLEA.

Electric Vehicle Company, one of the defendants
in the above entitled cause, hereby appeals from an
order made in the said cause on the fourteenth day
of February, 1906, overruling the plea of the said
defendant to the complainant's bill of complaint 20
therein and from the whole and every part thereof,
to the Court of Errors and Appeals in the last resort
in all causes.

Dated February 20, 1906.

LINDABURY, DEPUE & FAULKS,

*Solicitors for and of counsel with**Defendant Electric Vehicle Co.*

I conceive there is a good cause for an appeal in
the above stated cause.

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R. V. LINDABURY,

*Of Counsel with Defendant**Electric Vehicle Co.*

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NEW JERSEY COURT OF ERRORS AND
APPEALS.

10	<i>Between</i> RICHARD SIEGMAN, <i>Complainant-Appellee,</i> and ELECTRIC VEHICLE COMPANY and RUDOLPH H. KISSEL, <i>Defendants-Appellants.</i>	}	<i>On Bill, &c.</i>
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PETITION OF APPEAL OF ELECTRIC VEHICLE
COMPANY FROM ORDER OVER-
RULING PLEA.

*To the Honorable the Court of Errors and Appeals
in the last resort in all causes:*

The petition of Electric Vehicle Company, the ap-
pellant in the above stated cause, respectfully shows
that your petitioner finds itself aggrieved by an order
made in the Court of Chancery by his Honor William
J. Magie, Chancellor of New Jersey, bearing date the
fourteenth day of February, in the year one thousand
nine hundred and six, in a cause wherein the said
Richard Siegman was complainant, and the said Ru-
dolph H. Kissel and your petitioner were defendants,
in this respect: that the said order overrules the plea
theretofore filed by your petitioner to the bill of com-
plaint filed in the said cause by the said complainant.
And your petitioner humbly appeals from the said
order and the whole thereof upon the ground that the
same is erroneous and contrary to equity, for that the
said plea should have been sustained and a decree

made adjudging that the said plea was a sufficient answer to the complainant's bill of complaint, and that this defendant was not bound further to answer the complainant's said bill of complaint.

Your petitioner therefore prays that the said order of the Chancellor may be reversed, set aside and for nothing holden, and that your petitioner may have such further and other relief in the premises as to this honorable court shall seem meet.

LINDABURY DEPUE & FAULKS,

Solicitors for Appellant.

R. V. LINDABURY,

Of Counsel with Appellant.

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NEW JERSEY COURT OF ERRORS AND
APPEALS.

10 	<i>Between</i> RICHARD SIEGMAN, <i>Complainant-Appellee,</i> and ELECTRIC VEHICLE COMPANY, <i>Defendant-Appellant.</i>	} <i>Answer.</i>
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THE ANSWER OF THE ABOVE NAMED
 APPELLEE TO THE PETITION OF
 APPEAL OF ELECTRIC VEHICLE
 COMPANY, THE ABOVE
 NAMED APPELLANT.

30 This appellant, not acknowledging all or any of the
 matters which in the said petition of appeal are con-
 tained to be true, for answer thereto nevertheless says
 and admits that a decree was on the fourteenth day
 of February, nineteen hundred and six, made and
 entered in the Court of Chancery in the cause for that
 purpose mentioned in the said petition as is therein
 stated, but as to the substance and form thereof this
 appellee prays to refer thereto when the same shall be
 produced, and this appellee is advised and believes
 that the said decree is agreeable to equity, and he
 prays that the same may be affirmed with costs to be
 adjudged to him.

COULT & HOWELL,
Solicitors.

