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In summary, this may be ventured in respect to the right of the beneficiary to sue in Montana. The incidental beneficiary has no cause of action against the promisor. The creditor beneficiary is allowed a direct right except in the case of a grantee assuming a mortgage debt. Although there are no general pronouncements by our Court that the donee beneficiary has a direct suit against the promisor, and in spite of the language in early decisions and that of *Martin v. American Surety Co.*, it is believed that the Supreme Court of Montana is substantially committed to the doctrine that the donee beneficiary has a direct suit against the promisor. The donee beneficiary cases passed upon by the Supreme Court have involved "sole" beneficiaries of insurance policies; sub-contractors, laborers and materialmen under provisions of a surety bond; and cases of promises for the benefit of a child. Though there may be historical reason, there is no logical reason for preferring these to other donee beneficiaries. The language of the code is broad enough to permit recovery by any donee beneficiary. In view of the progress already made, the expectation seems warranted that, as occasion arises, other types of donee beneficiaries will be permitted a direct suit, in line with the growth of the law elsewhere in America.

—Carl Burgess.

**CORPORATIONS: LIMITATIONS UPON THE RIGHT OF
A STOCKHOLDER TO BRING A REPRESENTATIVE
SUIT IN MONTANA**

Does the complaining stockholder always have to petition the other stockholders for redress as a condition of his right to bring a derivative suit on behalf of the corporation? Such seems to be the conclusion of a recent A. L. R. Annotation,¹ and at least one Montana case, which goes so far as to say that

¹Annotation in 72 A. L. R. 621 to *Caldwell v. Eubanks* (1930) 326 Mo. 185, 30 S. W. (2d) 976. The annotator apparently concludes that there are only two situations in which application to the stockholders as a body will be excused: one is where the majority stockholders were in league with the wrongdoers, and the other where there is shown lack of time. In support of this proposition he cites every imaginable case on the subject, but it is contended and sought to be shown in this article that his theory is not supported by the better authority, and that it is subject to the same criticism as is herein made of the dictum in *Allen v. Montana Refining Co.* (1924) 71 Mont. 105, 227 P. 582. Rather, it would be more commensurate with sound policy to adhere to the rule as set out in *Continental Securities Co. v. Belmont* (1912) 206 N. Y. 7, 99 N. E. 138, 51 L. R. A. (N. S.) 112 and the exhaustive annotation thereto.

the complainant must first ask the majority stockholders to elect a new board of directors before he may institute a suit himself.²

The answer to the question posed cannot readily be put in one all inclusive statement usable for every possible situation. This is borne out by the wide variety of results which have been obtained in the many derivative suits which have been brought in the Montana court,³ as well as those in other jurisdictions,⁴ and the several attempts by the text writers to state a workable doctrine, which tend for the most part to be as conflicting as the decisions.⁵

It must be remembered that the existence of a right to bring a derivative suit at all depends upon there being at the outset a cause of action upon which the corporation itself might sue if the corporate officials were properly performing their functions.⁶ The following analysis shows the types of complaint that may be the basis for an attempted derivative suit by a stockholder:

A. When the act of which he complains is that of the directors and is within their discretion and power to per-

²Dictum in *Allen v. Montana Ref. Co.*, *supra* note 1; and see *State Bank v. Sheridan County* (1924) 72 Mont. 1, 230 P. 1097; *Cobb v. Lee* (1927) 80 Mont. 328, 260 P. 722, in which the *Allen* case is cited as *leading* authority on this point. But what was said in the *Allen* case about stockholder's representative suits was purely dictum, the case really turning on lack of jurisdiction in the Montana Court to enter a binding decree against a foreign corporation which calls for affirmative action in the internal affairs of the corporation. It is the suggestion of the court that even in a case involving fraud, application must be made to the majority stockholders as a condition to the right to sue representatively which is questioned herein.

³*Cf.* the cases *supra* note 2 with the following cases that apparently considered no demand upon the stockholders as a body to be necessary, for it was not mentioned in them, even by way of dicta. However, it is not clear that the court intended to state all the conditions precedent to bringing a representative suit in any of these cases: *Gerry v. Bismarck Bank* (1897) 19 Mont. 191, 47 P. 810; *Forrester v. B. & M. Min. Co.* (1898) 21 Mont. 544, 55 P. 229; *McConnell v. Combination M. & M. Co.* (1904) 30 Mont. 239, 76 P. 194, 104 Am. St. Rep. 703; *Brandt v. McIntosh* (1913) 47 Mont. 70, 130 P. 413; *Kleinschmidt v. American Min. Co.* (1914) 49 Mont. 7, 139 P. 785; *Deschamps v. Loisel* (1915) 50 Mont. 565, 148 P. 335.

⁴*Cf.* *Hawes v. Oakland* (1881) 104 U. S. 450, 26 L. Ed. 827; *Johns v. McLester* (1902) 137 Ala. 283, 34 So. 174, 97 Am. St. Rep. 27, and annotation; *Caldwell v. Eubanks*, *supra* note 1; *Continental Securities Co. v. Belmont*, *supra* note 1; and see note, 6 U. CHI. L. R. 269, 275.

⁵*Cf.* 13 FLETCHER, CYCLOPEDIA OF CORPORATIONS (Rev. ed. 1932) §§5939 to 5965; STEVENS, CORPORATIONS (1936) §162; 4 COOK, CORPORATIONS (8th ed. 1923) §§740 to 759; *Corporations*, 14 C. J. p. 934; 18 C. J. S. *Corporations* §559 *et seq.*; 6 U. CHI. L. R. 269.

⁶*Hawes v. Oakland*, *supra* note 4; and see 13 FLETCHER, *supra* note 5, §§5939, 5944; 40 WORDS AND PHRASES (Perm. ed. 1940) p. 194.

form, his complaint being based upon disagreement over the way things are run, clearly the complaining stockholder should be entirely out of court, for in the absence of fraud or negligence, his only recourse is to convince the other stockholders that they ought to exert their influence on the existing directors or elect a new board.⁷

B. Of a similar nature are those cases where there is a recognized corporate right of action, but the situation is such that the wrong complained of may be cured by a vote of the stockholders.⁸

C. However, where the act complained of was so wrongful in nature that the majority stockholders' vote could not cure it, application to the majority should not be necessary when the directors refuse to act.⁹

D. Qualifying the rule in C are those cases in which there is a recognized cause of action, but expediency and common sense dictate that it be disregarded.¹⁰

The Montana Court fails to recognize these distinctions in the *Allen* case when it says:

“ . . . if it be a fact that the directors were acting contrary to the best interests of the corporation, manifestly their duty was to oust the recalcitrant directors and elect members who will promote and protect the company's interests

⁷The test usually applied by the courts is to distinguish between wrongs void or voidable to determine whether they may be “ratified or confirmed” by the body of stockholders. See 6 U. CHI. L. R. 269, 270, for a discussion on this point and a proposal to “. . . define capacity to ratify in terms of possibility of a choice open to the majority to sue or not to sue.” Also see the annotation to *Continental Securities Co. v. Belmont*, in 51 L. R. A. (N. S.) 113. It might be said that there really is no right to bring a representative suit when the act complained of can be confirmed by the majority of the stockholders, because whatever the majority does, it is out of the complainant's hands. Even their silence might raise an inference of acquiescence to the director's action.

⁸An example is the situation that arises when the directors vote themselves overly large salaries. Since the majority of the stockholders may wish to confirm this action, they should be given an opportunity to do so before the complaining stockholder is allowed to air his grievance in court. See 13 FLETCHER, *supra* note 5 §§5821, 5822.

⁹Or the facts show that it would be useless to apply to them. 4 COOK, *supra* note 5, 3244. Many authorities have termed these *ultra vires* acts.

¹⁰For example, consider a corporate cause of action for damages against a labor union, or a situation in which the desirability of retaining the services of one or more of the defendants far outweighs the possible pecuniary gain to the corporation. The majority of the stockholders should be given an opportunity to pass upon the wisdom of the director's action before allowing the complainant to sue. However, where “. . . election not to sue would entail the surrender of valuable corporate rights without commensurate advantage to the corporation . . .” application to the majority stockholders should not be necessary. 6 U. CHI. L. R. 269, 271, 273.

. . . it was incumbent upon the plaintiffs that they appeal to the stockholders and that they be denied relief before they could institute this action; . . .'¹¹

The court applies literally the formula generally thought controlling: "a stockholder must exhaust all means of redress within the corporation itself before bringing an action in the interest of the corporation." Indeed, if such a formula is carried far enough, none of the distinctions made *supra* as to the nature of the stockholder's complaint *can* be recognized and he will have difficulty in getting before the court.¹² An examination of the annotation in 51 L. R. A. (N. S.) 113 will show that it was in reality an unfortunate accident that this general formula was ever applied to cases of type C. The formula's original purpose was to check disgruntled minorities from running to court over disagreements on policy (see types A, B, and D), whereas later courts seized on this handy aphorism and applied it to all derivative suits without distinction, a result which is without reason and which has led to much of the confusion in this field today.¹³

By far the greater number of cases involving stockholder's derivative actions that get into court come under type C,¹⁴ and the persuasiveness of the line of reasoning used, when the court requires the complaining stockholder to apply for redress to the majority stockholders as a condition to his right to sue, is entirely dependent upon the effectiveness of any remedies available to the majority stockholders. As to this, it is necessary to determine what power is reserved to the stockholders by the Montana Code. The "relief" which the ordinary individual stockholder may get by application to his fellow stockholders is limited to election of a new board of directors,¹⁵ removal of an objectionable director,¹⁶ or institution of a representative suit by

¹¹71 Mont. at p. 123, 227 P. at p. 537. See *supra*, note 2.

¹²There is a class of cases, distinguishable from those under consideration, where application to both the directors and the stockholders is excused by all courts, and that is where both the directors and the majority stockholders are shown by the facts to have been the wrongdoers. See *supra* note 1. We may eliminate this class from our discussion, for, ". . . the law . . . does not demand a request that a person or corporation sue him or itself, nor require the doing of any useless thing, as (a) prerequisite to the accrual of a right of action. . ." *Forrester v. B. M. Min. Co.* (1898) 21 Mont. 544, 549, 55 P. 229, 231.

¹³*Cf.* cases cited *supra*, notes 2 and 3 with the annotations cited *supra*, note 1.

¹⁴*Cf.* cases collected in 51 L. R. A. (N. S.) 113; 72 A. L. R. 621; *Corporations*, 14 C. J. p. 934; and 18 C. J. S. *Corporations* §559.

¹⁵R. C. M. 1935, §5937. It requires a majority vote to elect a director.

¹⁶R. C. M. 1935, §5940. A director may be removed by two-thirds vote of the stockholders.

them on behalf of the corporation,¹⁷ in the absence of charter or by-law provisions reserving extra-ordinary and special powers of control in the stockholders. The governing body of private corporations in Montana is the board of directors thereof, and this includes the power to institute suits in the corporate name.¹⁸

It should be recognized, particularly in Montana, that to require election of a new board of directors would avail the complaining stockholder nothing, considering the length of time and expense involved in calling a general stockholder's meeting. For this reason one writer seems to have come to the conclusion that there need be no request to the stockholders at all as a condition to bringing a derivative suit based upon a recognized corporate cause of action. He says:

"... The fact . . . that the shareholders in meeting assembled cannot control the discretion of the directors in bringing . . . suit; that the remedy of refusing to re-elect them involves delay, and involves the assumption that a minority of the shareholders can by the election control such a suit; that irreparable injury or the vesting of great financial interests may occur in the meantime; and that laches may arise as a bar to the stockholder's suit—has settled the rule that the stockholder's request to the corporate directors to institute the suit is sufficient."¹⁹

But, even if the minority stockholder can persuade the majority to act, it only serves to delay an action which unquestionably should be started immediately.²⁰ The course of the Montana decisions up to the *Allen* case seem to have recognized this fact—at least none of them went so far as to require application

¹⁷Once it is recognized that a minority stockholder has this right to bring a representative suit, the majority stockholders should also have the right, should they initiate it, in spite of *Brandt v. McIntosh* (1913) 47 Mont. 70, 130 P. 413, which held that the complainant must allege that he was a minority stockholder before he was entitled to sue by way of a derivative suit. Such holding can only be justified by the limited facts present in that case. Cf. 6 U. CHI. L. R. 269, where it is suggested that the majority might hire counsel and sue *directly* in the corporate name, but citing no authority.

¹⁸R. C. M. 1935, §5933. It will readily be seen from a perusal of the statutes that Montana law grants the stockholder little managerial power other than this indirect power to refuse to re-elect a recalcitrant director. As to the ineffectiveness of this power, see *Continental Securities Co. v. Belmont*, *supra* note 1, 99 N. E. at p. 141, where it is said, ". . . any action by them relating to the details of the corporate business is necessarily in the form of an assent, request, or recommendation. Recommendations by a body of stockholders can only be enforced through the board of directors. . . ."

¹⁹4 Cook, *supra* note 5, at p. 3242.

²⁰See note, 6 U. CHI. L. R. at p. 276, where it is said, ". . . The insistence on a demand, moreover, tends only to postpone not prevent litigation. . . ."

to the stockholders where there was a recognized corporate cause of action, nor did they intimate its necessity by way of dicta.²¹ Consequently, the natural result of adherence to the rule of the *Allen* case is to hog-tie individual stockholders, and facilitate management without corresponding ownership, thus making it easier for the directors and managers to avoid being held accountable for their acts even including positive frauds. There seems to be nothing in the common law or under the modern law of corporations to call for such a rule.²²

It is submitted, then, that the court when deciding the *Allen* case, should have followed the *Belmont* case with greater particularity. The rule of the *Belmont* case, and it was so quoted verbatim in the *Allen* case,²³ is as follows:

“It is the governing body or bodies of a corporation with power to enforce a remedy to whom the complaining stockholders must go with their demand for relief. The governing body of corporations in this state . . . is the board of directors. A complaining stockholder must go to such board for relief before he can bring an action, unless it clearly appears by the complaint that such application is useless. If the subject matter of the stockholder’s complaint is for any reason within the *immediate control, direction, or power of confirmation* of the body of stockholders it should be brought to the attention of such stockholders for action, before an action is commenced by a stockholder, unless it clearly appears by the complaint that such application is useless.”²⁴ (Italics supplied).

This rule was promulgated in the decision of a suit for an accounting for fraudulently and illegally issued stock and for the dividends paid thereon, against some of the corporate directors. The Court held that, since such issue could not be cured or ratified by any number of the stockholders, the complainant had

²¹*Supra* note 3. The influence of *Hawes v. Oakland*, *supra* note 4, seems to have been considerable in the decision of the *Allen* case, and this is unfortunate, in view of the interpretation which has been placed on the *Hawes* case in the years since it was decided. Most courts seem to have lost sight of the fact that the strictness of the rule adopted there, as well as the rule of procedure governing the Federal courts (Federal Equity Rule 23), was designed to prevent the institution of suits in the Federal courts based on a fictitious diversity of citizenship, and not designed to require application to the majority stockholders in all cases.

²²*Cf.* *Greenwood v. Union Freight Ry. Co.* (1881) 105 U. S. 13, 26 L. Ed. 961; *Brewer v. Boston Theater* (1870) 104 Mass. 378; *Shaw v. Staight* (1909) 107 Minn. 152, 119 N. W. 951, 20 L. R. A. (N. S.) 1077; *Gregory v. Patchett* (1864) 33 Beav. 595; and see 4 *COOK*, *supra* note 5, 3242; 13 *FLETCHER*, *supra* note 5, §5964.

²³71 Mont. at p. 123, 227 P. at p. 587.

²⁴*Continental Securities Co. v. Belmont*, *supra* note 1, 99 N. E. at p. 142.

no duty whatever to appeal to them, before instituting a representative suit. Close study of the quoted rule will show substantial conformity to the analysis made *supra*, and it seems that the rule advanced is supported by both better reasoning and authority.³³ The Montana court should adopt it for future cases, the situation being approached from the standpoint of what would be equitable to both ownership and management, rather than what seems to be a questionable tendency to favor management by placing unnecessary conditions on the right of a stockholder to institute a representative suit.

—Grover C. Schmidt, Jr.

DAMAGES: THE DOCTRINE OF REMITTITUR IN MONTANA

After finding by the Supreme Court¹ that defendant is entitled to a new trial because of excessive damages² the doctrine of remittitur permits the court to compel him to forgo that right provided that plaintiff accepts a reduced verdict.³ The doctrine came into use as a means of eliminating the expense and dilatory process of repeated trials and in many instances there can be

³³4 Cook, *supra* note 5, §740 *et seq.*

¹Remittitur is also applied by the trial courts, and its use therein is universally upheld. *Bull v. Butte Electric Railway Co.* (1924) 69 Mont. 529, 223 P. 514; *Northern Pacific Railway Co. v. Herbert* (1885) 116 U. S. 642, 29 L. Ed. 755, 6 S. Ct. 590; *Arkansas Cattle Co. v. Mann* (1888) 130 U. S. 69, 39 L. Ed. 854, 9 S. Ct. 458. No attempt is made in this comment to deal with this aspect of the doctrine.

²Though *increscitur* (increasing amount of the damages) is much less frequently indulged in than *remittitur*, it has been followed in some jurisdictions. *McCORMICK, DAMAGES* (1935) §19 at p. 82 and cases there cited. In *Dimick v. Schiedt* (1935) 93 U. S. 474, 55 S. Ct. 296, 79 L. Ed. 603, 95 A. L. R. 1150, the Supreme Court of the United States prohibited *increscitur* in any event. Mr. Justice Stone wrote a strong dissenting opinion, which was concurred in by three other Justices, in which he pointed out that it is altogether inconsistent on principle to utilize *remittitur* without recognizing *increscitur*.

³The doctrine is most frequently stated in terms of the plaintiff's acceptance of a reduced verdict in lieu of demanding a new trial, whereas the defendant is compelled to accept the judgment of the appellate court. 20 R. C. L., *New Trial*, §99; 54 C. J. REMITTITUR p. 108. Compulsory remittitur has been denied in both this country and England. *Kennon v. Gilmer* (1885) 5 Mont. 257, 5 P. 847; (1888) 131 U. S. 22, 33 L. Ed. 110, 9 S. Ct. 696. This decision was followed in *Kennon v. Gilmer* (1889) 9 Mont. 108, 22 P. 448. See also, *Watt v. Watt* (1905) House of Lords, A. C. 115, 2 Am. & Eng. Cases 672; *McCORMICK, DAMAGES* (1935) §19; 4 *SEDGWICK, DAMAGES* (9th ed. 1912) §1330.