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**Corporations—Stockholder's Action for Declaration of Dividends—  
Failure to Join Directors**

One of the problems facing a stockholder wishing to bring a suit for the declaration of dividends has been to find a forum in which the suit could be brought. In the past such a suit required that a majority of the directors be made parties defendant.<sup>1</sup> With the advent of huge corporations this became an almost impossible task, since it was likely that the board of directors would be made up of men from various states. It has been suggested that suits prosecuted against the directors in their various jurisdictions, holding all of the judgments in abeyance until the final judgment was secured, would produce the desired results.<sup>2</sup> The multiplicity of suits involved, however, makes this plan undesirable. The only alternative, waiting until all of the directors are assembled within one jurisdiction, and then obtaining service of process before they escape, is too uncertain to be practicable.

In *Kroese v. General Steel Castings Corp.*,<sup>3</sup> a solution was laid down which is simple and shows the modern bench's ability to provide a method whereby the ends of justice may be served. Action was brought by the plaintiff, a minority stockholder and a resident of New York, to compel the declaration and payment of accumulated dividends on preferred stock. The federal court decided the case on Delaware law as it would be interpreted by a Pennsylvania court.<sup>4</sup> When the suit was first instituted against the corporation, none of the directors were named as parties defendant; but upon the ruling of the district court that a majority of the board of directors were indispensable parties, three of the twelve members were served. The plaintiff claimed that there was no one state or federal jurisdiction in which a majority could be served. The district court held that the action could go no further without personal jurisdiction over a majority of the directors.<sup>5</sup> It was alleged, and for the purposes of this appeal taken to be true, that 92 per cent of the no-par common shares were held by four large users<sup>6</sup> of the corporation's products. Also outstanding were 100,000 shares of \$6.00 cumulative preferred no-par stock. Dividend arrearages on the cumulative preferred no-par stock amounted to \$57.75 per share when

<sup>1</sup> BALLENTINE, CORPORATIONS §234 (Rev. ed. 1946); 11 FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §5326 (Perm. ed. 1932).

<sup>2</sup> Schuckman v. Rubenstein, 164 F. 2d 952 (6th Cir. 1947); see 61 HARV. L. REV. 1253 (1948).

<sup>3</sup> 179 F. 2d 760 (3rd Cir. 1950), cert. denied, 70 Sup. Ct. 1026 (1950); see 98 U. OF PA. L. REV. 753 (1950).

<sup>4</sup> The corporation, with its principal place of business in Pennsylvania, was incorporated under the laws of Delaware.

<sup>5</sup> *Kroese v. General Steel Castings Corp.*, 9 F. R. D. 273 (E. D. Pa. 1949).

<sup>6</sup> American Steel Foundries Corporation, 38.33%; Baldwin Locomotive Works, 33.37%; American Locomotive Company, 13.14%; and Pullman Incorporated, 8.54%.

the complaint was filed. The corporation was in excellent financial condition.<sup>7</sup> In holding that the directors were not indispensable parties to the action, the court of appeals stated that a judgment against the corporation compelling the payment of dividends could be enforced by a judgment against the property of the corporation.

An action for the declaration of dividends is of an equitable nature.<sup>8</sup> In general, the courts will not interfere with the discretion of the directors in declaring dividends,<sup>9</sup> but there may be a contractual relationship which will strictly limit this discretion.<sup>10</sup> A corporation, however, is operated for the benefit of the stockholders; when there is an abuse of this discretion (i.e., the directors act in bad faith, through fraudulent motives, or for the benefit of others than the stockholders as a whole) a court of equity will compel the directors to declare a dividend.<sup>11</sup> In the past the action has been thought of, erroneously it seems, as one in personam against the directors for misconduct.<sup>12</sup> The duty co-relative to the stockholder's right rests on the corporation rather than on the directors as individuals. A noted text writer, in pointing out that the action is neither derivative nor for a wrong done to the corporation, states that the right to be enforced is against the corporation.<sup>13</sup> The wrong in failing to declare dividends is that of the corporation, acting as it must, through its board of directors, which serves most nearly in the capacity of principal, and consequently as the alter ego of the corporation.<sup>14</sup>

Is the judgment for a stated sum in the form of "judgment dividends" collectible from the corporation directly as in the case of a creditor? The scant authority seems to be in disagreement. A nega-

<sup>7</sup> On December 31, 1947, the corporation had a net worth of \$28,000,105; a capital surplus of \$4,133,449; an earned surplus of \$13,410,080; net current assets of \$12,114,409; and a ratio of current assets to current liabilities of seven to one.

<sup>8</sup> *BALLENTINE, CORPORATIONS* §234 (Rev. ed. 1946); 11 *FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS* §5326 (Perm. ed. 1932); 10 *ROCKY MOUNTAIN L. REV.* 201 (1938).

<sup>9</sup> *Crocker v. Waltham Watch Co.*, 315 Mass. 397, 53 N. E. 2d 230 (1944); *BALLENTINE, CORPORATIONS* §232 (Rev. ed. 1946); 11 *FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS* §5325 (Perm. ed. 1932).

<sup>10</sup> *New England Trust Co. v. Penobscot Chemical Fiber Co.*, 50 A. 2d 188 (Me. 1946).

<sup>11</sup> *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668 (1919).

<sup>12</sup> *Schuckman v. Rubenstein*, 164 F. 2d 952 (6th Cir. 1947); *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N. W. 668 (1919); *NY PA NJ Utilities Co. v. Public Service Commission*, 23 F. Supp. 313 (1938).

<sup>13</sup> *BALLENTINE, CORPORATIONS* §234 (Rev. ed. 1946) (in same section writer also states that directors should be joined as parties defendant).

<sup>14</sup> See *BALLENTINE, CORPORATIONS* §42 (Rev. ed. 1946). The courts in analogous situations have held the corporation liable for crimes and torts committed through its agents. *Crimes: Overland Cotton Mill Co. v. People*, 32 Colo. 263, 75 P. 924 (1904); *State v. Salisbury Ice & Fuel Co.*, 166 N. C. 366, 81 S. E. 689 (1914); *State v. The Rowland Lumber Co.*, 153 N. C. 610, 69 S. E. 58 (1910). *Torts: Nims v. Mt. Hermon Boys School*, 160 Mass. 177, 35 N. E. 776 (1893); *Hairston v. Atlantic Greyhound Corp.*, 220 N. C. 642, 18 S. E. 2d 166 (1942).

tive answer can be inferred from those cases requiring that directors be joined as parties defendant.<sup>15</sup> The *Kroese* case holds it collectible from the corporation,<sup>16</sup> pointing out, analogously, that when a creditor receives a judgment, some action is required by the board of directors, officers, or agents of the corporation if it is to comply with the judgment. These acts, however, such as passing a resolution for the payment of the debt, entering payment on the corporate books, and the physical tendering of payment, are purely ministerial. Such ministerial acts do not render the judgment more valid. If the ministerial acts are not performed, the judgment creditor can issue an execution, levy the same upon and sell the property of the corporation to the same extent as if it were a natural person.<sup>17</sup> In like respect if the directors failed to perform the proper ministerial acts necessary to declaring dividends, the stockholder could, through equity, sequester the property of the corporation or have a receiver appointed to carry out the judgment of the court.<sup>18</sup> It is not clear from the instant case whether each stockholder could obtain a judgment against the corporation for his share of dividends in the event the directors failed to declare a dividend as a result of the court's judgment. If the directors failed to declare a dividend, the appointment of a receiver would eliminate a multiplicity of suits, and thus best carry out the judgment of the court.

Indispensable parties are those whose interests are such that no decree can be rendered which will not affect them, and therefore the court cannot proceed until they are brought in.<sup>19</sup> The directors are not indispensable parties to an action for a declaration of dividends. They are required to take no formal action whatsoever in compliance with the judgment of the court. The judgment is sufficient to establish the rights of the stockholder to dividends.

One other case, *Schuckman v. Rubenstein*,<sup>20</sup> has been decided on this same point.<sup>21</sup> Only two of the nine members of the board of directors

<sup>15</sup> See *Schuckman v. Rubenstein*, 164 F. 2d 952 (6th Cir. 1947); *Gesell v. Tomahawk Land Co.*, 184 Wis. 537, 200 N. W. 550 (1924); *NY PA NJ Utilities Co. v. Public Service Commission*, 23 F. Supp. 313 (1938).

<sup>16</sup> "The duty of a corporation to pay dividends then and there has been imposed by the judgment of the court. . . . The situation becomes in substance the same as that in which any corporate creditor sues the enterprise in the corporate name to recover from it what it owes him. . . ." *Kroese v. General Steel Castings Corp.*, 179 F. 2d 760, 764 (3rd Cir. 1950).

<sup>17</sup> 10 FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §4741 (Perm. ed 1932).

<sup>18</sup> *Kroese v. General Steel Castings Corp.*, 179 F. 2d 760 (3rd Cir. 1950).

<sup>19</sup> *American Ins. Co. v. Bradley Mining Co.*, 57 F. Supp. 545 (N. D. Cal. 1944); *MacBryde v. Burnett*, 41 F. Supp. 661 (D. Md. 1941); *McRanie v. Palmer*, 2 F. R. D. 479 (D. Mass. 1942); *McINTOSH, NORTH CAROLINA PRACTICE AND PROCEDURE IN CIVIL CASES* §209 (1929). See *FED. R. CIV. P.* 19 (b); 3 MOORE, *FEDERAL PRACTICE* 2150 (2d ed. 1948).

<sup>20</sup> 164 F. 2d 952 (6th Cir. 1947).

<sup>21</sup> Three other cases, while not decided on this same point, raise this question. *O'Neill Co. v. O'Neill*, 108 Ind. App. 116, 25 N. E. 2d 656 (1940) (action to

were properly before the court. The court held that at least a majority of the board of directors were indispensable parties defendant. By dictum, however, the court indicated that the plaintiff might have a good cause of action against the corporation alone to recover dividends *already declared* without the joining of a majority of the board of directors. This indicates that once the discretion of the directors has been exercised and dividends declared, the courts can then enter a judgment against the corporation for the payment of the declared dividends. Their reasoning is based on the rule that it is within the discretion of the directors to declare dividends; and they must, therefore, be before the court in order that a judgment can be entered compelling them to declare dividends. This fails to consider one of the arguments in the *Kroese* case that the court in declaring dividends in a proper case replaces the discretionary action of the directors with the judgment of the court.

In North Carolina, the situation is somewhat different from that of the principal case because the statute regulating the declaration of dividends<sup>22</sup> requires that a stockholder first apply to the directors for a declaration of dividends, and if refused, an action of mandamus will lie. It must be alleged that such an application was made and refused by the directors before the court will grant relief under the statute.<sup>23</sup>

It is interesting to note that the objections<sup>24</sup> to ordering the declaration of dividends without a majority of the directors present as parties defendant do not arise in North Carolina. The North Carolina court has said in regard to the declaration of dividends that, "By virtue of the statute there is no discretion in the board of directors with respect to the performance of this duty."<sup>25</sup> And yet, in *Southern Mills, Inc. v. Armstrong*,<sup>26</sup> the court reached substantially the same result as those

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recover dividends on stock held in one man corporation; held, failure to object in time to lack of directors as parties constituted a waiver). *Jones v. Van Heusen Charles Co.*, 230 App. Div. 694, 240 N. Y. S. 204 (1930) (plaintiff brought stockholder's representative action to compel payment of dividends and for the mismanagement and misconduct of directors; held, the corporation, officers, and directors must be named as defendants). *Gesell v. Tomahawk Land Co.*, 184 Wis. 537, 200 N. W. 550 (1924) (demurrer to complaint was sustained because it did not establish propriety of compelling dividend and on further ground that directors were not made defendants).

<sup>22</sup> N. C. GEN. STAT. §55-115 (1943).

<sup>23</sup> *Winstead v. Hearne Bros. & Co.*, 173 N. C. 606, 92 S. E. 613 (1917).

<sup>24</sup> *Schuckman v. Rubenstein*, 164 F. 2d 952 (6th Cir. 1947), *cert. denied*, 333 U. S. 875 (1948) (court cannot declare dividend; therefore action is in personam against members of the board); *NY PA NJ Utilities Co. v. Public Service Commission*, 23 F. Supp. 313 (1938) (suit against directors for misconduct); *Gesell v. Tomahawk Land Co.*, 184 Wis. 537, 200 N. W. 550 (1924) (because declaration of dividends is within good-faith discretion of directors, they are entitled to be heard).

<sup>25</sup> *Cannon v. Wiscasset Mills Co.*, 195 N. C. 119, 123, 141 S. E. 344, 346 (1928).

<sup>26</sup> 223 N. C. 495, 27 S. E. 2d 281 (1943).

cases prior to the principal case. In the *Southern Mills* case, the plaintiff company brought an action for mandamus, mandatory injunction or other appropriate relief, naming the corporation and the three directors as defendants. Service on the two non-resident directors was by publication which was held to be insufficient, and the action was dismissed.

It seems the court could have held that the directors were not necessary parties to the action and that a mandatory injunction could have been granted against the corporation for the declaration of the dividends.<sup>27</sup>

The result of the principal case is commercially sound and conducive of wholesome conduct of corporate affairs. It is unconscionable that the majority stockholders of the voting stock could so choose their directors that a minority stockholder could not bring suit to enforce his rights due to his inability to get personal service of a majority of the widely scattered board of directors. By such a process, the majority stockholders could control the corporation through the directors almost without restriction. This the courts should not allow.<sup>28</sup>

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### Criminal Law—Transportation of Alcoholic Beverages

The Turlington Act<sup>1</sup> of 1923 made it unlawful in North Carolina to transport intoxicating liquor in any quantity for beverage purposes.<sup>2</sup> While this act has not been repealed, the Alcoholic Beverage Control Act<sup>3</sup> of 1937 has modified some of its provisions.<sup>4</sup> The basic trans-

<sup>27</sup> *Clark v. The Henrietta Mills*, 219 N. C. 1, 3, 12 S. E. 2d 682, 683 (1941). The action was, "to have corporate reorganization together with amendments to the charter of defendant, declared invalid as to plaintiff; to protect plaintiff's rights to accrued dividends on preferred stock claimed to be unlawfully invalid or defeated by the reorganization; to compel the payment of such dividends prior to the payment of dividends on reorganization stock; and to restrain defendant from the prior payment of dividends on any stock until dividends on plaintiff's preferred stock are first paid." Injunction was granted to preserve and enforce plaintiff's rights without requiring directors to be joined as defendants, although the question was not raised by the corporation.

<sup>28</sup> *Lebold v. Inland Steel Co.*, 125 F. 2d 369 (7th Cir. 1941), *cert. denied*, 316 U. S. 675 (1942).

<sup>1</sup> The Turlington Act is now N. C. GEN. STAT. §§18-1—18-30 (1943). It was intended to make the North Carolina prohibition law conform substantially with the National Prohibition Act, and in some respects it is more stringent. See *State v. Hickey*, 198 N. C. 45, 150 S. E. 615 (1929).

<sup>2</sup> N. C. GEN. STAT. §18-2 (1943). "No person shall manufacture, sell, barter, transport, import, export, deliver, furnish, purchase, or possess any intoxicating liquor except as authorized in this article. . . ."

<sup>3</sup> N. C. GEN. STAT. §§18-36—18-62 (1943). The A.B.C. Act was intended to establish a uniform system of administration and control of the sale of certain alcoholic beverages in North Carolina. It provides that in counties where an election has been held and a majority of those voting in the election have expressed themselves in favor of the operation of liquor stores, county A.B.C. stores may be established and operated under the supervision of the county A.B.C. Board. For a thorough discussion of the Act see *State v. Davis*, 214 N. C. 787, 1 S. E. 2d 104 (1939).

<sup>4</sup> See *State v. Barnhardt*, 230 N. C. 223, 52 S. E. 2d 904 (1949); *State v. Wilson*, 227 N. C. 43, 40 S. E. 2d 449 (1946).