Michigan Law Review

Volume 33 | Issue 6

1935

CORPORATIONS - FIDUCIARY RELATION OF DIRECTORS - PURCHASE OF STOCK FOR COMPANY

CORPORATIONS — FIDUCIARY RELATION OF DIRECTORS — PURCHASE OF STOCK FOR COMPANY — A company needed a block of stock offered to it in order to acquire certain patent rights. The finances of the company were insufficient to effect the purchase. The board of directors accepted the offer for the company with the understanding that the directors would acquire the stock individually and turn over to the company the needed patent rights. After bankruptcy, the trustee of the company sued to recover profits realized by the directors from a sale of the stock. *Held*, the inability of the company to purchase the stock itself does not relieve the directors from liability for profits made in breach of their fiduciary duties.[1] *Irving Trust Co. v. Deutsch*, (C. C. A. 2nd, 1934) 73 F. (2d) 121, cert. denied (U. S. 1935) 55 Sup. Ct. 405.

It is well settled that the directors and officers of a corporation stand in a fiduciary relation to the corporation, so that they will be held accountable for any personal profits made in violation of their fiduciary duties.[2] Where an officer of a corporation acquires for his own benefit some interest which the corporation at that time was unable to acquire on its own behalf, the courts seem to relax somewhat the rigidity of the rule. Where a lessor refuses to renew a lease with

[1] The court held that the fact that the board of directors of the company accepted the offer of purchase was decisive that the contract existed between the offeror and the company, regardless of the fact that the offeror had delivered the stock directly to, and had been paid by the defendant directors. The lower court seemed to consider the acceptance by the company a mere formality, with the real contract existing between the defendants and the seller of the stock. Irving Trust Co. v. Deutsch, (D. C. S. D. N. Y. 1932) 2 F. Supp. 971.

[2] Jackson v. Ludeling, 21 Wall. (88 U. S.) 616 (1874); New York Trust Co. v. American Realty Co., 244 N. Y. 209, 155 N. E. 102 (1926); 3 FLETCHER, CYCLOPEDIA CORPORATIONS, sec. 884 (1931); 2 THOMPSON, CORPORATIONS, sec. 1320 (1927). It is the duty of the director or officer to devote his abilities to the best interests of the corporation, free from all considerations of personal gain or profit. Coombs v. Barker, 31 Mont. 526, 79 Pac. 1 (1905); Allen-Foster-Willett Co., Petitioner, 227 Mass. 551, 116 N. E. 875 (1917). And it is generally said that the officer will be held to account even though the breach of duty caused no injury to the corporation, or even if it proved profitable to it. Western States Life Ins. Co. v. Lockwood, 166 Cal. 185, 135 Pac. 496 (1913); Bird Coal & Iron Co. v. Humes, 157 Pa. 278, 27 Atl. 750 (1893).

the lessee corporation, it is held that a director may acquire a renewal of the lease in his own name.[3] The departure from the orthodox rule that a trustee may not acquire on his own behalf a renewal of a lease held in trust is justified by the theory that the lessor is not bound to accept a corporation as a tenant. A similar result has been reached where an officer of a corporation has entered a contract with,[4] or bought land from, a third party after the latter's refusal to deal with the officer in his representative capacity.[5] But where the law limits the amount of property which a corporation may own, the officers may not acquire such property for their own use even after the corporation has received its legal allowance, unless notice be first given to all the shareholders to enable them to purchase such property if they so desire.[6] And when a director completes the payments on an option running to the corporation at a time when the latter is financially unable to do so, and thus acquires the property, the transaction may be avoided by the corporation and the director held accountable.[7] Yet it has been held that when a lessee corporation, with insufficient funds to exercise its option to purchase the property, assigns the option to a director, the latter will not be held accountable to the stockholders, for the reason that the director deprived the corporation of no rights, the option being of no value to it.[8] The instant case, in refusing to allow the director to acquire personal benefit from his official position when the corporation is solvent but in financial difficulties seems to be making a logical departure from the rule of the non-liability of a director where the corporation is insolvent and inactive.[9] For the officers of a weak corporation should be insulated from opportunity for personal gain at a time when the corporation requires their greatest disinterested efforts.

C. P. H.

[3] Crittenden & Cowler Co. v. Cowler, 66 App. Div. 95, 72 N. Y. S. 701 (1901); Jacksonville Cigar Co. v. Dozier, 53 Fla. 1059, 43 So. 523 (1907).

[4] Keokuk Northern Line Packet Co. v. Davidson, 95 Mo. 467, 8 S. W. 545 (1888).

[5] Kendall v. Webster, 14 B. C. 390 (1909).

[6] Young v. Columbia Oil Co., 110 W. Va. 364, 158 S. E. 678 (1930), noted, 38 W. VA. L. Q. 158 (1932).

[7] Wing v. Dillingham, (C. C. A. 5th, 1917) 239 Fed. 54.

[8] Hannerty v. Standard Theater Co., 109 Mo. 297, 19 S. W. 82 (1892).

[9] When a corporation is insolvent and no longer actively functioning as a going concern, a director may, without accountability, buy for his own benefit corporate property at a foreclosure sale, may purchase a franchise to conduct a competing business, or may retain for his own use money paid to him by a rival concern for not entering the field of his corporation on his own behalf. Grand Amusement Co. v. Palladium Amusement Co., 315 Mo. 907, 287 S. W. 438 (1926); Jasper v. Appalachian Gas Co., 152 Ky. 68, 153 S. W. 50 (1913); Murray v. Vanderbilt, 39 Barb. (N. Y.) 140 (1863).