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CORPORATIONS-OFFICERS AND DIRECTORS--"CORPORATE OPPORTUNITIES" DOCTRINE

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CORPORATIONS—OFFICERS AND DIRECTORS—"CORPORATE OPPORTUNITIES" DOCTRINE—Plaintiff corporation brought a bill in equity for an accounting of profits arising from an alleged breach of fiduciary duty by defendant, a former officer and director. The alleged breach consisted of defendant's action in procuring a contract for the manufacture of a saw sharpening machine for the *X* corporation, wholly owned by him, without disclosing such facts to his associate directors of plaintiff corporation. Plaintiff corporation was engaged in the manufacture of polishing machines, while the *X* corporation manufactured lawn

mowers. At the time of the contract, defendant "knew that . . . [plaintiff corporation] desired to enlarge its field of manufacture to include anything which it was equipped to make, and . . . [it] was equipped to manufacture this saw sharpener."[1] From a final decree confirming the master's report in favor of the plaintiff corporation, defendant appealed. *Held,* affirmed. In obtaining the contract without disclosing the facts to his associate directors, the defendant, although not acting in bad faith, failed to recognize his fiduciary obligation and became liable for the profits of his wholly owned corporation resulting therefrom. *Production Machine Co. v. Howe,* (Mass. 1951) 99 N.E. (2d) 32.

A person who assumes a position as director or officer of a corporation, becoming a fiduciary thereby, necessarily restricts his freedom in personal business dealings. This restriction stems from the fiduciary's duty of undivided loyalty, and, in this phase of the law, finds expression in the doctrine of "corporate opportunities." The limitations imposed by this doctrine, however, are uncertain; especially in cases wherein it is claimed that a director, by appropriating a particular business opportunity for himself or for other business interests with which he is associated, has exploited a corporate opportunity which should have been secured for the benefit of the corporation.[2] It is clear that a director cannot purchase for himself property which it is his duty to purchase for the corporation;[3] likewise, it is clear that he has a right to engage in similar, yet independent, business enterprises.[4] Somewhere between these two situations, the areas of permissible and forbidden conduct shade into each other. The courts have generally required the complaining corporation to show that it had an existing interest in the particular opportunity, either actual or in expectancy, or that the opportunity was essential to its existence.[5] Recovery is based on the theory of

[1] Master's report, quoted in the principal case at 34.

[2] On this general subject, see Fuller, "Restrictions Imposed by the Directorship Status on the Personal Business Activities of Directors," 26 WASH. UNIV. L.Q. 189 (1941); Lake, "The Use for Personal Profit of Knowledge Gained While a Director," 9 MISS. L.J. 427 (1937); Ramsey, "Director's Power to Compete With His Corporation," 18 IND. L.J. 293 (1943); and comments in 39 COL. L. REV. 219 (1939); 35 MARQ. L. REV. 44 (1951); 31 CALIF. L. REV. 188 (1943); 44 YALE L.J. 527 (1935); and 54 HARV. L. REV. 1191 (1941).

[3] 13 AM. JUR., Corporations §1004 (1938); 19 C.J.S., Corporations §777 (1940).

[4] This, however, is not an unlimited right. The directors must act in good faith and must not interfere with the business enjoyed by the corporation. The cases are collected in 64 A.L.R. 782 (1930).

[5] Blaustein v. Pan American Petroleum and Transport Co., 263 App. Div. 97, 31 N.Y.S. (2d) 934 (1941); Guft v. Loft, Inc., 23 Del. Ch. 255, 5 A. (2d) 503 (1939), noted in 13 TEMPLE L.Q. 534 (1939) and commented on in 35 MARQ. L. REV. 44 (1951); Zeckendorf v. Steinfeld, 12 Ariz. 245, 100 P. 784 (1909); News-Journal Corporation v. Gore, 147 Fla. 217, 2 S. (2d) 741 (1941); Lagarde v. Anniston Lime & Stone Co., 126 Ala. 496, 28 S. 199 (1899); and Colorado and Utah Coal Co. v. Harris, 97 Colo. 309 at 313, 49 P. (2d) 429 at 431 (1935): "For plaintiff to prove its expectancy, which was the very crux of its case, we think it was bound to establish, not only that the properties in question possessed value to it, but that it had a practical, not a mere theoretical, use therefor." In 3 FLETCHER, CYC. CORP. §862 (1947), it is said that the general rule does not apply where the evidence fails to show that there was an obligation on the part of the

unjust enrichment and consequently, if there is a disability which prevents the corporation from taking advantage of the opportunity, whether it be financial, legal, or otherwise, it is felt that the director can act for himself with impunity.[6] Recent decisions in Massachusetts, however, indicate a departure from this traditional view. Thus, in *Durfee v. Durfee & Channing, Inc.*,[7] decided in 1948, the Massachusetts court expressly rejected it and instead spoke in terms of the "fundamental fairness" of the transaction. If the sweeping language of the instant case is to be taken at face value, it would seem that this court has gone still further in its departure. Here the court said that a director is under a duty reasonably to protect the interests of the corporation and that a failure to disclose a possible business opportunity, in which the corporation might be interested, constitutes a violation of this duty regardless of good or bad faith. It is submitted that the import of the court's language which, in effect, is to require disclosure of all opportunities of theoretical, as well as practical, advantage to the corporation places too great a burden on the director. The exercise of managerial discretion demands some leeway. However, the amount of such leeway should not be as broad as that allowed under the "expectancy" or property interest concept; instead, it should be only as broad as that allowed under a concept of fundamental fairness. To employ this latter concept as a test of liability would require the court to look at various circumstances which, taken together, give a complete picture of the transaction: (1) whether the corporation had laid specific plans to appropriate this particular opportunity as opposed to general plans to appropriate all profitable opportunities; (2) whether the opportunity was of practical, as distinguished from mere theoretical, value to the corporation; (3) whether the corporation had been negotiating for such an opportunity or advantage; (4) whether the officer was authorized or specially charged with the duty of acquir-

officer to purchase the property in question for the corporation or to offer the same to such corporation. In this latter connection, see Westerly Theater Operating Co., Inc. v. Pouzzner, (1st Cir. 1947) 162 F. (2d) 821.

[6] "Where a corporation declines because of legal barriers, to avail itself of an opportunity, or it is the settled policy of the corporation not to engage in a particular line of business, or it has declined the opportunity for business reasons, or the transaction is beyond the powers of the corporation, or the opportunity is not available either because a party refuses to deal with it or because the corporation sought, but without success to obtain it, the opportunity is one in which the corporation has no legitimate interest of expectancy and may be embraced by the officer or director as his own." 3 FLETCHER, CYC. CORP. §862.1 (1947). See Hart v. Bell, 222 Minn. 69, 23 N.W. (2d) 375 (1946); Urban J. Alexander Co. v. Trinkle, 311 Ky. 635, 224 S.W. (2d) 923 (1949). Compare, however, Irving Trust Co. v. Deutsch, (2d. Cir. 1934) 73 F. (2d) 121, on the question of financial inability of the corporation. Also, as to unjust enrichment, see Gamlin Chemical Co. v. Gamlin, (D.C. Pa. 1948) 79 F. Supp. 622.

[7] 323 Mass. 187, 80 N.E. (2d) 522 (1948). Compare Lincoln Stores, Inc. v. Grant, 309 Mass. 417, 34 N.E. (2d) 704 (1941), an earlier decision, noted in 55 HARV. L. REV. 866 (1942), wherein the court employed the "expectancy" or property interest formula. On the general question of liability of directors in Massachusetts, see Tilden, "The Fiduciary Duty of Corporation Directors in Massachusetts," 28 BOST. UNIV. L. REV. 265 (1948) and the comment in 22 BOST. UNIV. L. REV. 300 (1942).

ing such opportunities; (5) whether knowledge of the opportunity came through his official position; (6) whether corporate funds or facilities were in any way used; (7) whether the corporation was in a position to avail itself of the opportunity; (8) whether acquisition placed the director in a position adverse to that of the corporation; (9) whether the director contemplated resale to the corporation; and (10) whether the corporation was small with active management in the hands of a few. No one of these circumstances by itself should be conclusive.[8] All of them should be weighed and as the scale tips on the question of fundamental fairness, so should it tip on the question of liability.

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[8] See BALLANTINE, CORPORATIONS, rev. ed., §79 (1946).