A model statute could provide for minimum standards in contraceptives to be fixed by some medical authority and should prohibit misleading advertising of inefficient articles. There may also be good ground for prohibiting sales to minors. But it is suggested that with respect to advertising, no restrictions in addition to those of the general obscenity statutes are necessary or appropriate.

NECESSITY OF APPLICATION TO SHAREHOLDERS IN DERIVATIVE SUITS

Since the purpose of a shareholder's *derivative* action is to remedy injuries to the shareholders as a corporate group rather than to them as individuals,[1] one of the cardinal requirements is that the plaintiff exhaust all means of redress through the corporation itself before bringing suit in its behalf.[2] To satisfy this condition the plaintiff must allege a demand for action upon the "corporate authorities,"[3] or facts clearly indicating that such request would be futile or impossible.[4] The term "corporate authorities" as used in this connection, of course, includes the corporate officers and the board of directors, but whether or not it also includes the body of shareholders is not conclusively settled by the decisions or text books.

"The fact that a demand has been made upon the directors and they have refused to act, does not .... *ipso facto* relieve the plaintiff from seeking corporate redress from the shareholders."[5] Having been frustrated in proper demands for action upon the officers and board of directors, to what extent and

[1] For a lucid discussion of the distinction between a shareholder's direct and individual cause of action and a shareholder's derivative suit for the enforcement of a corporate right, see Stevens, Corporations § 162 (1936). It is possible for a shareholder to institute a class or representative action of either type. See also Moore, Federal Practice c.23 (1938); 13 Fletcher, Cyclopedia Corporations §§ 5939–5965 (rev. ed. 1932); 4 Cook, Corporations §§ 740–759 (8th ed. 1923).

[2] "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 simulated effort, with [*sic*] 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." Hawes v. Oakland, 104 U.S. 450, 460 (1881).

[3] Hawes v. Oakland, 104 U.S. 450 (1881); Rathbone v. Parkersburg Gas Co., 31 W.Va. 798, 8 S.E. 570 (1888); Miller v. Murray, 17 Colo. 408, 30 Pac. 46 (1892); Latimore v. Richmond Ry., 39 S.C. 44, 17 S.E. 258 (1893); Stedtfeld v. Eddy, 45 Idaho 584, 264 Pac. 381 (1928); Caldwell v. Eubanks, 326 Mo. 185, 30 S.W. (2d) 976 (1930).

[4] "And he [the stockholder] must show a case, if this is not done, where it could not be done, or it was not reasonable to require it." Hawes v. Oakland, 104 U.S. 450, 461 (1881). 13 Fletcher, *op. cit. supra* note 1, at 263.

[5] 2 Moore, Federal Practice 2269 (1938).

for what purposes must the minority shareholder exert efforts to secure action by the stockholders as a body? Rule 23 of the Federal Rules of Civil Procedure, formerly Federal Equity Rule 27,[6] requires the complaint to state efforts to secure action on the part of the managing directors "and, if necessary, from the shareholders."[7] The rule therefore leaves the problem undecided. There seems to be no conflict in the federal and state decisions in regard to this matter[8] since there is discernible in both lines an attempted harmonization with the English doctrine as announced in *Foss v. Harbottle*[9] and developed in later cases.[10]

In the traditional language of the American courts, the "test" employed is the distinction between wrongs "void and voidable," or between acts that can and cannot be "ratified or confirmed" by the body of stockholders.[11] If only "voidable," the formula runs, the matter is "capable of ratification" by the majority and must be voted upon before the complainant can sue. If "void" and not "subject to confirmation," a request upon them is dispensed with. There is a tendency on the part of some courts to label all *ultra vires* and "fraudulent" acts as "void" for this purpose. Such language would suggest doubt as to the right of the majority shareholders, under any circumstances, to compromise or to disregard causes of action arising from such acts. The majority of shareholders undoubtedly have this right in many situations. It is proposed therefore to define capacity to "ratify" in terms of the possibility of a choice open to the majority to sue or not to sue. The question of the necessity for a demand should be subordinate to the determination of this primary question.

Wrongs commonly referred to as "ratifiable" are those in which the majority

[6] The rule of Hawes v. Oakland, 104 U.S. 450 (1881) quoted in note 2 *supra*, was adopted as equity rule No. 94 in the federal courts, later changed to rule 27, and is now contained in Rule 23 of the Federal Rules of Civil Procedure.

[7] The provision reads as follows: "In an action brought to enforce a secondary right on the part of one or more shareholders in an association, incorporated or unincorporated, because the association refuses to enforce rights which may properly be asserted by it.... the complaint shall aver (1) that the plaintiff was a shareholder at the time of the transaction of which he complains or that his share thereafter devolved on him by operation of law and (2) that the action is not a collusive one..... The complaint shall also set forth with particularity the efforts of the plaintiff to secure from the managing directors or trustees and, if necessary, from the shareholders such action as he desires, and the reason for his failure to obtain such action or the reasons for not making such effort."

[8] See 13 Fletcher, *op. cit. supra* note 1, at § 5964. The rule of court adopted by the federal courts has had strong influence on the states.

[9] 2 Hare 461 (1843).

[10] Bagshaw v. Eastern Union Ry. Co., 7 Hare 114 (1849); Gregory v. Patchett, 33 Beav. 595 (1864); MacDougall v. Gardiner, L.R. 1 Ch. Div. 13 (1875); Mason v. Harris, L.R. 11 Ch. Div. 97 (1879); Mozley v. Alston, 1 Phill. Ch. 790 (1847); Lord v. Co. of Copper Miners', 2 Phill. Ch. 740 (1848).

[11] See Brewer v. Boston Theater, 104 Mass. 378 (1870); Kessler v. Ensley Co., 123 Fed. 546 (C.C. Ala. 1903); Continental Securities Co. v. Belmont, 206 N.Y. 7, 99 N.E. 138 (1912).

shareholders have an election to proceed on one of several courses, *e.g.*, the power to rescind or affirm a contract voidable because authorized by directors personally interested. In such cases, it is obviously desirable that, before suit by an individual shareholder is permitted, the question of affirmance be submitted to the shareholders as a body. As pointed out in part I *infra*, the majority have this right of election only when there are bona fide alternatives to be weighed in the interest of the corporation. Where such election is possible the necessity of a demand is clear. Where, on the other hand, the election not to sue would entail the surrender of valuable corporate rights without commensurate advantage to the corporation, or where for other reasons mentioned in part II *infra*, the option in the shareholders is foreclosed, the plaintiff should be permitted to bring a derivative suit without application to other shareholders and regardless of the attitude of the majority.

It is true that the cases evade such a clear-cut classification. The language of many cases and the holdings of a few[12] are to the effect that a demand on shareholders is a prerequisite to the bringing of a derivative suit even where a vote on their part that no suit be brought would not preclude a later derivative action. In part III *infra*, various possible explanations for these cases are examined, but the cogency of each is seriously questioned. Whatever these reasons are they must, however, be kept separate from the rationale that where a choice falls to the majority, a demand is necessary in order to get them to act.

I

In many cases derivative suits are dismissed because the failure to take the requested action falls within the proper discretion of the board of directors.[13] If the minority shareholder is merely complaining of what he deems "unwise" policy on the part of the directors or officers in the management of the affairs of the corporation there will be no judicial interference under the familiar rule that so long as those in charge are not affected with an adverse interest,

[12] See note 32 *infra*.

[13] Hawes v. Oakland, 104 U.S. 450 (1881) (shareholder in water company seeking to enjoin corporation from furnishing city with water free of charge beyond what the contract with city allegedly specified); Huntington v. Palmer, 104 U.S. 482 (1881) (shareholder seeking to enjoin payment by directors of an allegedly overassessed tax); Corbus v. Alaska Treadwell Gold Mining Co., 187 U.S. 455 (1903) (shareholder seeking to enjoin corporation from paying allegedly illegal license tax); Elliot v. Puget Sound Wood Products Co., 52 Wash. 637, 101 Pac. 228 (1909) (shareholder complaining of purchase of allegedly useless patent); Wunderlich v. Coeur D'Alene Vulcan Mining Co., 40 Idaho 173, 232 Pac. 588 (1924) (shareholder seeking to compel corporation to redeem corporate property from execution sale); Latimore v. Richmond Ry., 39 S.C. 44, 17 S.E. 258 (1893) (shareholder in lessor corporation seeking to compel faithful performance of lease covenants by lessee); Van Tassel v. Spring Perch Co., 113 Conn. 636, 155 Atl. 832 (1931) (shareholder objecting to change of corporate product); Pierce v. Old Dominion Copper Mining & Smelting Co., 67 N.J. Eq. 399, 58 Atl. 319 (1904) (shareholder complaining of renting of equipment from another corporation); Dimpfell v. Ohio & Mississippi Ry. Co., 110 U.S. 209 (1884) (shareholder objecting to the purchase of new facilities).

their discretion is final.[14] Unless the policy pursued is extremely prejudicial to the corporation and indirectly to the minority, the complaining shareholder is out of court. His sole recourse evidently is an appeal to the majority to exercise whatever influence they possess over the board.

Where the directors are disqualified, however, because adversely interested,[15] the decision to seek judicial redress may rest with the majority shareholders. Whether or not the latter have alternative courses of action must of necessity depend upon the circumstances. In refusing to sue, the majority may be motivated by the desirability of retaining the services of the defendant, of preserving the good name of the corporation, or of averting antagonism.[16] For example in *Kessler v. Ensely Co.*[17] where the directors fraudulently obtained judgment against the corporation with the consequent sale of the corporate property to themselves, it was held that the decision as to the desirability of bringing suit rested with the majority of the shareholders; and that their action, with full knowledge of the facts, in refusing to rescind was binding on the minority, even though the transaction had been fraudulent and would have been set aside at the suit of the corporation.[18] Such criteria as the size of the

[14] "The vast and increasing importance of the business transacted by corporations and the immense number of stockholders in many of these companies, require that the courts should closely scrutinize actions brought by shareholders where the cause of action is primarily one belonging to the company. If it be once conceded that such companies may be embarrassed and subjected to cost and expense by every stockholder who thinks he has a grievance, the usefulness of corporations would be seriously crippled." Miller v. Murray, 17 Colo. 408, 418, 30 Pac. 46, 49 (1892).

[15] Boyd v. Sims, 87 Tenn. 771, 11 S.W. 948 (1889) (directors leasing corporate property at allegedly inadequate rental to company in which they had interest); Holmes v. Jewett, 55 Colo. 187, 134 Pac. 665 (1913) (less than required quorum of stockholders attempting in good faith to transfer mining claims to officer of the corporation); Wright v. Floyd, 43 Ind. App. 546, 86 N.E. 971 (1909) (fraudulently obtained confession of judgment by director against corporation); Caffall v. Bandera Telephone Co., 136 S.W. 105 (Tex. Civ. App. 1911) (alleged "conspiracy" of officers to sell part of corporate property to rival); Montgomery Light Co. v. Lahey, 121 Ala. 131, 25 So. 1006 (1899) (alleged mismanagement and misappropriation of corporate funds by directors); Hagood v. Smith, 162 Ala. 512, 50 So. 374 (1909) (director retaining proceeds after authorized sale of corporate property); Foss v. Harbottle, 2 Hare 461 (1843) (directors selling their own property to corporation at allegedly excessive prices); Wolf v. Pennsylvania Ry. Co., 195 Pa. 91, 45 Atl. 936 (1900) (alleged diversion of funds receivable from lessee corporation); Passmore v. Allentown & Reading Traction Co., 267 Pa. 356, 110 Atl. 240 (1920) (directors permitting alleged breach of lease covenants by lessee corporation in which they are interested). And see Bill v. Western Union Tel. Co., 16 Fed. 14 (C.C.N.Y. 1883); 72 A.L.R. 628 (1931).

[16] See note, 4 Univ. Chi. L. Rev. 495 (1937).

[17] 123 Fed. 546 (C.C. Ala. 1903); and see Kessler & Co. v. Ensley Co., 129 Fed. 397 (C.C. Ala. 1904).

[18] "The transactions here complained of not being void, but merely voidable .... the power to affirm or to disaffirm is not an individual prerogative, but the right and power of the whole body of stockholders collectively. This collective body must act and decide according to the vote of the majority. .... A majority of stockholders, in a case of this kind, represent the ultimate corporate sovereignty .... and can bind the minority by its refusal to disaffirm as to a matter intra vires." Kessler v. Ensley Co., 123 Fed. 546, 560 (C.C. Ala. 1903).

corporation and the amount involved, the various possible benefits to the corporation direct and indirect, and the chances of recovery by litigation are taken into account. Conceivably, even where the amount involved is large, it may be deemed to the best interests of the corporation to disregard the valuable cause of action. Consider, for example, a corporate cause of action for damages against a labor union. Here the decision of the directors as to the desirability of suit almost certainly would be conclusive. In most cases, however, persuasive excuses for not enforcing a valuable cause of action are likely to be rare since the pecuniary benefit as against the detriment to the corporation is often difficult to discern. Close scrutiny of alleged reasons for not bringing suit is therefore in order.

II

There are, on the other hand, several cases in which it is clear that the desires of the majority will not be permitted to control because, for one reason or another, only one course of action can be followed with fairness to all.[19] This course of action may be made mandatory by statute,[20] or by the particular exigency confronting the shareholders. In these cases failure by the complainant to make a demand upon the shareholders is usually held not to prevent him from bringing his derivative cause of action. In the leading case, *Continental Securities Co. v. Belmont*,[21] the wrong to the corporation was the fraudulent issue of fifteen hundred shares of stock in payment of a claim for pretended services and property of nominal value. It was declared that regard-

[19] Continental Securities Co. v. Belmont, 206 N.Y. 7, 99 N.E. 138 (1912); Brewer v. Boston Theater, 104 Mass. 378 (1870); March v. Eastern Ry. Co., 40 N.H. 548 (1860); Greenwood v. Union Freight Ry. Co., 105 U.S. 13 (1881); Forrester v. Boston & Montana Cons. Copper & Silver Mining Co., 21 Mont. 544, 55 Pac. 229 (1898); Ellis v. Penn Beef Co., 9 Del. Ch. 213, 80 Atl. 666 (1911). And see also McCampbell v. Fountain Head Ry. Co., 111 Tenn. 55, 77 S.W. 1070 (1903); Albers v. Merchants' Exchange, 45 Mo. App. 206 (1891); Planten v. National Nassau Bank, 174 App. Div. 254, 160 N.Y. Supp. 297 (1916); aff'd 220 N.Y. 677, 116 N.E. 1070 (1917); Red Bud Realty Co. v. South, 153 Ark. 380, 241 S.W. 21 (1922); Alexander v. Searcy, 81 Ga. 536, 8 S.E. 630 (1889); Shaw v. Staight, 107 Minn. 152, 119 N.W. 951 (1909); National Power & Paper Co. v. Rossman, 122 Minn. 355, 142 N.W. 818 (1913).

[20] Ellis v. Penn Beef Co., 9 Del. Ch. 213, 80 Atl. 666 (1911); Pollitz v. Wabash Ry. Co., 142 App. Div. 755, 127 N.Y. Supp. 782 (1911). See also Greenwood v. Union Freight Ry. Co., 105 U.S. 13 (1881).

[21] 206 N.Y. 7, 99 N.E. 138 (1912). Although the New York Court of Appeals was readily able to distinguish the case from Hawes v. Oakland, 104 U.S. 450 (1881), the leading American case requiring a preliminary demand on the stockholders, the Appellate Division saw "no compelling reason why [the rule of Hawes v. Oakland] should be adopted in this state, for it is not based upon substantial reason and it could not fail to be oppressive and practically destructive of justice in many instances. Where, as in this case, there are 350,000 shares of stock and doubtless thousands of stockholders . . . . it would be most costly and time-consuming to endeavor to bring home to them for consideration the facts which should spur them to action on their part as stockholders. If they refused to approve the course of the plaintiffs in their demand on the directors, then such refusal would not alter the plaintiff's right to a remedy on behalf of the corporation, for no ratification could take place by formal action or by inaction." 150 App. Div. 298, 303, 134 N.Y. Supp. 635, 639 (1912).

less of *bona fides* the stockholders could not affirm the transaction. Borrowing the terminology of *Foss v. Harbottle*,[22] the court dispensed with the demand because the acts sought to be redressed were not "subject to ratification."[23] The failure to insist upon an application to the stockholders may be explained on the ground that under the circumstances a suit was the only course open to the majority shareholders. Similarly in a case where the directors of a corporation had twice compensated themselves for the same services and where the majority of the stockholders had voted to ratify, a bill for an accounting was sustained for the reason that no majority of the shareholders could *gratuitously* condone the fraudulent acts of the defendants over the plaintiff's objection.[24] Conceding that a *compromise* on fair terms was legitimate,[25] the court held a *surrender* of a valuable corporate right without comparable benefit to the corporation was not.[26]

It should be emphasized that whether or not the majority is empowered to compromise a valuable corporate cause of action depends not so much on the degree of moral turpitude of the wrongdoers as on the amount of injury suffered by the corporation and the type of settlement offered. Although the courts purport to distinguish between actions for fraud and actions for negligence, no plausible reason is offered for the difference. It would seem that the majority can as well compromise a cause of action for fraud as for negligence, provided an adequate *quid pro quo* to the corporation is apparent to the court. Conversely, the stockholders may no more gratuitously surrender a cause of action for huge damages resulting from negligent injury than they might a cause of action for fraud involving a similar amount.[27]

It is essential that any election made by the majority be a *bona fide* one. Such a possibility may be precluded where the majority is itself tainted with an adverse interest in the transaction. Positive evidence of this may be lacking, but it has been suggested that scrutiny of the character of the conduct sought to be ratified may be fruitful in inferring the motives of the majority or those who control the majority. "Where the conduct of the directors was dishonest there is some probability that the ratification by the majority was part of the same scheme."[28] Certainly such an inference is justified where the

[22] 2 Hare 461 (1843).

[23] Continental Securities Co. v. Belmont, 206 N.Y. 7, 18, 99 N.E. 138, 142 (1912).

[24] Eshleman v. Keenan, 187 Atl. 25 (Del. Ch. 1936).

[25] For a case illustrating a successful compromise see Karasik v. Pacific Eastern Corp., 180 Atl. 604 (Del. Ch. 1935).

[26] See Stevens, *op. cit. supra* note 1, at 667.

[27] Compare Kessler v. Ensley Co., 123 Fed. 546 (C.C. Ala. 1903); Wright v. Floyd, 43 Ind. App. 546, 86 N.E. 971 (1909); Hersey v. Veazie, 24 Me. 9 (1844), with Rathbone v. Parkersburg Gas Co., 31 W.Va. 798, 8 S.E. 570 (1888); Doud v. Wisconsin, Pittsville & Superior Ry. Co., 65 Wis. 108, 25 N.W. 533 (1885); Caldwell v. Eubanks, 326 Mo. 185, 30 S.W. (2d) 976 (1930).

[28] Note, Ratification of Director's Frauds, 4 Univ. Chi. L. Rev. 495, 496 (1937).

wrongdoers themselves own a majority of the shares or in other ways dominate the shareholders. And where the wrong was threatened by the majority,[29] or participated in by them,[30] or confirmed by their vote,[31] the demand has been held unnecessary. No action at a shareholders' meeting would bar the plaintiff's remedy.

III

Even in situations where the majority has no power to take action barring the suit, the necessity of demand is urged as one ground for decision[32] and indicated by a great mass of *dicta* in others.[33] Numerous are the cases in which the complaining shareholder has shown to the satisfaction of the court that such a request was impossible or "unavailing"; and where except for such circumstances, the inference is that a demand would have been required.[34] Since

[29] Barr v. Pittsburgh Plate-Glass Co., 40 Fed. 412 (C.C. Pa. 1889); Williams v. Erie Mountain Cons. Mining Co., 47 Wash. 360, 91 Pac. 1091 (1907); Liggett v. Roanoke Water Co., 126 Va. 22, 101 S.E. 55 (1919); Pollitz v. Wabash Ry. Co., 142 App. Div. 755, 127 N.Y. Supp. 782 (1911).

[30] Chicago v. Cameron, 120 Ill. 447, 11 N.E. 899 (1887); Glenn v. Kittanning Brewing Co. 259 Pa. 510, 103 Atl. 340 (1918); Wilson v. Brown, 269 Pa. 225, 112 Atl. 1 (1920); Von Arnim v. American Tube Works, 188 Mass. 515, 74 N.E. 680 (1905); Jacobson v. Brooklyn Lumber Co., 184 N.Y. 152, 76 N.E. 1075 (1906); Sigwald v. City Bank, 82 S.C. 382, 64 S.E. 398 (1909); Wills v. Nehalem Coal Co., 52 Ore. 70, 96 Pac. 528 (1908); Hyams v. Calumet & Hecla Mining Co., 221 Fed. 529 (C.C.A. 6th 1915); Joy v. Ft. Worth Compress Co., 24 Tex. Civ. App. 94, 58 S.W. 173 (1900).

[31] Delaware & Hudson Co. v. Albany & Susquehanna Ry. Co., 213 U.S. 435 (1909); Tillis v. Brown, 154 Ala. 403, 45 So. 589 (1908); Decatur Mineral Land Co. v. Palm, 113 Ala. 531, 21 So. 315 (1896); Eshleman v. Keenan, 187 Atl. 25 (Del. Ch. 1936); Meeker v. Winthrop Iron Co., 17 Fed. 48 (C.C. Mich. 1883).

[32] Rathbone v. Parkersburg Gas Co., 31 W.Va. 798, 8 S.E. 570 (1888); Ward v. Hotel Randolph, 65 W.Va. 721, 63 S.E. 613 (1909); Deveny v. Hart Coal Co., 63 W.Va. 650, 60 S.E. 789 (1908); Caldwell v. Eubanks, 326 Mo. 185, 30 S.W. (2d) 976 (1930); Dorrah v. Pemiscot County Bank, 213 Mo. App. 541, 256 S.W. 560 (1923); Vogler v. Punch, 205 Mo. 558, 103 S.W. 1001 (1907); Barthold v. Thomas, 210 S.W. 506 (Tex. 1919); Mount Radford Trust Co., 93 Va. 427, 25 S.E. 244 (1896); Elmergreen v. Weimer, 138 Wis. 112, 119 N.W. 836 (1909); Smith v. Coolidge Banking Co., 147 Ga. 7, 92 S.E. 519 (1917); Stedtfeld v. Eddy, 45 Idaho 584, 264 Pac. 381 (1928); Tuscaloosa Mfg. Co. v. Cox, 68 Ala. 71 (1880); Merchant & Planters Line v. Wagner, 71 Ala. 581 (1882); Montgomery Light Co. v. Lahey, 121 Ala. 131, 25 So. 1006 (1899); Johns v. McLester, 137 Ala. 283, 34 So. 174 (1902); Howze v. Harrison, 165 Ala. 150, 51 So. 614 (1910); Louisville & Nashville Ry. Co. v. Neal, 128 Ala. 149, 29 So. 865 (1900); Moore v. Lewisburg & Ronceverte Electric Ry. Co., 80 W.Va. 653, 93 S.E. 762 (1917); Scalzo v. Commercial Trust & Savings Bank, 239 Ill. App. 330 (1926). *Cf.* Continental Securities Co. v. Belmont, 206 N.Y. 7, 99 N.E. 138 (1912); Planten v. National Nassau Bank, 174 App. Div. 254, 160 N.Y. Supp. 297 (1916), aff'd 220 N.Y. 677, 116 N.E. 1070 (1917).

[33] See Bartlett v. New York, N.H. & H. Ry. Co., 221 Mass. 530, 109 N.E. 452 (1915); see also cases cited in note 34 *infra*.

[34] Shoening v. Schwenk, 112 Iowa 733, 84 N.W. 916 (1901); Tillis v. Brown, 154 Ala. 403, 45 So. 589 (1908); North v. Union Savings & Loan Ass'n, 59 Ore. 483, 117 Pac. 822 (1911); Stahn v. Catawba Mills, 53 S.C. 519, 31 S.E. 498 (1898); Sigwald v. City Bank, 82 S.C. 382, 64 S.E. 398 (1909); Beckett v. Planters' Compress & Bonded Warehouse Co., 107 Miss. 305,

the rationale given in cases which insisted upon a demand as a means of inducing the majority to exercise whatever election is open to them is not applicable here, a different explanation must be sought where there is no such election.

It is frequently said that application must be made to the body of shareholders as a means of exhausting efforts to obtain redress within the corporation itself. The requirement may thus be imposed in order to avoid unnecessary litigation. The persuasiveness of this suggestion depends upon the efficacy of the remedies the majority of the stockholders have in combatting a stubborn board of directors. Usually the only remedy is the election of a new board.[35] In dispensing with a demand entirely the court in *Continental Securities Co. v. Belmont*[36] was undoubtedly persuaded by the feeble part enjoyed by the stockholders in the control of corporate affairs. There may not be time to remove the offenders. Ere the time for election comes "irreparable injury and the vesting of great financial interests"[37] may occur, or laches arise to bar the stockholder's suit. "The fact," says one writer, "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 shareholders can by election control such suit . . . . has settled the rule that the shareholder's request to the corporate directors to institute a suit is sufficient."[38]

While it is conceivable that the majority of the stockholders might vote to have suit brought, then hire counsel and have suit proceed in the corporate name rather than derivatively, no instances of such procedure have been found. The insistence upon a demand, moreover, tends only to postpone not prevent litigation. Since in this class of cases it is assumed that it is not within the power of the majority to bar suit, litigation sooner or later must result. It is not clear that it would be more desirable to have the suit conducted by counsel retained for the corporation and, in any event, there is no great likelihood that application to the shareholders would result in such action.

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65 So. 275 (1914); Decatur Mineral Land Co. v. Palm, 113 Ala. 531, 21 So. 315 (1896); Wills v. Nehalem Coal Co., 52 Ore. 70, 96 Pac. 528 (1908); Liggett v. Roanoke, 126 Va. 22, 101 S.E. 55 (1919). "Even when their [the directors'] acts are *ultra vires*, or otherwise illegal, a complaining member must first seek his remedy within the corporation. The only exception to the rule that a stockholder must apply to the directors, and also, if need be to the corporation, for redress of a wrong done to it . . . . is when it appears that such application would be unavailing to protect his rights." Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 497, 16 N.E. 426, 431 (1888).

[35] See Boyd v. Sims, 87 Tenn. 771, 775, 11 S.W. 948, 949 (1889).

[36] 206 N.Y. 7, 16, 99 N.E. 138, 141 (1912). But see Rathbone v. Parkersburg Gas Co., 31 W.Va. 798, 805, 8 S.E. 570, 573 (1912), where the feasibility of electing a new board by the stockholders was an argument strongly relied upon by the court in insisting upon a demand.

[37] 4 Cook, *op. cit. supra* note 1, at 3242. See Greenwood v. Union Freight Ry. Co., 105 U.S. 13 (1881) where refusal to act by the directors made loss of the corporate franchise imminent.

[38] 4 Cook, *op. cit. supra* note 1, at 3242.

It might be urged that a demand upon the body of shareholders is desirable as a means of giving the shareholders notice of the suit and an opportunity to join. Under such a view, however, it would be difficult to explain why demand should ever be excused, as is frequently the case.[39] While notice of the pendency of such suits would seem desirable, other means are available, and the cost should probably not be borne by the plaintiff.

It may be that the demand on the shareholders is insisted upon as a purely formal requirement in the perfection of the plaintiff's derivative cause of action, imposed by statute or precedent. Some state statutes specifically so provide[40] and Federal Rule 23[41] is perhaps susceptible of such an interpretation. But in this rule the qualifying words "if necessary" may be interpreted to make the demand unnecessary in cases where the shareholders have no power to "ratify."[42] In the absence of persuasive reasons for a requirement of demand in such cases, it is to be anticipated that in federal and state courts alike the rule of the *Belmont* case will be followed with increasing frequency.

JUDICIAL REVIEW OF NEGATIVE ORDERS OF THE FEDERAL COMMISSIONS

The Federal Power Act[1] and the Public Utility Holding Company Act of 1935[2] require, in general, the approval of the proper commission[3] before a corporation subject to either act may sell or otherwise dispose of any part of its facilities valued in excess of $50,000, merge with any other unit, issue any security, alter the rights of security holders, or service any affiliate or subsidiary. If, after due hearing, one of the commissions unreasonably refuses to approve some proposed action, the problem arises as to what relief the aggrieved party may obtain in the federal courts.

[39] See notes 4, 29, 30, and 31 *supra*. What will constitute an excusing circumstance is within the discretion of the court. An inference that the wrongdoers dominated the shareholders because the latter were blood relatives was refused to be drawn in Caldwell v. Eubanks, 326 Mo. 185, 30 S.W. (2d) 976 (1930) and Hagood v. Smith, 162 Ala. 512, 50 So. 374 (1909). The practical difficulty of convening the stockholders was deemed sufficient to excuse a demand in Shoening v. Schwenk, 112 Iowa 733, 84 N.W. 916 (1901). The necessity of haste may often excuse the demand. See Passmore v. Allentown & Reading Traction Co., 267 Pa. 356, 110 Atl. 240 (1920).

[40] See Ga. Civil Code tit. 22, c.711, § 2224 (1933); Smith v. Coolidge Banking Co., 147 Ga. 7, 92 S.E. 519 (1917); Alexander v. Searcy, 81 Ga. 536, 8 S.E. 630 (1888).

[41] Note 7 *supra*.

[42] See opinion of Justice Stone in Rogers v. Guaranty Trust Co. of New York, 288 U.S. 123, 133 (1933).

[1] 49 Stat. 847 (1935), 16 U.S.C.A. § 824 (Supp. 1938), amending Federal Water Power Act, 41 Stat. 1077 (1920), 16 U.S.C.A. 791 (1927).

[2] 49 Stat. 803 (1935), 15 U.S.C.A. 79 (Supp. 1938).

[3] The Public Utility Holding Company Act of 1935 is administered by the Securities and Exchange Commission, and the Federal Power Act by the Federal Power Commission.