will again become an integrated oil company and through its subsidiaries will be so situated that it can be in constant competition with Indiana subsidiaries. Indiana, however, may continue to elect a majority of the board of Pan American. Under such circumstances real competition between the parent and its seventy-eight per cent-owned subsidiary is as unlikely as that the Indiana directors on the Pan American board could completely divorce themselves from considerations of Indiana's welfare in situations in which the interests of the two corporations conflict. In virtually admitting that the Indiana-controlled directors on Pan American cannot be disinterested,[28] the court furnishes a sufficient answer to any argument that the relief granted is adequate.[29]

Corporations—Sale of Controlling Minority Interest under Questionable Circumstances—[Federal].—The plaintiff, an incorporated investment trust, had been in the control of a group of minority shareholders who had solicited proxies and secured the election of their candidates as directors. This controlling group sold their stock in a block to a syndicate. When the control had been transferred, the directors in office successively resigned within a period of a few minutes, and after each resignation the remaining directors elected to office a member of, or an individual "suggested" by, the syndicate. Immediately afterwards, the syndicate, all the members of which became directors, systematically looted the corporation's assets by substituting worthless securities for valuable ones. Subsequently a new board of directors was elected. In an action by the corporation against members of the original controlling group and the directors who had relinquished control to the syndicate, *held*, that "the owners of control are under a duty not to transfer it to outsiders if the circumstances surrounding the proposed transfer are such as to awaken suspicion[1] and put a prudent man on

[28] 174 Misc. 601, 662, 664, 21 N.Y.S. (2d) 651, 709, 711 (S. Ct. 1940).

[29] An appeal in the principal case has been filed in the appellate division. The plaintiffs have filed a cross-appeal from that portion of the judgment refusing to grant permanent relief as asked for in the complaint. It is not without significance that Pan American is proceeding with construction of a pipe line from the East Texas field to its refineries on the Gulf. Standard Corporation Records, Guide and Index Section, November 28, 1940, p. 10, and Chicago Daily News, col. 4, p. 45 (Dec. 13, 1940).

[1] The suspicious circumstances were: the agreement to have a large part of the corporation's assets converted into cash and available as such at the time of the sale; the several warnings to the defendant director by counsel of the corporation of the danger of dealing with little-known parties; the fact that the same corporation had been looted by another group five years before which should have been a vivid reminder of the dangers to which these investment trusts were subject; the presence of a director whose questionable ethical standard was well-known; and the inflated price paid.

The payment of an inflated price is not of itself a suspicious circumstance, for a controlling group may receive a higher than market price by virtue of its strategic position, and the buyer may desire control for an honest business reason (cf. Stanton v. Schenck, 140 Misc. 621, 251 N.Y. Supp. 221 (S. Ct. 1931) where control of Loew's Theaters, Inc. was passed to Fox Theaters, Inc.). But an investment trust, whose assets are but the ready equivalent of cash, cannot give the opportunities of a commercial or industrial venture unless it holds stocks of a nature peculiarly desirable to the purchaser. In the absence of knowledge of this fact, the payment of a price equivalent to several times the market value of the stock is a circumstance which should put a reasonable man on his guard.

guard." Judgment for the plaintiff generally with further proceedings ordered for purposes of assessing damages. *Insuranshares Corp. of Delaware v. Northern Fiscal Corp.*[2]

It is usually said that a stockholder, including a majority stockholder, owes no fiduciary duty to the corporation or to other stockholders. Thus a shareholder is not subject to the disabilities of a director in dealing with the corporation or its shareholders and may deal at arm's length in transactions involving the purchase or sale of assets or securities of the corporation.[3] But in certain situations, a stockholder, usually a majority shareholder, may be held to the same standard of conduct as is required of a director. Where the shareholder actually controls the corporation, through dummy directors, the court may look beyond the corporate set-up and treat the stockholder as a director.[4] Thus, in holding the minority stockholders to a similar standard of conduct, the court in the instant case emphasized that the transaction was "a sale of control, to which the stock sale was requisite, but nevertheless a secondary matter."[5]

In previous cases where a controlling shareholder not on the board of directors has been treated somewhat as a fiduciary, the litigation has involved dealings between the shareholder and the corporation, rather than a sale by the shareholder of his stock and his control.[6] But, although no cases have resolved the problem, there are dicta that a majority shareholder cannot sell out to one—such as a competitor—whom he reasonably should suspect of intending to ruin the corporation.[7] Whether the majority shareholder actually controls the management of the corporation at the time of the sale is apparently of little importance here, since the purchaser automatically obtains ultimate control and can eventually succeed in his purpose by electing a subservient board of directors. On the other hand, where the controlling shareholder owns only a minority of shares, sale of his stock does not result in passing control to the purchaser in the absence of an agreement between the seller and the reigning board of directors and the purchaser. If there is no such agreement, the rights of the other (majority) shareholders are not so likely to be prejudiced by the sale for they will commonly be able to prevent that change in the directorate which would permit the purchaser to loot the corporation. But where there is an agreement to pass control, as in the instant case, the seller of minority shares should be on guard to protect the other shareholders and

[2] 35 F. Supp. 22 (Pa. 1940).

[3] Rothchild v. Memphis & C. R. Co., 113 Fed. 476 (C.C.A. 6th 1902).

[4] Ervin v. Oregon R. & Nav. Co., 27 Fed. 625 (C.C. N.Y. 1886); see Kavanaugh v. Kavanaugh Knitting Co., 226 N.Y. 185, 195, 123 N.E. 148, 151 (1919); Farmers' Loan & Trust Co. v. New York & N.R. Co., 150 N.Y. 410, 434, 44 N.E. 1043, 1050 (1896); Southern Pacific Co. v. Bogert, 250 U.S. 483, 492 (1919); Edwards v. Plains Light & Water Co., 49 Mont. 535, 547, 143 Pac. 962, 965 (1914); Gamble v. Queens County Water Co., 123 N.Y. 91, 99, 25 N.E. 201, 202 (1890); 13 Fletcher, Cyc. Corp. § 5811 (perm. ed. 1932).

[5] Insuranshares Corp. of Delaware v. Northern Fiscal Corp., 35 F. Supp. 22, 24 (Pa. 1940).

[6] Wheeler v. Abilene Nat'l Bank Bldg. Co., 159 Fed. 391 (C.C.A. 8th 1908); Meeker v. Winthrop Iron Co., 17 Fed. 48 (C.C. Mich. 1883); Hyams v. Calumet & Hecla Mining Co., 221 Fed. 529 (C.C.A. 6th 1915); 13 Fletcher, Cyc. Corp. § 5810 (perm. ed. 1932).

[7] See Pennsylvania R. Co. v. Commonwealth, 7 Atl. 368, 373 (Pa. 1886); Southern Pacific Co. v. Bogert, 250 U.S. 483 (1919); Hunnewell v. New York Central & H.R.R. Co., 196 Fed. 543 (C.C. N.Y. 1911); Farmers' Loan & Trust Co. v. New York & N.R. Co., 150 N.Y. 410, 44 N.E. 1043 (1896).

the corporation, for the purchaser can use his control to deplete the corporate assets before the next election of directors.[8]

Assuming that under certain conditions a stockholder must exercise care in disposing of his shares, what is the extent of that duty? The court in the instant case hesitated to attempt "any general definition," but laid down a rule no broader than that necessitated by the particular facts: Where "circumstances surrounding the proposed transfer are such as to awaken suspicion" the seller is under a duty not to transfer "unless a reasonably adequate investigation discloses such facts as would convince a reasonable person that no fraud is intended or likely to result."[9] A fortiori, actual knowledge of the purchaser's destructive intent would result in holding the seller liable.[10] The reluctance of the court to state that the seller has a positive duty of investigating the purchaser is perhaps partly explained by the considerations that corporate shares are treated by the commercial world as freely alienable[11] and that imposition of such a duty appears to go beyond the assumption of risk that is commonly attributed to large —even majority—shareholders. But it may be questioned whether these considerations should be of weight where the stockholder is being treated by the court primarily as a corporate manager rather than as an investor.

In the instant case, the controlling stockholders did not deal directly with the purchasers, but the negotiations were carried on by the board of directors. The court, having stated that one of the director-defendants was in fact agent for all of the controlling shareholders before the court, imputed the knowledge of suspicious circumstances possessed by the agent to his principals, who were held for their negligence in failing to investigate these circumstances.[12]

The court did not discuss what circumstances are necessary to establish an agency relationship in this situation, but it appears that the court thought that an agency exists whenever a director is completely subservient to a shareholder.[13] This view leads

[8] While the method of changing the directorate used in the instant case is very common, Bosworth v. Allen, 168 N.Y. 157, 61 N.E. 163 (1901); Oil Shares, Inc. v. Kahn, 94 F. (2d) 751 (C.C.A. 3d 1938), rev'd on other grounds 304 U.S. 551 (1938), the seriousness of the action is not excused on the plea that it is a normal incident to a sale of controlling stock.

[9] Insuranshares Corp. of Delaware v. Northern Fiscal Corp., 35 F. Supp. 22, 25 (Pa. 1940).

[10] If the court were to require actual knowledge of the purchaser's intent before holding the seller liable, the burden of proof would seemingly be placed upon the plaintiff. It may well be that the desire to make the cause of action of more than doubtful benefit impelled the court to adopt the more liberal view in the instant case.

[11] Reconsideration of Share Certificate Negotiability, 7 Univ. Chi. L. Rev. 497 (1940).

[12] The court was highly impressed with the fact that "the banks, with all their credit facilities made absolutely no investigation of the financial standing and resources of the purchasers and at no time received any information to indicate to them that the purchasers had any money whatever." Insuranshares Corp. of Delaware v. Northern Fiscal Corp., 35 F. Supp. 22, 27 (Pa. 1940).

[13] The assumption of the court raises the question of the liability of interest groups who have a "representative" on the board of directors. It is suggested that the question may be decided on the basis of the shareholding-interest group's motive in exercising control. In particular, "With the investment trust occupying a unique place in the financial world today. . . . there is increasing danger of selling out for the purpose of making profit on shares." Lattin, Equitable Limitations on Statutory or Charter Powers Given to Majority Stockholders, 30 Mich. L.

to a sound result, for a shareholder who controls a corporation from behind the scenes through a dummy directorate should be subject to the same disabilities as one who exercises his control while on the board of directors.[14]

The court in the present case suggests that damages are to be measured by the injury resulting to the corporation from the shortcomings of the controlling stockholders. Since only a fraction of the controlling stockholders were actually before the court, a question arises as to whether full damages can be recovered from those defendants. Because recovery was based upon breach of fiduciary duty by the entire controlling group, it would appear that the individual defendant is to be treated as one of several joint tort-feasors who are jointly and severally liable.[15] It should be noted, however, that the court, while holding the defendants for negligent omissions, dismissed the charge of "knowingly participating in a fraudulent conspiracy" as "not established by the evidence."[16] It is possible that in the absence of a conspiracy, the several defendants could be treated as co-promoters who have divided a wrongful *profit*, in which situation it is sometimes held that each promoter is liable only for his share of the profit.[17] But this result appears unwarranted in the instant case, since the action was based upon the total injury to the corporation and was not limited to a recovery of the unjust profits—presumably measured by the excess of purchase price over the market price—received by the controlling shareholders.

Criminal Law—Accessory after the Fact—Misprision of Felony—[Michigan].—The defendant, knowing a felony had been committed, failed to notify the police or to do anything toward the apprehension and bringing to justice of the guilty person. An information, which resulted in a conviction, was filed charging him with the common law crime of misprision of felony. On an appeal from an order denying leave to withdraw a plea of guilty, *held*, that mere non-disclosure of knowledge of a felony committed by another is not a crime; the conduct of the accused must be such as to make him an accessory after the fact. Misprision of felony, short of accessory after the fact,

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Rev. 645, 659 (1932). And the imputation of a "representative's" knowledge to the interest group he represents does not seem to be too harsh.

[14] "Control" may be exercised by an officer of the corporation (Field v. Western Life Indemnity Co., 166 Fed. 607 (C.C. Ill. 1908); Westwood v. Continental Can Co., 80 F. (2d) 494 (C.C.A. 5th 1935)) as well as by the directors (McClure v. Law, 161 N.Y. 78, 55 N.E. 388 (1899); Keystone Guard v. Beaman, 264 Pa. 397, 107 Atl. 835 (1919); Robotham v. Prudential Ins. Co., 64 N.J. Eq. 673, 53 Atl. 842 (1903); see Jackson v. Smith, 254 U.S. 586 (1921)).

[15] It may be pointed out that the question of whether this "quasi-fiduciary" duty of the controlling group is based upon a trust, contract, or tort relationship is undecided, although the court, in the instant case, assumes that the defendants are joint tort-feasors. The problem of whether contribution over would be allowed, and if so, the problem of apportionment, may possibly be based upon the court's assumption of the underlying relationship between the shareholders of a corporation. See Harper, Torts § 303 (1933); 2 Williston, Contracts § 345 (1936); Rest., Trusts § 258 (1935).

[16] Insuranshares Corp. of Delaware v. Northern Fiscal Corp., 35 F. Supp. 22, 28 (Pa. 1940).

[17] Measure of Recovery against a Promoter Who Sells Property to a Corporation in Breach of Fiduciary Duty, 7 Univ. Chi. L. Rev. 534 (1940).