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ARTICLES

RESTRAINTS ON INCUMBENT DIRECTORS IN INTRACORPORATE BATTLES FOR CONTROL

Dr. Aaron Yoran*

[Editor's Note: The first portion of Dr. Yoran's article, dealing with directors' maneuvering power in closed corporations, appeared in the Winter issue of the Review.]

Proxy Battles

The modern proxy contest has become a grotesque travesty of an orderly machinery for corporate decision making.

—Prof. B. Manning in 67 Yale L. J. 1478 (1958)

A. Insurgents' Access to Shareholders

As in a contest for power in a closed corporation, incumbent directors of public corporations may attempt to frustrate their unseating in a proxy battle by diluting the voting power of the insurgent, or by disturbing the exercise of his voting power. Management also has in its arsenal a variety of tactics which can make its performance look better or fend off the takeover threat. It suffices to say that there exists a clear tendency for the restraining rules espoused for private companies to be eased where publicly held companies are concerned. See the English "duo", Hogg v. Cramp-horn, Ltd. [1967] Ch. 254 and Bamford v. Bamford [1970] Ch. 212, and the Delaware "trio", Cheff v. Mathes, 199 A.2d 548 (Del. 1964); Bennett v. Propp, 187 A.2d 405 (Del. 1962); Kors v. Carey, 158 A.2d 136 (Del. Ch. 1960).

The term "proxy" will be used indiscriminately hereinafter for both the form of authorization and the agent.

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56 The term "proxy" will be used indiscriminately hereinafter for both the form of authorization and the agent.

57 See generally the revolutionary article of Eisenberg, Access to the Corporate Proxy Machinery, 83 Harv. L. Rev. 1489 (1970) [hereinafter cited as Eisenberg].

58 Inspection of the shareholders list is also significant to a takeover bidder. A prospective bidder, however, may forgo the list at least until he makes the offer public, or acts
has the corporate records at its disposal; the insurgent, however, can obtain such a list only if the corporate records are open to inspection, or if management has a duty to furnish such a list. Similarly, the right of access to the corporate books and records is of crucial importance, because by inspecting the books and records, the insurgent may gather important information for his campaign. Indeed, concrete proof of management failures gleaned from these sources could mean victory for the insurgent.

1. England

In England, Sections 110-15 of the Companies Act require that every company keep a register of members open for inspection by every member without charge, and by outsiders on payment of a token fee. If a company has more than fifty members, it must also keep an index accompanying the register. Furthermore, every member and any outsider can obtain a copy of the register on payment of a fixed copying fee. Compliance with this disclosure duty is safeguarded by criminal penalties for defaulting companies and their officers, and by judicial power to compel immediate compliance.

The only "loophole" in the English scheme is that there is no statutory requirement that the register be kept current. Furthermore, a company may close the register of members "for any time or times not exceeding in the whole thirty days in each year." However, before closing, a company must give public notice in a local newspaper of the

through a straw man, in order to surprise the incumbents. A derivative plaintiff might also seek a list in order to muster a sufficient front of plaintiffs to be free from deposit of security statutes. Cf. Studebaker Corp. v. Gittlin, 360 F.2d 692 (2d Cir. 1966). A derivative plaintiff might also seek inspection of the corporate books and records to substantiate his case.

60 Id. at §§ 110, 113. The maximum charge for an outsider is a shilling. Id. at § 113 (1).
61 Id. at § 111.
62 Id. at § 113 (2). The fee is two shillings maximum per one hundred words. See Yoran, Insider Trading in Israel and England, 7 Israel L. Rev. 215, at 219, n.11. (1972) [hereinafter cited as Insider Trading].
63 Companies Act, 1967, c. 81, §§ 110 (4), 111 (4), 113 (3).
64 Id. at § 113 (4). If the company employs an outside register agent, the latter is put in a position of an officer regarding both penalties for noncompliance and the court's power to order compliance. Id. at § 114.
66 Companies Act, 1967, c. 81, § 115.
registered office's district.\textsuperscript{67} Apparently, the Act does not insure timely notice to potential insurgents, nor does it state the length of time between the notice and the closing. Moreover, the principal office of a company may be situated in a location different from its registered office. Insurgents might not see the notice published in the district of the registered office, and would consequently overlook it. The registers for directors\textsuperscript{68} and controlling shareholders,\textsuperscript{69} also open to inspection,\textsuperscript{70} are designed to prevent the employment of nominees or the use of bearer shares from causing the members' register not to reflect the true ownership. Hence, insofar as directors and controlling shareholders comply with their reporting duties, management will not have knowledge superior to that of insurgents about the distribution of voting power in the company.\textsuperscript{71}

English law\textsuperscript{72} also provides insurgents with another device for bringing their campaign to the individual shareholder. Holders of at least five percent of the voting power, or not less than 100 shareholders on whose shares at least 10,000 pounds has been paid up, have a right to demand that the corporation give notice to shareholders of a resolution that the five percent holders seek to present at the upcoming annual general meeting. The five percent holders can also demand that the corporation circulate to the voting shareholders a statement of not more than one thousand words, prepared by the five percent holders, advocating the adoption of the proposed resolution.\textsuperscript{73} Legal writers agree that this device is useless;\textsuperscript{74} the notice and circular are sent at the insurgents' expense,\textsuperscript{75} and the directors can refuse the insurgents' demands upon

\textsuperscript{67} Id.

\textsuperscript{68} Id. at §§ 27, 29. See Insider Trading, supra note 62, at 246.

\textsuperscript{69} Companies Act, 1967, §§ 33, 34. See Insider Trading, supra note 62, at 246.

\textsuperscript{70} Companies Act, 1967, §§ 29 (7), 29 (10), 34 (5), 34 (7).

\textsuperscript{71} Management is always alerted to transfers of blocks of shares. It might trace nominee-held shares to the true owners, or it might discover the owners of bearer shares by the latter's appearance (or giving proxy) in an earlier meeting. Hence, management will have an advantage over insurgents if controlling shareholders do not comply with the reporting duties.

\textsuperscript{72} Companies Act, 1948, § 140.

\textsuperscript{73} They can also urge shareholders to vote against management's proposals.

\textsuperscript{74} Gower, supra note 18, at 483-84; R. Pennington, Company Law 522 (2d ed. 1967) [hereinafter cited as Pennington]; R. Pennington, The Investor and the Law 428-29 (1968).

\textsuperscript{75} The company, however, may resolve otherwise. See note 77 infra. The only saving to insurgents when they use the corporate machinery occurs when the circular is sent out together with the corporate notices.
obtaining a court decision that the insurgents have abused their rights "to secure needless publicity for defamatory matters." Circulating the material by the insurgents themselves according to an available list of shareholders, without being limited to a thousand words, has proven an effective way to conduct the campaign.

The right to have management circulate the insurgents' material is limited to annual general meetings. However, another important right of the insurgents is to have extraordinary general meetings called. This right is possessed by shareholders holding not less than ten percent of the paid-up voting shares. If the directors do not proceed duly to convene a meeting within 21 days from the date of the request to do so, the insurgents may convene the meeting themselves and charge the expenses, to be borne ultimately by the directors, to the corporation. This right enables insurgents to wage a proxy fight as they deem necessary, and not at the whim of management. The insurgents' need to circulate their material themselves is not an impediment because they would normally do so.

Finally, a shareholder has no statutory or common law right to inspect the corporate books. This is surprising, because English company law relies heavily on partnership principles, and complete disclosure among partners is a fundamental principle of partnership law.

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76 Companies Act, 1948, § 140(5).

77 There is only one possible advantage in resorting to Sec. 140, which provides that the circulation be at the expense of the opposition "unless the company otherwise resolves." If the resolution can be retrospective, i.e., passed after the insurgents gain control, and if the general rule is that successful insurgents cannot recover in the usual case, then it pays to take advantage of the Sec. 140 mechanism. Presumably the resolution should be by the general meeting. It is common knowledge, however, that the former opposition, which succeeded in the principal proxy fight, will obtain such approval. On the other hand, when the opposition circulates its material through the corporation it exposes itself to management. The opposition's material will have no time to be effective before management counterattacks, possibly in the very same dispatch. See Gower, supra note 18, at 483.

78 Companies Act, 1948, § 132.

79 The Act requires the directors to "proceed duly to convene a meeting" within 21 days from the date of request, yet does not fix a deadline for the meeting to be held. The Jenkins Committee recommended a deadline of 28 days from the day of the sending of the notice. Jenkins Report, ¶ 468(b). This recommendation, which would insure that the meeting be held within 49 days from the date of request, has not yet been implemented.

80 This will be a reduction from their remuneration. Companies Act, 1948, § 132(5).


82 Gower, Some Contrasts Between British and American Corporation Law, 69 Harv. L. Rev. 1369, 1380 (1956).
2. The United States

In the United States, shareholders have qualified common law and statutory rights to inspect the shareholders list (or stock ledger) and corporate books. All states require that the inspection be for a corporate purpose and in good faith. However, the rules vary from state to state as to what constitutes a corporate purpose, as to who bears the burden of proof, and as to what conditions are necessary for shifting that burden. The courts are somewhat more lenient in enforcing compliance with the right to inspect the shareholders list than with the right to inspect the corporate books. This is explained by the greater burden which examining the books and records places on the corporation. Generally, incumbents take advantage of the fact that the rights are conditioned on proper purpose by employing dilatory tactics. Thus, by

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83 This discussion is limited to the availability of these rights in control battles. See also E. Aranow & H. Einhorn, Proxy Contests For Corporate Control, Ch. 2 (2d ed. 1968) [hereinafter cited as Aranow & Einhorn]. On the question of obtaining a shareholders list, see W. Cary, Cases and Materials on Corporations 295-99 (abr. 4th ed. 1970) [hereinafter cited as Cary]; Newman, Inspection of Stockholder Ledgers and Voting Lists, 16 Sw. L. J. 439 (1962). On the right to inspect the corporate books and records, see Cary at 851-58. On both rights, see N. Lattin, R. Jennings & R. Buxbaum, Corporations, Cases and Materials 417-43 (4th ed. 1968) [hereinafter cited as Lattin, Jennings & Buxbaum].

84 Statutes usually add a requirement that the corporation compile a list of record stockholders and make it available to shareholders prior to the annual meeting. See, e.g., ABA-ALI MODEL BUS. CORP. ACT § 29 (rev. § 31) (1969) [hereinafter cited as MBA]. See Note, 27 U. Conn. L. Rev. 288 (1957) which criticizes the Delaware statute as inadequate because 10 days prior to the meeting is too short a period and because the statute lacks teeth.

85 This is true even where the statute conferring the right does not contain any qualification.


87 Typical conditions are a qualification period and a minimum holding. In New York, for example, 5% holding and six-month qualification (as of record) shift the burden regarding a shareholders list. Cary, supra note 81 at 297. A qualification period and minimum holding are sometimes preconditions to the right to inspect books itself. MBA § 46.


the time the insurgent can win a suit to compel inspection, the incumbents have initiated their own campaign. Therefore, the enunciated rules of what constitutes a proper purpose do not reflect the extent to which inspection rights are available.

It is well settled that waging a proxy battle is a proper purpose for obtaining a shareholders list, and although decisions concerning take-over bids are less conclusive, the majority opinion holds that such a purpose is also proper. Acting under a common law right, the party requesting a shareholder list must sustain the burden of proof. If the plaintiff can rely on a statute, the corporation must show that his real motive is improper. Collateral improper motives in addition to a proper motive do not frustrate the right. In an attempt to avoid the common law re-

brin the suit for inspection in New York, if they can establish jurisdiction, because the New York courts are known to be effective enforcers of the inspection rights. Stephan, id., at 90. Hornstein, CORPORATION LAW AND PRACTICE, § 619 (1959, Supp. 1968).

There is no decision squarely in point that this is a proper purpose for inspecting the corporate books and records.


strictions on the right of inspection, several states have enacted statutes that do not limit this right. The courts, however, have read even into such statutes a proviso that the list can be denied upon a showing of improper motive. 93

The American courts' recognition of the shareholder's common law right to inspect corporate books and records, while such right was refused in England, can be explained in part by the surprisingly small amount of information that American states 94 require corporations to supply to their shareholders. 95 Few states require that annual reports be filed with a state agency, 96 some require annual filing to stockholders; 97 and others require the furnishing of financial reports to stockholders upon request. 98 With such statutory provisions, the only way to gain information is through access to the corporate books and records, 99 and the scope of the "books and records" open to inspection is somewhat

93 E.g., Dines v. Harris, 88 Colo. 22, 291 P. 1024 (1930), and Slay v. Polonia Pub. Co., 248 Mich. 609, 229 N.W. 434 (1930). The rationale of the courts was that since the remedy for enforcing the right is the discretionary remedy of mandamus, their discretion is not fettered. Other jurisdictions have given the statutes their literal meaning, upholding the rights of competitors. This, in turn, has led to corrective legislation. E.g., Furst v. W. T. Rawleigh Medical Co., 282 Ill. 366, 118 N.E. 763 (1918); Pick v. Wesbar Stamping Corp., 238 Wis. 93, 298 N.W. 58 (1941). Lattin, Jennings & Buxbaum, supra note 83, at 424; 5 Fletcher, Cyclopaedia Corporations, § 2220 (perm. ed. 1967, rev. vol.) [hereinafter cited as Fletcher]; Note, Corporations-Shareholder's Right To Inspect Books—Recent Statutory Amendment, 1942 Wis. L. Rev. 292. Note also the tightening of the Delaware provision, which at one time read like the English provision.


95 See Gower, supra note 18, at 454 for a description of the English statutory requirements of financial reports. In England only directors have a free right of access to the corporate books and records. Companies Act, 1948, § 147 (3). A shareholder in England has an absolute right to inspect the minutes of general meetings only. Id. § 146.

96 These are Illinois, Massachusetts, Michigan and Missouri. See, Fletcher, supra note 93, §§ 2258-59; Lattin, Jennings & Buxbaum, supra note 83, 417 n.1; Legis, Disclosure of Corporate Affairs, 47 Harv. L. Rev. 335 (1933).


98 E.g., Cal. Corp. Code § 3013 (1955). The right is often conditioned on the holding of a certain percentage of stock. Id. § 3011; Fletcher, supra note 93, § 2272.1; Lattin, Jennings & Buxbaum, supra note 83, 417 n.5.

99 The Michigan provision, Bus. Corp. Law § 21.45, amplifies the relation between financial reports and the right of inspection. Shareholders eligible for inspection may require a sworn statement "embracing a particular account of its [the corporation's] operations and properties in reasonable detail."
unsettled. It includes not only the corporate constitution, minute books, stock books, and all the records containing financial information,\textsuperscript{100} but also contracts and other documents relating to the corporate business.\textsuperscript{101} It does not include, however, information prepared for management's use, drafts of financial reports,\textsuperscript{102} or confidential data supplied by a merging party.\textsuperscript{103}

Until recently, American statutes left to the corporate constitutions to provide whether shareholders can initiate a general meeting.\textsuperscript{104} In many instances, the constitutions did not delineate such a right, which prevented minority shareholders from expressing their views to fellow incorporators on a proposed course for the corporation.\textsuperscript{105} Further, even if an insurgent faction mustered a majority\textsuperscript{106} of the voting power, it could not unseat the incumbents until the end of their term of office.\textsuperscript{107}

\textsuperscript{100} Kemp v. Sloss-Sheffield Steel & Iron Co., 128 N.J.L. 322, 26 A.2d 70 (1942); State ex rel. Cowell v. Helen Shop, Inc., 211 Tenn. 107, 362 S.W.2d 787 (1962).
\textsuperscript{101} Kemp v. Sloss-Sheffield Steel & Iron Co., 128 N.J.L. 322, 26 A.2d 70 (1942).
\textsuperscript{102} State ex rel. Jones v. Ralston Purina Co., 358 S.W.2d 772 (Mo. 1962).
\textsuperscript{104} It has been generally assumed in the United States that shareholders do not have a right, aside from the right under 17 C.F.R. § 240.14a-8, to have their proposals for corporate action circulated by the corporate proxy machinery. Eisenberg, supra note 57, at 1520, argues that shareholders do have a right "to submit proposals which are within the shareholders' authority to initiate—at least in a corporation in which there is a custom of submitting proposals to shareholders through the proxy materials." Eisenberg contends that Carter v. Portland Gen. Elec. Co., 227 Ore. 401, 362 P.2d 766 (1961), is not a persuasive authority against his proposition. Eisenberg, supra note 57, at 1522-24.

Eisenberg, furthermore, argues that, in an election contest, insurgents have a right that the corporate (incumbents') proxy material include insurgents' designated candidates for directorship. Id. at 1505. Eisenberg's theme is that, since "the proxy system is today's shareholders' meeting, the right (under the statutes of all the states) to nominate directors carries with it access to the proxy materials for that purpose." Id.

\textsuperscript{105} Being able to call a shareholders' meeting is not sufficient for initiating a corporate action even if such action needs shareholder approval. The corporate statutes leave certain matters to be initiated only by the directors. E.g., a sale of substantially all the assets, MBA § 72 (rev. § 79); voluntary dissolution, MBA § 77 (rev. § 84); and merger, MBA § 65 (rev. § 71). Under the MBA, shareholders may initiate amendment of the by-laws if the charter reserves to the shareholders the power (rev. § 27), but they may not initiate amendment of the charter (rev. § 58).

\textsuperscript{106} A provision like Del. Gen. Corp. Law § 228 (1969) that a majority by written consent can substitute for a general meeting enables majority insurgents to circumvent this obstacle.

\textsuperscript{107} If the corporation has a staggered board and it takes more than a simple majority to amend the by-laws, a successful tender offer for more than 50% of the shares does not secure control.
Only recently have legislatures begun to confer upon minority shareholders the right to have a general meeting convened.\(^\text{108}\)

3. **Comparison**

The English rule requiring that a shareholders' register be open to public inspection is superior to the American rules. However, to insure current accuracy, vital in corporate control battles, the English rule should be improved by making daily updating a statutory requirement. The English experience is that the right of inspection has not been abused, nor can it easily be abused. Conditioning the inspection on propriety of purposes and motives as do the American rules destroys the right. The American practice of "selling"\(^\text{109}\) a list is a by-product of the restricting rules. The list is of value only because it is not publicly available. What damage can be inflicted if a "competitor" or a

Moreover, the term of office of the incumbents may actually continue beyond the date on which the next annual meeting is due; if the incumbents fail to convene the meeting, they gain several additional months until they can be legally forced to convene the meeting.

A recent English case underscores the difference between English and American law on the subject. An American corporation took over an English corporation, had an extraordinary meeting convened, and replaced the directors. However, the American corporation found itself impotent to cause the convening of a general meeting of a 70% American subsidiary of the English corporation to remove the latter's board. Pergamon Press Ltd. v. Maxwell, [1970] 1 W.L.R. 1167. See also note 20 supra.

\(^\text{108}\) MBA § 26 (rev. § 28) provides for ten percent of the shareholders to have the right to call a special meeting. Accord: Mass. Law ch. 156B, § 34 (1970); Gen. Stat. N.C. § 55-61(c) (1965). Other states confer the right only to holders of 20%: e.g., Cal. Corp. Code Ann. § 2202 (1955). Maryland confers the right upon 25% of the shareholders. Md. Ann. Code art. 23 § 38(c) (1970). Ohio Rev. Code Ann. § 1701.40(a) follows Maryland but allows the corporate constitution to decrease or increase the percentage, provided it does not exceed 50%.

The state of New York has not yet acted in this direction. N.Y. Bus. Corp. Law § 602(c) (McKinney 1963) provides that special meetings "may be called by the board and by such person or persons as may be authorized by the certificate of incorporation of the bylaws." Note that in *Pergamon* once the acquirer succeeded in convening a general meeting of the subsidiary, he would have prevailed. Even if the corporate constitution of the subsidiary did not allow removal without cause, he could have had the general meeting amend the by-laws to include such a provision. (Such an amendment would be valid under § 601 as amended in 1965.) § 706 (b) states that "if the certificate of incorporation or the by-laws so provide, any or all of the directors may be removed without cause by vote of the shareholders." N.Y. Bus. Corp. Law § 706(b) (McKinney 1963).

\(^\text{109}\) State *ex rel.* Theile v. Cities Service Co., 31 Del. 514, 115 A. 773 (1922), held that obtaining a list to sell is an improper purpose which frustrates the right of inspection.
“raider” obtains a list? Refusing a list virtually deprives shareholders of a free choice in electing management and in other shareholders' actions. The corporate books and records are another matter. The normal channel of information to shareholders should be the annual financial reports, and defects in the rules regulating these reports should be met squarely. Although corporate books and records contain business secrets and cannot be made available automatically to any shareholder, secreting them might lead to mismanagement and perpetuation of control. Thus, a provision for a qualified right is necessary. In the United States, where the losing party does not pay his adversary's attorney's fees, it is the corporation (i.e., the incumbents) that should bear the burden of showing the insurgents' improper purpose for the latter's right to injure the corporation. In England, the burden might be placed on the insurgent, not only because he is the plaintiff, but also because he has superior knowledge about his own purposes and motives.

B. Removal of Directors

Related to the right of shareholders to convene a general meeting are the causes and voting power necessary to remove a director during his term of office. Two fundamental rules of corporate law conflict to make difficult the question concerning grounds for removal. On one hand, because the management of the corporation is entrusted to the directors, the shareholders may not instruct the directors as to the manner in which they should run the business, and a right to remove

110 These terms, plus "pirates," "looters," and "scavengers" are some of the most common terms used to describe insurgents, especially in the context of takeover bids.
111 It is the position of the author that there is room for the introduction of a qualified right to inspect corporate books and records in England.
112 Another advantage possessed by incumbents is the leeway they have in fixing the date of the annual meeting. A recent American decision upheld the convening of an annual meeting eight months after the earlier one, despite the insurgents' charge that this was a move to stave off an emerging proxy battle. Mansdorf v. Unexcelled, Inc., 28 App. Div. 44, 281 N.Y.S.2d 173 (Sup. Ct. 1967). Cf. Northwest Indus. v. B.F. Goodrich Co, 301 F. Supp. 706, 709, n.7 (N.D. Ill. 1969).
113 In the United States this is normally done by a statutory provision. See MBA § 33 (rev. § 35). In England the statutes are silent, and it is customary for the articles of association to set out such a rule. Table A, Companies Act, 1948, § 80.
114 Automatic Self-Cleansing Filter Syndicate Co. v. Cuninghame, [1906] 2 Ch. 34; Salmon v. Quin & Axtents Ltd., [1909] 1 Ch. 311, aff'd [1909] A.C. 442; Shaw & Sons
directors at any time without cause comes painfully close to allowing the shareholders to instruct puppet directors in the management of the business. On the other hand, the ultimate control that shareholders possess over management is their right to hire and fire, and depriving shareholders of the right to remove at will renders corporate democracy a mockery. The stricter the requirement of a special majority for removal, the more entrenched directors become during their term of office. The following sections analyze English and American solutions or proposed solutions of this dilemma.

I. England

Until 1947, the English Companies Act did not regulate the voting power needed for removing a director. It was customary for companies to provide that only by extraordinary or special resolution might a director be removed. The company law revision committee, known as the Cohen Committee, recommended strengthening shareholders' control over directors, and to achieve that result Section 184 of the 1948 Act was passed. Section 184(1) provides that "a company may by ordinary resolution remove a director before the expiration of his period (Salford) Ltd. v. Shaw, [1935] 2 K.B. 113; Scott v. Scott, [1943] I All. E.R. 582; Charlestown Boot & Shoe Co. v. Dunsmore, 60 N.H. 85 (1880). This principle has been reenacted lately in the Bamford case. See generally Slutsky, The Relationship Between the Board of Directors and the Shareholders in General Meeting, 3 B.C.L. Rev. 81 (1968).

116 LATTIN, CORPORATIONS 213-14 (1959) emphasizes this point.

117 Ballantine, in discussing the principle that, unless a statute or the corporate constitution permits, directors cannot be removed during incumbency without cause, calls this an "unsound rule" because it infringes upon corporate democracy. H. BALLANTINE, CORPORATIONS 434 (rev. ed. 1946) [hereinafter cited as BALLANTINE].

The justification for the principle is that directors, "Unlike ordinary agents, occupy a unique position as top echelon officers of the corporation." LATTIN, id.

It has also been argued that allowing removal of directors is a "double-edged sword." In public corporations, directors usually have effective control over general meetings, and they will utilize the removal power to get rid of nonconforming colleagues. Beuthin, A Director Firmly in the Saddle, 86 S. Afr. L.J. 489 (1959).

118 Another customary provision was that directors could not be removed during office. Bushell v. Faith, [1970] 2 W.L.R. 272, 276. The practical impact of the two provisions was identical since it took a 3:1 vote to pass an extraordinary or special resolution and to amend the articles.

119 REPORT OF THE COMMITTEE ON COMPANY LAW AMENDMENT, Cmd. 6659, 124 (1945) [hereinafter cited as the COHEN REPORT].

1116 "Ordinary resolution" is not defined in the Companies Act. The term is used to mean that a bare majority of the votes cast is needed to pass the resolution. Special or extraordinary resolutions need a three-quarters majority to pass.
of office, notwithstanding anything in its articles, or in any agreement between it and him."

The section, which further requires special notice of the proposed removal and election of a replacement to be sent to voting shareholders, means that advance notice must be given four weeks prior to the meeting by the person making the proposal to the company, and by the company to the shareholders. The company must send a copy of the removing resolution to the concerned director, who has a right to be heard on the resolution at the meeting, and who can require the company to circulate his defense representation among the shareholders at corporate expense. Nevertheless, the company or any other aggrieved party may apply to the court for permission to deny the director's right of circulation because "it is being abused to secure needless publicity for defamatory matter." These procedural safeguards for the directors do not apply when the corporate constitution permits removal by a simple majority without these safeguards.

Recently, the English courts have faced the difficult problem whether Section 184 can be circumvented by arming the incumbent directors with rights sufficient to defeat their removal. In the case of Bushell v. Faith, the incumbent took refuge in an article of association that weighted the voting power of directors for the sole purpose of defeating

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120 The removal may be a breach of a service contract. The incumbents might well arm themselves with service contracts that would make their dismissal costly. Companies Act, 1947, § 184 does not interfere with the contractual rights of the director. Gower, supra note 18, at 134-36.

121 Companies Act, 1948, § 184(2).

122 Id. at § 142. If a written personal notice is sent, the period is two weeks; if another channel of communication is used, the period is three weeks. Id. at §§ 142, 133(2) (b).

123 Id. at § 184(2).

124 Id. at § 184(3). If the company does not comply, the director has a right to have his circular read at the meeting in addition to his right to address the meeting. It seems that the substitution right is useless, since by the time of the meeting, the impeaching faction may very well have obtained sufficient proxies to carry the vote. Hopefully, should the matter come before the courts, they would adjourn the meeting and decree compliance by the company rather than permit the violator to redeem himself so cheaply.

125 Id.

126 This is because Companies Act, 1947, §§ 184(2) & (3) refer only to removal resolutions under § 184. Gower, supra note 18, at 134, n.59 § 184(6) specifically preserves more far-reaching removal powers under the corporate constitution.


a removal resolution. Although the incumbent held only one-third of
the outstanding shares, he outvoted the controlling shareholders and re-
mained in office. The House of Lords decided subsequently that the
article in question did not run afoul of Section 184(1).129 The decision
of the majority in the House of Lords was labeled by one scholar as de-
rising from an application of “desolating logic.”130 The circumstances
in Bushell v. Faith did not call for strict construction. In an attempt to
cumvent Section 184(1), an article granting a veto power to direc-
tors relative to their removal, instead of providing that “a director may
veto his removal,” the court said that “in the event of a resolution . . .
for the removal from office of any director, any shares held by that di-
rector shall . . . carry the right to three votes per share.” The court
could easily have rewritten the article and decided that it ran contrary
to Section 184(1). The fact that multiple voting rights are not con-
demned does not compel a conclusion that every utilization of weighted
voting rights is valid. Thus, when the avowed objective of a gimmick
is to prevent removal where Parliament stated that removal will ensue,
a court should have no problem in implementing Parliament’s will. In
short, the reasoning of Lord Morris of Borth-Y-Gest and of Justice
Ungoed-Thomas is much more appealing than that of their brethren.

Bushell v. Faith suggests that if the incumbents can succeed in passing
two articles, one giving them a veto against their removal and the other
safeguarding the first article from any possible amendments (in both
cases, by means of loaded voting rights rather than a merely personal
veto), a shareholder who purchases even more than 75% of the shares
will have to wait until the term of office of the incumbents expires be-
fore he can achieve control. During their term of office, management

129 The rationale of the Court of Appeal and of the House of Lords was that as long
as multiple and restricted voting rights are generally recognized, no different rule can
apply to voting rights weighted specifically for blocking a removal resolution. Only
Lord Morris of Borth-Y-Gest endorsed the reasoning of Ungoed-Thomas J. of the
Chancery Division (not reported), who held that the purpose of the article in question
was to make a director irremovable and that it was tantamount to a requirement that
more than a simple majority he necessary for a removal.

Russell, L. J., in the Court of Appeal and Lord Reid in the House of Lords expressed
an obiter that voting rights weighted only for defeating an amendment of the articles
are valid also. The other justices did not address themselves to this issue. It seems,
however, that the principle espoused in Bushell v. Faith, that loading the voting power
for a particular resolution is valid, compels the same result as regards Section 10. Section
10 enables a company to amend its articles by a special resolution.

could completely control the company with perhaps only nominal ownership, depriving the concept of "shareholders' democracy" of its meaning.\textsuperscript{131}

2. The United States

American shareholders have an inherent common law right to remove directors for cause, even if such right is not expressly stated in the corporate constitution.\textsuperscript{132} Whether or not there is a specific provision to this effect, an opportunity to be heard must be given to the concerned director. The courts will pass on both the adequacy of the opportunity to explain the charges and the question of whether the charges indeed constitute a cause for removal.\textsuperscript{133} Removal without cause is possible only if there is a permissive clause in the governing statute or in the corporate constitution.\textsuperscript{134} Only a few states have adopted the optional provision of the Model Business Corporation Act (MBA),\textsuperscript{135} which states that a majority of shareholders may remove directors without cause,\textsuperscript{136} and other states have provided by statute that such removal will be valid if the charter contains a permissive provision.\textsuperscript{137} The effect of the latter statute is to prevent a contention that removal without cause violates the statutory provision that the business shall be managed by the

\textsuperscript{131} This analysis assumes that clauses granting a class vote to a "class" of shareholders to block an amendment to the articles which affects their rights are valid, and that directors constitute a "class" worthy of such a protecting clause. The validity of such protecting clauses had been assumed until the issue recently arose in Australia. While one case upheld an article conferring a class vote (Crumpton v. Morrine Hall Pty. Ltd., (1965) 82 W.N. (Pt. 1) (N.S.W.) 456), a second found it of no avail (Fischer v. Easthaven Ltd. (1963) 80 W.N. (N.S.W.) 1155). Both cases are discussed in Baxt, \textit{The Variation of Class Rights}, 41 Aust. L.J. 490 (1968). See Prentice, \textit{Removal of Directors from Office}, 32 Mod. L. Rev. 693, 696 (1969). On the question of blocking amendment of articles, see also Hahlo, \textit{Restrictions on the Alteration of Articles}, 86 S. Afr. L.J. 349 (1969).


\textsuperscript{133} See cases cited note 132 \textit{supra}.

\textsuperscript{134} See the references in Cary, \textit{supra} note 83, at 128 n.7.

\textsuperscript{135} MBA \textsection 36 A (rev. \textsection 39).

\textsuperscript{136} Cal. Corp. Code Ann. \textsection 810 (1955); Gen. Stat. N.C. \textsection 55-27(f). The provisions prevent circumvention of cumulative voting. If there is cumulative voting, a removal resolution against which sufficient votes to elect the director were cast is invalid. Cumulative voting is nonexistent in England. Gower, \textit{Some Contrasts Between British and American Corporation Law}, 69 Harv. L. Rev. 1369, 1390 (1956) [hereinafter cited as \textit{Gower}].

\textsuperscript{137} E.g., N.Y. Bus. Corp. Law \textsection 706 (b) (McKinney 1963).
board. In most states, even today a successful bidder must wait until the annual meeting to place himself in control. Commenting on this arrangement, Professor Gower in 1956 wrote that the rule prevailing in most American states seemed strange, and his comment has lost none of its force with age.

3. Comparison

English law is superior in this respect to the American system, and hopefully, more American states will implement the provisions of the Model Business Corporation Act. Even so, English provisions are not perfect, as shown by the case of Busbell v. Faith, and there is room for tightening Section 184 to prevent circumventing devices.

C. Proxy Regulation

1. England

When the legislature finally regulated proxies in 1947, it also broached the questions herein considered. Management can send proxies and proxy statements at the corporation's expense, and designate its nominees as proxies. However, if "invitations to appoint as proxy a person or one of a number of persons specified in the invitations are issued at the company's expense," they must be sent to all shareholders alike and not just to those friendly to management. The proxy can be a one-way proxy. Aside from the common law rules concerning

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138 Gower, supra note 136, at 1389.
139 This discussion is included here to provide an overview of access to the proxy machinery by incumbents and insurgents. Because this material is a subject in itself, only a brief discussion appears here. See also pp. 433-34 supra for a discussion of the English shareholders' proposal rule.
140 Most of the recommendations of the Cohen Committee (Cohen Report, ¶ 132-34) were implemented by Sec. 5 of the 1947 Act, reenacted in § 136 of the 1948 Companies Act. The section entitles every shareholder to appoint a proxy, whether or not a member, who in private companies may also speak at the meeting. § 136(1). A proxy may vote only at a poll. § 136(1)(c). The shareholder's right to appoint a proxy must be stated prominently in the notice calling for the meeting. § 136(2). See further Gower, supra note 18, at 434-87.
141 Companies Act, 1948, § 136(4).
142 Id. This reverses the common law rule of Wilson v. L.M.S. Ry., [1940] Ch. 393.
143 The British Federated Stock Exchanges require a two-way proxy by listed companies. Stock Exchange Rules, Sch. VIII, Part A, ¶ 14. The Cohen Committee refused to recommend such a statutory rule, fearing its rigidity, and preferred to leave the matter with the exchanges, which can apply the rule flexibly. Cohen Report, Cmd. 6659, ¶ 132 (1945). The Jenkins Committee recommended that a statutory requirement of a two-way proxy be enacted. Jenkins Report, ¶ 464.
fraudulent and negligent statements, there is no regulation of the content of the proxy material.

2. The United States

The "proxy section" of the 1934 Securities Exchange Act, Section 14(a), was designed to promote the suffrage rights of shareholders, and to insure a higher standard of conduct by management. State laws, securing only the right to appoint a proxy, did not regulate the procuration of proxies. Abuses by management of their control of the proxy machinery led to a national regulation. Section 14(a), laying only the foundation, made it unlawful to solicit proxies in interstate commerce in contravention of proxy rules to be promulgated by the SEC "as necessary or appropriate in the public interest or for the protection of investors." At first, the proxy rules required only adequate information and full disclosure by shareholders. However, it soon became SEC policy to facilitate the opposition's presentation of its views to shareholders in order to achieve "fair corporate suffrage." Hence, Rule 14a-7 requires management, which solicits proxies, either to

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144 *Gower, supra* note 136, at 1393 wrote: "[T]he common law rule banning trick or misleading circulars [is] a rule which the English courts have perhaps developed further than the American." Examination of the American common law reveals that the Americans do not really lag behind. *Eisenberg, supra* note 57, at 1492-93, n.13, gathers the references.


147 Axe, *Corporate Proxies*, 41 Mich. L. Rev. 38, 46-48 (1942). This in itself was a breakthrough from the common law rule that allowed voting by proxy only if the corporate constitution so provided. Id., at 38-46. Today each state secures the right to vote by proxy. L. Loss, *Securities Regulations* 857-58 n.1 (1961) [hereinafter cited as Loss].

Today there is state proxy regulation, modeled on the SEC proxy rules, as regards insurance companies. This is done to enable the insurance industry to avoid the effect of the 1934 Act, since § 12(g)(2)(G)(II) of the 1934 Act, 15 U.S.C. § 78l(g)(2)(G)(II) (1964), conditions the exemption from the 1934 Act on such state regulation.

For state regulation of any corporation, see the rules of California, Cal. Corp. Code Ann. § 3637 (1955), the pioneer in this area.

148 See note 146 supra.

149 For a description of the development, see Friedman, *S.E.C. Regulation of Corporate Proxies*, 63 Harv. L. Rev. 796, 808 (1950). Loss 121-31. Yet, as *Eisenberg, supra* note 57, stated, even today "the Proxy Rules deal elaborately with the information that must accompany a proxy solicitation, but only tangentially with access to the corporate proxy machinery." Id. at 1493.

150 17 C.F.R. § 240.14a-7 (1971).
supply a shareholders list to any voting shareholder, or forward his proxy material to shareholders on the latter’s account. Doubtless management will choose to forward the material instead of providing a shareholders list.\textsuperscript{161} In the latter instance, shareholders are not exposed to personal solicitation by the insurgents. However, Rule 14a-7 does not preempt the common law right to obtain a shareholders list for a corporate purpose,\textsuperscript{162} but enables insurgents to bring their campaign to shareholders and still fight management for the shareholders list in court. Another rule, Rule 14a-8,\textsuperscript{163} gives the insurgents a “free ride” on the corporate treasury. Any voting stockholder can compel management to include in its proxy statement a proposal\textsuperscript{164} that is a “proper subject for action by security holders” under the laws of the corporation’s domicile.\textsuperscript{165} If management opposes the proposal, it is also obliged to include

\textsuperscript{161} Loss 890-94.


\textsuperscript{163} 17 C.F.R. § 240.14a-8 (1971).

\textsuperscript{164} There are two important limitations on the scope of the rule. First, it does not apply to elections for office. Second, it does not extend to counter-representations to management’s proposals. \textit{Id.} The English scheme, discussed in pp. 433-34 \textit{supra}, does not contain any of these restrictions. Rule 14a-8 also contains safeguards against abuses by repetitious harassing proposals. \textit{See} Rules 14a-8(c) (3) & (4), 17 C.F.R. § 240.14a-8(3) & (4) (1971).

\textsuperscript{165} Rule 14a-8(c) (1), 17 C.F.R. § 240.14a-8(c) (1) (1971). It is a difficult question whether the propriety of the proposal should be decided under federal or state law. \textit{See} S.E.C. v. Transamerica Corp., 163 F.2d 511 (3d Cir. 1947) cert. denied 332 U.S. 847 (1948); Brooks v. Standard Oil Co., 308 F. Supp. 810 (S.D.N.Y. 1969); The Dyer cases, especially Dyer v. S.E.C., 289 F.2d 242 (8th Cir. 1961) and Dyer v. S.E.C., 266 F.2d 33 (8th Cir. 1959). For references to S.E.C. decisions and to writings, see Eisenberg, \textit{supra} note 57, at 1523 n.133.

Rules 14a-8(2) and 14a-8(5) go further in restricting the shareholders’ proposal rule. The former excludes proposals submitted “for the purpose of enforcing a personal claim or redressing a personal grievance against the issuer or the management, or primarily for the purpose of promoting general economic, political, racial, religious, social or similar causes.” The latter excludes proposals consisting of “a recommendation or request that the management take action with respect to a matter relating to the conduct of the ordinary business operations of the issuer.”

The eligibility of two recent, celebrated proposals revolved around these rules. The first involved Ralph Nader’s Project on Corporate Responsibility proposals for General Motors’ 1970 annual meeting. \textit{See} Schwartz, \textit{The Public Interest Proxy Contest: Reflections on Campaign GM}, 69 Mich. L. Rev. 421 (1971). The second involved the Medical Committee for Human Rights’ proposal that Dow Chemical stop manufacturing napalm. Although the SEC held the management was warranted in refusing to include this proposal in its proxy statement, a court held that it had the power to review the SEC
in its proxy statement a statement of the proponent in support of the proposal in not more than 100 words. Certain aspects of Rule 14a-8 go further than its English counterpart: the presentation of opposing views is at corporate expense; the right is given to every voting shareholder; and the right is not limited to annual meetings. On the other hand, the English section allows a statement of 1,000 words, while the American rule allows only 100 words. As in many other areas, the English lag in enforcement devices. In a clear case of unjustified refusal by management, the SEC will obtain an injunction against management's solicitation, but in England, the shareholder himself must go to court in all cases.

Other aspects of the proxy rules also merit mention. The proxy rules apply not only to all listed companies, but since 1964, to those companies whose gross assets exceed $1,000,000 and which have at least 500 holders of record of equity securities. The rules apply to all the decision. Medical Comm. for Human Rights v. S.E.C., CCH Fed. Sec. L. Rep. ¶ 92,708 (C.A.D.C. 1970).

Anticipating that an increase in the number of shareholders' proposals will result, the SEC is now reconsidering the proxy rules. CCH Fed. Sec. L. Rep., Report Letter No. 337, p. 5, Nov. 11, 1970. See also the letter of the SEC Division of Corporate Regulation directing the Fidelity Trend Mutual fund to include in its proxy material a controversial shareholders' proposal. The proposal would require fund managers to consider, in deciding whether to invest in a certain corporation, the corporation's record on pollution control, minority hiring, and operations in South Africa and Rhodesia. CCH Fed. Sec. L. Rep. ¶ 78,070. See generally Bane, Shareholders Proposals on Public Issues, 26 Bus. Law 1017 (1971); Note, Proxy Rule 14a-8: Omission of Shareholder Proposals, 84 Harv. L. Rev. 700 (1971).

The English section does not explicitly contain similar restrictions. However, it applies only to resolutions to be moved at the meeting. The division of power between shareholders (general meeting) and directors will probably be read into the section to restrict the qualifying proposals.

Companies Act, 1948, § 140.

This enables "the statement to be expressed in reasonable English instead of jingle-ese." Gower, supra note 136, at 1393.

1934 Act, §§ 12(a) & 12(g), 15 U.S.C. §§ 78 1(a) & (g) (1964). The proxy rules apply also to shares of registered investment companies and registered holding companies and their subsidiaries. Investment Companies Act, Rule 20a-I(a), 17 C.F.R. § 270.20a-1(a) (1969); Public Utility Holding Companies Act, Rules 60-61, 17 C.F.R. §§ 250.60-61 (1969). The Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency promulgated similar rules for the banks that they regulate.

Until 1964, Gower's criticism of the American scheme in which incumbents may solicit selectively or forgo soliciting and thus defeat the disclosure philosophy of the proxy rules was valid. Gower, supra note 136, at 1393. § 14(c), enacted in 1964, requires that nonsolicited shareholders be supplied by the corporation with "information sub-
factions in a contest. Insurgents have one concession: Rule 14a-2(a) enables them to solicit ten persons or less without being subject to the proxy rules.

The courts allow each faction standing to complain about the other. After standing was established for shareholders who themselves were not deceived by the alleged violation, came the landmark decision of the Supreme Court in J. I. Case Co. v. Borak. Borak firmly established that private rights may be implied from violations of the proxy rules. Shortly thereafter, the Second Circuit in Studebaker Corp. v. Gittlin decided that management may enjoin violations of the proxy rules. Although Gittlin may seem merely to apply the Borak holding to its own facts, it in fact embodies far-reaching implications, stating that management as such has a role to play in the enforcement of the proxy rules. Gittlin involved a proxy solicitation by the plaintiff to gather sufficient shares to qualify him under the New York provision for obtaining a shareholders list, as a prelude to a proxy fight for board representation. The court observed that damage to the corporation was possible because a control battle is often only the first stage in initiating a possibly damaging transaction, even without further resort to the proxy machinery. In fact, when considering whether the corporation had proved irreparable harm, a traditional condition for an injunction, the court held that the violation of the proxy rules per se constitutes such harm. The court did not even purport to consider the opposing view of allowing standing to the corporation, i.e., to the incumbent management. Its approach was totally pro-management. Citing the famous quotation from the Senate Report concerning “irresponsible outsiders seeking to wrest control of a corporation away from honest and conscientious corporation officials,” the court concluded that the target management is not intended to “maintain a posture of strict neutrality” in a control contest. Instead, the court allowed it to use the corporate treasury in its fight against the “raiders.”

159 17 C.F.R. § 240.14a-2(a) (1971).
162 Studebaker Corp. v. Gittlin, 360 F.2d 692 (2d Cir. 1966).
163 360 F.2d at 695.
Section 13(d), added by the Williams Act, and reinforced by Rules 13d-1 through 13d-3, also buttresses the defensive arsenal of the incumbents. This section requires an insurgent who purchases shares registered under Section 12 of the 1934 Act or shares of a closed-end investment company to file with the SEC, with target management, and with the Stock Exchange, a Schedule 13D, if the purchase results in his becoming a beneficial owner of more than five percent of the shares of the class. Avoidance of Section 13(d) is not possible by purchasing more than two percent during any twelve months.

For purposes of Section 13(d), two or more persons acting as a partnership, limited partnership, syndicate, "or other group for the purpose of acquiring, holding, or disposing of securities of an issuer" are deemed a person. This takes the "group" idea further than it generally applies in the 1934 Act by virtue of the definition of person in Section 3(a)(9). Under Section 16(a), a person who becomes a 10% holder of any equity security registered under Section 12 must file with the SEC and with the Stock Exchange a statement disclosing the amount of all equity securities held by him, and he must thereafter report changes in his holdings. Section 13(d) imposes heavier burdens. First, holdings of different persons must be aggregated for the purpose of Section 13(d) but not for Section 16(a). Second, the disclosure required under Section 13(d) is more detailed and revealing than that under Section 16(a). Under Section 13(d), the insurgent must disclose the purpose of the purchase, and if the purpose is to acquire control,

167 For an application of § 13(d) to restrain incumbents see the complaint filed by the SEC in S.E.C. v. Posner, CCH Fed. Sec. L. Rep. § 93,049.
170 The Williams Act set a 10% exempt limitation amendment. Pub. Law No. 91-567, Act of Dec. 21, 1970, however, lowered the floor to 5%. The reason for the amendment was that insurgents stopped short of purchasing 10% to avoid disclosure. 5% ownership was thought substantial enough to require disclosure. Statement of SEC Chairman H. Budge in Hearing Held Before the Subcommittee of Securities of the Senate Committee on Banking and Currency, 91st Cong. 2d Sess. 10 (1970) [hereinafter cited as March Hearing].
any plan or proposal to liquidate the target corporation, to sell its assets, to merge it with any other corporation, or to make any other major change in its business or corporate structure. The insurgent has to reveal, among other exposing disclosures, the source and amount of funds for the purchase, and arrangements for proxies he has with shareholders. Beginning with the original disclosure, the insurgent must file promptly with the SEC and send to the target and the Exchange amendments disclosing any material changes in the facts set forth in the original Schedule 13D statement. Thus, the insurgent is required to inform the incumbents about any new acquisition of shares, plans, and arrangements. The incumbents may utilize this valuable information to pressure lenders and shareholders, to construct antitrust obstacles, and to effect other defensive measures, limited only by their imagination.

One court has already decided that Sections 13(d) through 16(d) are a basis for private rights. In that case, a shareholder's action against an insurgent who failed to file either a 13(d) or 16(a) report was sustained on the theory that, had plaintiff known about the existence of a 10% shareholder, he would not have paid as high a price as he paid for shares in the company. The Seventh Circuit has recently assumed that Section 13(d) implies private rights, and that a target has standing to wage a Section 13(d) action. The court held that a Schedule 13D filing is required when holders of more than 10% (now 5%) agree to act in concert regarding a position against management by acquiring shares. A showing of agreement to act in concert plus a subsequent purchase by a member of the group creates a rebuttable presumption that the group has agreed to further its aims by purchasing shares. On this reasoning, the court upheld a wide preliminary injunction disfranchising the insurgent group. The shareholders were prevented from using their original as well as their new shares to convene a general meeting to have the board enlarged so that the president could be impeached.

176 The disclosure must be made within ten days of the purchase. A § 16(a) report need not be filed until the tenth day of the following month.
177 For a zealous criticism of § 13(d), see the testimony of J. Eskin in *March Hearings, supra* note 170, at 126-39.
The injunction would remain in force until it was determined that the insurgents had complied with Section 13(d). In short, the court thought that decreing compliance would not restore the status quo. Shareholders might have sold shares to insurgents or given them proxies before incumbents had a fair chance to present their case to shareholders, basing their decisions, *inter alia*, on statutory disclosures by insurgents.

The *Bath* court took great pains to demonstrate that its interpretation of Section 13(d) is buttressed by the legislative history 180 of the Williams Act, and protects shareholders, not incumbents. However, it is difficult to comprehend how Section 13(d) can be read in the manner of the Seventh Circuit. The section requires disclosures from "any person who, after acquiring . . . equity security is directly or indirectly the beneficial owner of more than 10 per centum of such class" (emphasis added), and verbal "acrobatics" cannot delete the words "after acquiring" from the section. Furthermore, the exception for purchases of not more than two percent during a year becomes meaningless under *Bath* if a group is the purchaser. The court was also unable to answer insurgents' contention that imposing disclosure duties on an agreement to upset incumbents, which contemplates share purchases, virtually nullifies the effect of Rule 14a-2(a) of the proxy rules. Rule 14a-2(a) exempts from the proxy regulation solicitation of less than ten persons. Insurgents forcefully argued that the exemption was designed to afford insurgents a degree of flexibility in making their preliminary sounding of strength, and to mitigate the inherent advantages that incumbents have in battles for control. The court was unable to explain why contemplation of purchases (evident by later purchases), usually an integral part

180 "[T]he group would be required to file the information called for in section 13(d) (1) within 10 days after they agree to act together, whether or not any member of the group had acquired any securities at that time." H. R. Rep. No. 1711, 90th Cong., 2d Sess. 8-9, 1968 U.S. Code Cong. & Adm. News 2811, 2818.

The court purported to rely not on this one passage but on "the overriding purpose of Congress in enacting [the Williams Act] to protect the individual investor when substantial shareholders or management undertake to acquire shares in a corporation for the purpose of solidifying their own position in a contest over how or by whom the corporation should be managed." *Bath Indus., Inc. v. Blot*, 427 F.2d 97 (7th Cir. 1970). Actually, the *Bath* proposition will assist incumbents only when insurgents purchase less than 2%. If insurgents purchase 2% or more, then under Sec. 13(d) (3) they must comply anyway. Under Sec. 13(d) (3), incumbents have only to show concert plus 2% purchase, not concert to acquire. Concert to hold suffices. Under the *Bath* test too, the duty starts only with the purchase; the insurgent has to file the 13D Schedule within ten days from purchase. Thus, *Bath* distorts the statutory language in those cases, probably few, where an insurgent group purchases less than 2%.
of a control battle, destroys the right to an undisclosed preparation for the contest. It is decisions such as Batt that call to mind Professor Manne's evaluation of the Williams Act as pro-incumbent legislation.\textsuperscript{181}

The proxy rules contain an anti-fraud provision, Rule 14a-9,\textsuperscript{182} which prohibits material misstatements or half-truths in proxy solicitation. Furthermore, it is now settled that Rule 10b-5 applies to proxy solicitation for securities transactions in any company, even those not registered under Section 12(g) of the 1934 Act.\textsuperscript{183} The requisite showing under Rule 10b-5 of a nexus with interstate commerce or the mails does not present serious difficulties. The required disclosures under the proxy rules serve as an important restraint on control-motivated transactions of directors that require stockholder approval. However, if management is ready to disclose that certain measures, such as staggering the board or raising the majority vote for merger, are designed to eliminate take over bids, its control over the proxy machinery may enable it to carry the vote.\textsuperscript{184}

While the SEC scrutinizes proxy materials of all factions, there is no similar governmental clearance in England. Only proxy material of the management of quoted companies must be cleared with the Exchanges.\textsuperscript{185} The SEC proxy rules require a proxy to be two-way for each matter referred to therein, unless it relates only to election to office.\textsuperscript{186} If a matter relates to election to office and other matters, it must provide means for the shareholder to withhold authority to vote for the election of directors.\textsuperscript{187} However, if the proxy form conspicuously so states, the proxy can be voted for election of the designees if the shareholders have not withheld authority.\textsuperscript{188} As a general rule, discretionary authority to the proxy is prohibited.\textsuperscript{189} The important exception to this rule concerns matters whose presentation at the meeting is unknown to the solicitors a reasonable time prior to the solicitation.


\textsuperscript{182} 17 C.F.R. § 240.14a-9 (1971).


\textsuperscript{186} Rule 14a-4(b) (1), 17 C.F.R. § 240.14a-4(b) (1) (1971).

\textsuperscript{187} Rule 14a-4(b) (2), 17 C.F.R. § 240.14a-4(b) (2) (1971).

\textsuperscript{188} \textit{Id}.

\textsuperscript{189} Rule 14a-4(c), 17 C.F.R. § 240.14a-4(c) (1971).
In such instances, the proxy material must specifically secure the right of discretionary vote.\textsuperscript{190}

D. Expenses of Proxy Battles

Easier access to the proxy machinery is not the sole advantage management possesses in a proxy battle.\textsuperscript{191} If management can finance the expenses\textsuperscript{192} of a proxy fight from the corporate treasury, its success is virtually assured. In response to the contention that its use of the corporate treasury is a misapplication of funds, management can raise two defenses. The first is that it is in the corporate interest to inform shareholders of the points in issue between the opposition and management. Management can support this contention by asserting that the insurgent’s policy is injurious to the corporation. The second, an argument relied upon by incumbents to justify their use of corporate funds, is that on most occasions the insurgents are themselves corporations, whose management draw upon their own corporate treasuries to finance

\textsuperscript{190} Rule 14a-4(c) (1), 17 C.F.R. § 240.14a-4(c) (1) (1971).

\textsuperscript{191} For an admirable discussion of the inherent advantage of the incumbents’ stockholders’ inertia, see A. Berle & G. Means, The Modern Corporation and Private Property 86, 88, 139 (1932); Douglas, Directors Who Do Not Direct, 47 Harv. L. Rev. 1305, 1315-17 (1934); Friedman, Expenses of Corporate Proxy Contests, 51 Colum. L. Rev. 951 (1951). See also In re Dorman, Long & Co., [1934] Ch. 635, 655-56.

\textsuperscript{192} A proxy battle is a very expensive, rather prohibitive proposition. See the data collected by Aranow & Einhorn, supra note 83, at 543-44, about the cost of some of the more vigorous proxy battles of the last two decades. See also Machtinger, Proxy Fight Expenditures of Insurgent Shareholders, 19 Case W. Res. L. Rev. 212, 213 (1968). The figure usually cited to underscore this point is the $2,159,000 cost of the two factions in the New York Central Railroad proxy fight of 1954. The insurgents won that battle and had the corporation defray their expenses. Gower put it aptly: “it meant that it cost the New York Central’s shareholders about two million dollars to substitute the management of Mr. Young for the management of Mr. White. I do not suggest that Mr. Young was not worth it, but the shareholders would presumably have been happier still if he had not cost them quite so much.” Gower, Company Directors and Take-Over Bids, 2 The Law in Action 119, 128-29 (1957).

Machtinger, id., at 213, gathered from the SEC Annual Reports that, in the years 1956-66, 26,152 proxy solicitation statements were filed with the SEC, but only 272 contests for the election of directors occurred, of which 168 were for the control of the board. The percentage of proxy contests to management’s proxy statements declined from 1.79% in 1958 to 0.80% in 1967. Hetherington, Fact and Legal Theory; Shareholder, Managers, and Corporate Responsibility, 21 Stan. L. Rev. 248, at 269, n.76 (1969). The resort by insurgents to takeover bids instead of proxy battles accounts for this decrease in proxy contests. Of 23 proxy battles during 1956-60, only 9 were fully successful. D. Austin, Proxy Contests and Corporate Reform 53-54 (1965).
proxy expenses. Consequently, if prohibited from access to the corporate treasury, the incumbent management would face a distinct disadvantage.

The first defense has been a primary issue in cases in both England and the United States. The second has not been squarely confronted in the reported cases and is more in the nature of an undercurrent, yet it cannot be easily disregarded. With their tendency to treat insurgents as underdog shareholders, some writers overlook the fact that, to the extent that management controls a corporation, the insurgent corporation represents the interests of its own incumbents. It is assumed that the insurgent has a business purpose in attempting to gain control, thus making it very difficult to bring an action for waste against the insurgent's management. In this light, a court's readiness to find a business purpose on the side of incumbent management is more understandable. However, the remedy for abuses by empire-seeking insurgent corporations should be to curtail these abuses rather than to allow their adversaries to respond with counteracting abuses. Judicial thinking in this area is examined below.

1. The English Approach

In England, the question of tapping the corporate treasury arose as early as 1886. In Studdert v. Grosvenor, the directors of the Army and Navy Co-operative Society were ordered in a derivative suit to

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103 Gower, supra note 18, at 630, presents this point.
   In the event of a proxy contest, if the directors may not freely answer the challenges of the outside groups and in good faith defend their actions with respect to corporate policy for the information of the stockholders, they and the corporation may be at the mercy of persons seeking to wrest control for their own purposes, so long as such persons have ample funds to conduct a proxy contest.
Eisenberg, supra note 57, at 1499-1502, submits that the prevention of a situation where management is forced to capitulate is the only justification for allowing management access to the corporate proxy machinery. Eisenberg, id., at 1500, suggests a matching rule: management will be allowed to use the corporate machinery (including funds) to the extent that that is necessary "to meet insurgents on equal terms."

105 An insurgent's management can draw on the resources of its corporation to finance the expenses of battle, but other corporations in the insurgent's "group" cannot contribute funds to the battle. Such contribution would be ultra vires and a waste of assets even if the target is a potential purchaser of the products of the contributors. See Kaufman v. Wolfson, 153 F. Supp. 253 (S.D.N.Y. 1957).

106 [1886] 33 Ch. D. 528.
terminate their practice of sending stamped\textsuperscript{197} proxies, with prepaid reply envelopes, designating\textsuperscript{198} directors as proxies.\textsuperscript{199} Justice Kay of the Chancery Division observed that “such a course of proceeding would practically give the directors power to determine in such manner as they might think fit any question that might arise at such meeting.”\textsuperscript{200} The court held that only printing and sending expenses of “proper forms of proxy papers”\textsuperscript{201} were intra vires. Proper proxies were those which “would not tend in any way to influence the votes of the shareholders receiving them.”\textsuperscript{202} Printing and posting expenses of improper proxies, as well as stamping expenses of the proxies and return posting expenses\textsuperscript{203} were ultra vires under any circumstances.\textsuperscript{204}

\textit{Studdert} was declared invalid by the Court of Appeal in \textit{Peel v. London \& North Western Ry.},\textsuperscript{205} a case involving a continuous fight over corporate policy,\textsuperscript{206} in which the directors employed the same procedure regarding proxies as in \textit{Studdert}. In addition, they bombarded\textsuperscript{207} shareholders with circulars and sent company officials to so-

\textsuperscript{197} Stamps on proxies pose little problem today. No stamp duty is now due on a proxy to vote at a single meeting and adjournments thereof. Stamp duty (of 10 s.) is due only on a general proxy to vote at more than one meeting. 1949 Finance Act, 12, 13 & 14 Geo. 6, c. 47, § 35 & Sch. 8. Gower, supra note 18, at 484, n.77.

\textsuperscript{198} See p. 445 supra.

\textsuperscript{199} The main issue in the case was the charging to the corporation of the costs of libel actions brought by directors. However, the issue of the charging of proxy expenses was not geared to a general meeting held to ratify the litigation costs. See the editor’s note accompanying the reported case, Studdert v. Grosvenor, [1886] 33 Ch. D. 528, at 531. The halfhearted attempt of Buckley, L. J., in the \textit{Peel} case to explain \textit{Studdert} as relating only to proxies to approve the legal charges cannot be accepted.

\textsuperscript{200} Studdert v. Grosvenor, [1886] 33 Ch. D. 528, 539.

\textsuperscript{201} Id. at 540.

\textsuperscript{202} Id. It seems that it follows from the court’s formulation that expenses due to attempts to persuade the shareholders through circulars of the merits of the directors’ stance are also not chargeable to the corporation. Only a two-way proxy not accompanied by a proxy statement would qualify if the court’s statement is taken literally.

\textsuperscript{203} The court reasoned that proxies are a matter of convenience for shareholders. Therefore, “the directors have no more right to expend the funds of the company to promote the convenience in this respect of a shareholder, who may be too indolent to attend the meeting, than they would in providing him with posthorses or a special train to enable him to attend.” Id. at 539-40.

\textsuperscript{204} The court intimated that, even in cases of blank proxies, the expenses of the stamp on the proxy and the postage stamp for the return are an ultra vires misapplication of funds. Id. at 539.

\textsuperscript{205} [1907] 1 Ch. 5.

\textsuperscript{206} The points in issue were coordination with other railways, the size of wagons to be used, and the extent of elaboration of the company’s statistics and accounts.

\textsuperscript{207} Peel v. London N.W. Ry. [1907] 1 Ch. 5, 6.
licit personally certain shareholders. The court unanimously held that all the expenses were intra vires and chargeable to the company, reasoning that directors have a duty to take whatever steps are reasonably necessary to convene a general meeting and obtain the "best expression of the voice of the corporators in general meeting." Such expenses are, however, subject to two restrictions. They must not be excessive and must be "reasonably necessary" for obtaining the shareholders' views on the disputed subjects. It followed from this principle that the postage on proxies and return postage were chargeable to the corporation. These two expenses are neutral in that they merely make the voting rights more effective, and without more, do not promote the interests of management over the opposition.

A more difficult question appeared in regard to the expenses calculated to obtain the proxies for management. The court felt that directors have the additional duty to inform shareholders of all facts relevant to the business policy in issue which are known to them by virtue of their corporate position. Such information was considered essential for the shareholders to shape an intelligent decision. The court went further and disposed of the case by holding that directors also have a duty and a right to advise shareholders of their opinion, i.e., of the best course for the corporation to follow. The duty to advise legalizes expenses calculated to influence or to solicit. In other words, incumbents may take not only the steps necessary to inform shareholders, but also those necessary to effectively present management's case, such

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208 Id. at 18.
209 Id. at 19.
210 In the oft-quoted words of Vaughan Williams, L. J.:

Is it to be said that the board of directors of a company, whether a railway company or other company, who have had to adopt a particular policy, when that policy is impeached by others (be the number of those who impeach big or small) have not the positive duty to inform the shareholders what have been the reasons for the policy which has been theretofore adopted, and why they think that that policy should be maintained in the future? I cannot myself understand any one having a doubt as to the directors having that duty. . . . I't is their duty to give information of the facts which they think justify the policy. It is their duty to put forward to the company those reasons which they think justify the policy which the company with their assistance as managers has adopted, and to say to the company, if they think in good faith that it is the best advice, 'Do not attend to those people who are circularizing you to set aside the policy of the company up to this date, but on the contrary trust us and leave it to us.' Id. at 12.

211 The decision of Vaughan Williams, L. J., alludes also to the "raiders" contention in support of the court's proposition:

The attack in this particular case happens to be an attack by an association of high-minded gentlemen who only have the interests of the company at heart;
as circulars and personal solicitations. The court's holding was formulated by Lord Justice Buckley.

The point here decided is that directors bona fide acting in the interests of the corporation, and not to serve their own interests, are entitled and bound to inform and guide the corporators in matters affecting the corporate interests and any expenses reasonably incurred in so doing may be borne out of the funds of the company.

The Peel decision is appealing inasmuch as it seeks to make the suffrage rights of shareholders meaningful. Indeed, there is no point in going half way, charging part of the expenses of executing a proxy to the corporation and part to the directors. Nevertheless, it does not follow that all of management's expenses in a proxy fight should be borne by the corporation. The farther one moves from the expenses for facilitating the exercise of the franchise, the more questionable becomes the corporate interest in the expenses. To start from the outer limits, it can hardly be said that the expenses for all the gimmicks that usually accompany a political campaign are a matter of corporate interest. Such expenses do more than inform shareholders; they apply hard pressure on them to support management. Therefore, the reasoning of the court in Peel that the same rule should apply to expenses for informing and persuading would seem fallacious.

With respect to expenses for informing, the question arises as to the partiality and selectivity of the information that management might...

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212 None of the three Justices (Vaughan Williams, L.J., Fletcher Moulton, L. J., and Buckley, L. J.) addresses himself specifically to the question of personal solicitations by corporate officers. It appears that the court endorsed counsel for defendants' contention that "[i]f it is lawful for directors, as one set of officials, to send out circulars conveying information, it is also lawful for the minor officials of the company to convey information and ask shareholders whether they will support the policy of the directors. The company is entitled to the assistance of all its officers." Id. at 9. Query whether the company is entitled to outside assistance (proxy solicitors)?

213 Id. at 21.

214 In this category are included expenses for drafting, printing, and sending the notice of a meeting and an accompanying proxy; expenses for the convention and holding of the meeting, for processing the adequacy of proxies, and for the ballot and processing of the results.

215 In this category are included persuasion expenses: public relations, proxy solicitors, personal campaigning and soliciting, and entertaining voters, for example.
furnish. The safeguard against a one-sided presentation of the issues in dispute lies in the common law rules\textsuperscript{216} prohibiting fraudulent or negligent misrepresentations.\textsuperscript{217} Furthermore, the adversary system can be relied upon to bring out the omissions and falsehoods in the board's statements.

If such is the case, the insurgents' circulars,\textsuperscript{218} even circulars of unsuccessful insurgents, are of corporate interest much the same as the incumbents' circulars. Insofar as the insurgents advocate changes in policy, the information that they possess is relevant to shareholders. Moreover, defeated incumbents are not obliged to return the proxy battle expenses. Why should the law regard insurgents differently?

Likewise, there is an ever-existing danger that an attempt to take over simply for control per se will be described as a battle over policy. A similar danger exists relative to management's motivation for a proxy fight. In \textit{Peel}, it was admitted that management had "policy" motives. Moreover, the opposition tried only to pass certain resolutions and change business policy, not to grasp control itself. The court did not have to deal with the question of how to determine management's motives.\textsuperscript{219} The better rule, it seems, would place the burden of proving

\textsuperscript{216} Only the common law rules apply. The Prevention of Frauds (Investments) Act 1958, 6 & 7 Eliz. 2, c. 45, § 13 does not apply because the solicitation is directed toward obtaining proxies, not toward influencing a sale or purchase. The 1967 Misrepresentation Act, 16 & 17 Eliz. 2, c. 7, does not apply because there is no contract between the solicitor and the shareholders. Appointing a proxy, although a consensual transaction, is not a contract.

\textsuperscript{217} Courts do not hesitate to vitiate resolutions passed as a result of "tricky" circulars. Baillie v. Oriental Tel. Co., [1915] 1 Ch. 503; Tiessen v. Henderson, [1899] 1 Ch. 861; Kaye v. Croydon Tramways Co., [1898] 1 Ch. 358. See also \textit{Gower}, supra note 18, at 482.

\textsuperscript{218} Note that reimbursing a successful insurgent will not put him on the same footing with incumbents because the insurgent will still need a bridging loan, which might not be available.

\textsuperscript{219} Buckley, L. J., went to great pains to go on record that a control-motivated expense is a misapplication of funds. Those who are conversant with the affairs of joint stock companies are well aware that cases often arise in which the board in power are anxious to maintain themselves in power, to promote their own re-election or to drive the policy not really in the interests of the corporation, but for some private purpose of their own, down the throats of the corporators at a general meeting, and in which they issue at the expense of the company circulars and proxy papers for the purpose of attaining that object. When a case of that kind comes before the Court, I sincerely trust that the decision of this Court in this case will not be cited as any authority for justifying the action of the directors. \textit{Peel} v. London N.W. Ry., [1907] 1 Ch. 5, 21.

However, incumbents so well manage with the \textit{Peel} rule that no control-motivated case has come before the courts.
the “policy” motivation on management, which is justified by management’s ultimate knowledge of its motives and by the simplicity in converting a fight over personalities to a fight over policy. Moreover, the change in personalities, even if inspired only by a desire to grasp control, almost always causes some change in business practices. The Peel rule\textsuperscript{220} virtually enables management to charge the expenses of the proxy battle to the company. Even shifting the burden of proof is no more than a minimal safeguard, as insurgents usually advocate (in their election platform) changes in business policy, whether the business record of management is good or bad. Thus, they supply management with evidence that the contest is one of policy rather than of personality questions.

To revert to the recovery at least of a successful insurgent’s expenses, it is germane to note that frequently the insurgent is a corporation. The meaning of a recovery rule would encumber the target corporation with the expenses of both its ousted management and the insurgent, while the latter remains intact. Should the shareholders of the insurgent bear the expenses of the takeover only to the extent of the insurgent’s holding in the target? Section 140(1) of the 1948 Companies Act implies that such is the rule if the insurgent passes a resolution at the target corporation’s general meeting to such effect. Legal writers disagree\textsuperscript{221} whether the rule of Section 140(1) is limited to instances where the mechanism of the section is followed,\textsuperscript{222} or whether it expresses an application of a general rule. Against the generality of the rule, it has been argued that reimbursement of the insurgent would be an ultra vires waste of assets.\textsuperscript{223}

\textsuperscript{220} The most troubling aspect of Peel is that the expenses for personal solicitation of certain shareholders by corporate officials during working hours were approved in spite of the restrictions on reasonableness. See notes 209 & 213 \textit{supra}. One would hope that expenses for professional solicitors and entertainment of shareholders (the English learned quickly from the American example, see Gower, \textit{supra} note 192, at 126-27) are not reasonably necessary for effective franchise rights and presentation of management’s views. The practice in England is that management charges these costs too \textit{(id.), at 128}. Thus far no derivative suits have been brought.

\textsuperscript{221} Gower, \textit{supra} note 192, at 229, suggests that § 140(1) implies a general rule. Weinberg, \textit{Take-Over\textsc{s} and Amalgamations} 289 n.79 (2d ed. 1967) vigorously objected.

\textsuperscript{222} See pp. 433-34 \textit{supra}.

\textsuperscript{223} Weinberg, \textit{supra} note 221, citing Parke v. Daily News Ltd., [1962] Ch. 927, 954, and cases cited therein. Weinberg raises § 54 of the Companies Act, which prohibits a company to assist the purchase of its shares, as an additional reason for opposing Gower’s view in the context of takeover bids. § 54 is irrelevant in proxy battles since the corporate funds are not used “for the purpose of or in connection with a purchase”
It is submitted here that, in this respect, reimbursement of incumbents and insurgents should stand exactly on the same footing. The expense is intra vires insofar as it represents the cost of informing shareholders of the merits and the demerits of conflicting corporate business policies. It seems, however, that the Privy Council’s decision in *Campbell v. Australian Mutual Provident Society* 224 weakens the insurgents’ chances of recovering from the company.

In *Campbell*, the incumbents, seeking to amend the by-laws to expand the society’s business, solicited proxies for the amendment through circulars and personal solicitation by corporate officers. They also advertised their circulars. The proxies were one-way proxies that designated the directors as proxies. The insurgent group demanded that the directors also circulate at the society’s expense a circular on their behalf with a two-way proxy, and adjourn the called meeting to “enable members to have as full notice of the reasons against the extension policy as members had of directors’ reasons in favour of the same.” 225 The board refused the demand, and the insurgents brought an action seeking to establish that the by-laws were not properly amended, *inter alia*, because the incumbents had charged their expenses to the society and had refused to circulate the insurgents’ material. The action also sought to recover from the incumbents their proxy battle expenses. The Privy Council held that management had acted properly, noting that “it was right for the directors to give their advice and put things in train to enable the members to act upon that advice,” 226 and that it was proper to expend whatever funds they saw fit for this purpose. On the other hand, they held that there was “no obligation either legal or moral upon the directors” 227 to circulate the material of the insurgents.

Several points emerge from the opinion. First, the court explicitly upheld the utilization of corporate officers for personal solicitation. Second, the holding that the directors do not have a duty to circulate insurgent’s material might, on the rationale of the *Peel* case, lead one to conclude that the reimbursement of insurgents is ultra vires and not of shares. If, however, the proxy battle is only a prelude to a merger, § 54 might well become relevant.

225 Id. at 6.
226 Id. at 7.
227 Id. at 6.
capable of ratification by a general meeting.\textsuperscript{228} The third point, relating to the right of minority shareholders to bring a suit alleging misapplication of corporate funds to finance a proxy battle, necessitates a brief review of the previous cases.

In Studdert, the court allowed the minority action to be brought, accepting the allegation that the utilization of corporate funds to finance management's campaign is an ultra vires waste of assets.\textsuperscript{229} The expense was regarded as not capable of ratification and as challengeable under an exception to the rule of Foss v. Harbottle.\textsuperscript{230} In Peel, Lord Justice Buckley intimated that it did not appear that the expense could be regarded as ultra vires in the proper sense. He thought that the corporators were the best judges of what expenses were "reasonably necessary" to have effective representation of shareholders, and that the expense was capable of ratification.\textsuperscript{231} In other words, even if the court concluded that the directors did not have a right to draw upon the corporate coffers, a minority action could not prevail because the act was capable of ratification. The next step in this direction was taken in Campbell. The court assumed that misapplication of the assets does not amount to an ultra vires act, and that, because there was no allegation of fraud or bad faith, "this would be sufficient of itself to dispose of the whole appeal."\textsuperscript{232} This statement seems unfortunate and evidences the confusion in English law regarding minority suits. Expropriation of corporate assets is "fraud on the minority," even without bad faith.\textsuperscript{233} In light of the decisions holding that use of corporate assets for management's campaign is an application for corporate purposes, the holdings on insurgent's right to bring an action are thus only of academic value.\textsuperscript{234}

\textsuperscript{228} As Williams, L. J., stated in Peel, "[T]he question is whether they have the duty—a duty which might reasonably involve the issue of these circulars—for unless they have this duty, in my judgment they have no right whatever to issue them. [T]hey cannot as a board have a right to do anything which is not within the scope of the execution of the duties imposed upon them." Peel v. London N.W. Ry., [1907] 1 Ch. 5, 12.

\textsuperscript{229} Studdert v. Grosvenor, [1886] 33 Ch. D. 528, 534-35.

\textsuperscript{230} [1843] 2 Hare 461.

\textsuperscript{231} Peel v. London N.W. Ry., [1907] 1 Ch. 5, 19-20.

\textsuperscript{232} [1908] 99 L.T. 3, 6.

\textsuperscript{233} Gower, supra note 18, at 588.

\textsuperscript{234} If the holdings were that such use is not for a corporate purpose, the issue of a minority's standing would become significant. The Peel and Campbell cases would not recognize such standing. Interestingly enough, use of corporate powers and assets to fend off takeover bids was held to be not for a corporate purpose, but ratifiable. Yet a minority plaintiff is allowed standing. The action, however, is stayed and the matter
2. The American Approach

a. Corporate Underwriting of Incumbents

The difficult question of the defrayment of proxy battle expenses has been the subject of litigation in the United States more often than in England, and American literature on the subject is abundant. Naturally, a comprehensive analysis is beyond the scope of this article, and such will not be attempted here. The rule enunciated by case law has been that proper and reasonable management expenses in a bona fide battle over corporate policy are chargeable to the corporation. Policy issues, defined broadly, include, for example, conflict over a service contract of a director, and charges of self-dealings or self-serving transactions. Expenses for a battle over control per se are not chargeable to the corporation. The most difficult questions are (a) what expenses are proper and reasonable, and (b) on whom does the burden of proof as regards propriety and reasonableness lie.

It is agreed that the expenses of providing shareholders with wide-spread information relevant to the policy dispute are made for a corporate purpose. However, it remains somewhat unsettled whether expenses for solicitation are proper. Expenses for advising shareholders of management's position in the dispute are considered an integral part of the expenses of furnishing pertinent information for a reasoned decision. The major issue revolves around the propriety of expenses for solicitation that goes beyond advising. They include the funds expended for advertisements in the media, personal canvassing, employment of professional solicitors and of public relations firms, entertainment of shareholders, and the vast sums expended in "a strenuous campaign to persuade and cajole in a hard-fought contest for control."


See Aranow & Einhorn, supra note 83, chs. 20-22; M. Feuer, PERSONAL LIABILITIES OF CORPORATE OFFICERS AND DIRECTORS 115-21 (1961); L. Loss, SECURITIES REGULATIONS 857-66 (1961); Emerson & Latchman, Proxy Contest Expenses and Shareholders Democracy, 4 CASE W. RES. L. REV. 5 (1952); Emerson & Latchman, Proxy Contests: A Study in Shareholder Sovereignty, 41 CALIF. L. REV. 393 (1953); Friedman, Expenses of Proxy Contests, 51 COLUM. L. REV. 951 (1951); Machtinger, Proxy Fight Expenditures of Insurgent Shareholders, 19 CASE W. RES. L. REV. 212 (1968). See also, Note, 36 CORNELL L. Q. 558 (1951); Note, 43 VA. L. REV. 391 (1957) and the notes listed in note 242 infra. This list does not purport to be exhaustive.


Id., at 172, 128 N.E.2d at 295.
Most of the cases have arisen in New York and Delaware. At about the same time when the Peel case arose in England, the New York Court of Appeals passed on similar issues in Lawyers' Advertising Co. v. Consolidated Railroad Lighting & Refrigerating Co.\(^{238}\) The New York court, espousing a narrower rule than the English, held that expenses for advertising the convention\(^{239}\) of a special meeting were intra vires.\(^{240}\) However, the court decided that further expenses incurred in urging shareholders to execute proxies already in their possession and in counteranswering circulars of contestants were ultra vires as to the directors, but conceded "that the directors who caused this publication acted in good faith and felt that they were serving the best interests of the stockholders."\(^{241}\)

The dispute in Lawyers' Advertising, arising between the president and the board over alleged misapplication of assets by the president, probably would be classified in present day terminology as a policy dispute.\(^{242}\) Nevertheless, the court held that it would be dangerous to allow incumbents to charge to the corporation expenses for solicitation, by publishing advertisements, or "by analogy, of dispatching special messengers."\(^{243}\) The notices were "proceeding by one faction in its contest with another for the control of the corporation,"\(^{244}\) and did not serve any corporate purpose. In short, Lawyers' Advertising reached a result different from Peel as to expenses for soliciting, as distinguished from informing.

In 1955, when the question was reconsidered in New York in the cornerstone case of Rosenfeld v. Fairchild Engine & Airplane Corp.,\(^{245}\)

\(^{238}\) 187 N.Y. 395, 80 N.E. 199 (1907).


\(^{240}\) "Proper and honest corporate management was subserved by widespread notice to stockholders on questions affecting the welfare of the corporation, and there is no impropriety in charging the latter with any expenses within reasonable limits which were incurred in giving sufficient notice of a special meeting at which the stockholders would be called upon to decide these questions." Lawyers Advertising Co. v. Consolidated Ry. Lighting & Refrigerating Co., 187 N.Y. 395, 80 N.E. 199, 200 (1907).

\(^{241}\) Id. at —, 80 N.E. at 201.

\(^{242}\) See note 236 supra and accompanying text.


\(^{244}\) Id. at —, 80 N.E. at 200-01.

the court split 3:1:3. Judge Froessel and his two supporters ruled that in a contest over policy, corporate directors have the right to make reasonable and proper expenditures from the corporate treasury for the "solicitation of proxies and in defense of their corporate policies and are not obliged to sit idle by." 246 This includes expenses of "persuading the stockholders of the correctness of their position and soliciting their support for policies which the directors believe, in all good faith, are in the best interests of the corporation." 247 This parallels the rule laid down in Peel. As in England, the application of the rule favors incumbents even more than the rule itself.

The lower court in Rosenfeld had found as fact that "the management group incurred a substantial amount of needless expense which was charged to the corporation." Nevertheless, the incumbents prevailed because the plaintiff did not segregate the specific ultra vires expenditures. Judge Froessel's decision placed the burden of proof on the plaintiff 248 to establish the motivation of management and the impropriety and classification of expenses. Judge Desmond, in his concurring opinion, noted that only the expenses of serving formal notices and of routines proxy solicitation may be assessed to the corporation. Expenses for procuring proxies from informed shareholders are "intrinsically unlawful." 249 However, he shared the majority's view that the "burden was on plaintiff to go forward to some extent with such particularization and proof," 250 and that in failing to do so, plaintiff failed to establish a prima facie case.

Judge Van Voorhis, writing a strong dissent in which two of his brethren joined, vigorously rejected the distinction between policy battles and battles for control per se, pointing out how easily every battle can be depicted as one involving corporate policy. He thought that in any proxy battle "only such [expenses] as [are] reasonably related to informing the stockholders fully and fairly concerning the corporate

(1956); 31 N.Y.U.L. Rev. 825 (1956); 31 Notre Dame Law. 308 (1956); 23 U. Chi. L. Rev. 682 (1956); 24 U. Cin. L. Rev. 606 (1955); 7 W. Res. L. Rev. 198 (1956).


247 Id.

248 The action was a derivative one. Plaintiff's standing to trigger a corporate suit for waste of assets was not doubted.

249 Id. at —, 128 N.E.2d at 295 (1955). Desmond, J., was of the opinion that a ratification by a general meeting is therefore of no avail.

250 Id. at —, 128 N.E.2d at 294.
affairs should be allowed,” and that expenditures beyond that should be ultra vires. Since the lower court found that there were some needless expenses, the plaintiff made a prima facie case. As in other instances where it is established that directors have a personal interest in a corporate expenditure that they have authorized, the burden is on them to go forward with the evidence of the propriety and reasonableness of specific items of expenditure.

From this analysis, clearly the majority of the court (Judge Desmond and the Van Voorhis group) was of the opinion that expenses of a solicitation campaign cannot be assessed to the corporation. The incumbent directors prevailed only because of the majority’s refusal to shift the burden of going forward with the evidence. As earlier noted, it is not the rule regarding intra vires expenses, but rather its application that tips the scale in favor of management.

The propriety of the expenses for exerting pressure on shareholders by hiring professional solicitors has been assumed in one New York case, but has been rejected by at least one jurisdiction and at one time by the SEC. Interestingly enough, the New York court supported its conclusion by arguing that the proxy rules contemplate the propriety of the employment of professional proxy solicitors. The proxy rules merely require that soliciting factions disclose their employment of proxy solicitors, their remuneration, and the financiers. The duty to disclose an act does not legalize that act.

In a leading Delaware case, Hall v. Trans-Lux Daylight Picture Screen Co., battle was waged between the views of Peel and Lawyers’ Advertising, and Peel prevailed. In the process, however, the facts and

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251 Id. at —, 128 N.E.2d at 297.
253 In re Zickl, 73 N.Y.S.2d 181 (Sup. Ct. 1947).
257 Several writers have made this point. For the references, see Aranow & Einhorn, supra note 83, at 559, n.55.
258 171 A. 226 (Del. 1934).
259 Somehow Peel was “americanized” into Pell in the court’s decision.
260 See note 235 supra.
principles of the two cases were stated inaccurately. The court finally concluded that in contests over policy as distinguished from contests over management personnel, incumbents may defray to the corporation expenses "reasonably necessary to inform the stockholders of the considerations which the directors deem sufficient to support the wisdom of the policy advocated by them and under attack, and in the same communications which the directors address to the stockholders in support of their policy they may solicit proxies in its favour."\(^{261}\) The decision does not detail the proxy expenses but it seems that all of them were to finance circulars. It should be noted that the Delaware court erroneously distinguished Lawyers' Advertising by maintaining that it dealt with a pure contest over personnel.\(^{262}\) Likewise, the Peel case was incorrectly described\(^{263}\) as a contest over policy arising in a directors' election. The court held that management can withdraw money from the corporate coffers, not only when a policy question arises in the abstract, but also when policy questions arise in a contested election. Observing that questions of policy and personnel are "inextricably blended,"\(^{264}\) the court found that a contested merger proposition and a suggested "spinning-off" of stock in a subsidiary were the basis of the conflict between the two slates. The court, finding as a matter of fact that policy issues were involved, did not dwell on the burden of proof.\(^{265}\)

As in other states, the outer boundaries of expenses chargeable to the corporation are not clear in Delaware.\(^{266}\) Most of the limited Delaware law on the subject has emerged from the continuous contest over the control of M.G.M.\(^{267}\) In Campbell v. Loew's Inc.,\(^{268}\) a fight arose between two factions of management, pitting the president and a minority of the board against the majority of the board. The president's slate represented a minority only because several of its nominees had resigned from the board. Although holding that the president's group had suffi-

262 See notes 242 and 235 supra and accompanying text.
263 Hall v. Trans-Lux Daylight Picture Screen Corp., 171 A. 226, 228-29 (Del. 1934).
264 Id. at 229.
266 In 1944, a federal court on a motion for a preliminary injunction observed that no Delaware case thus far had sanctioned the hiring of professional proxy solicitors by management at corporate expense. Hand v. Missouri-Kansas Pipe Line Co., 54 F. Supp. 649, 650, n.1 (D. Del. 1944).
267 For an account, see Cary, supra note 83, at 220-21. Finally, one insurgent (Kirk Kirkorian) succeeded in 1969 in taking over M.G.M. via the tender offer route.
268 134 A.2d 852 (Del. Ch. 1957).
cient "corporate status" to use corporate funds to present its position to stockholders, the court enjoined that group from using corporate facilities and employees in connection with its solicitation. The court based its injunction on the rationale that involving corporate employees in the dispute would carry the intra-corporate strife even deeper within the corporation. Because the chancellor noted that his decision was based on the corporate status of the two quarreling factions, the decision is not authority for the impropriety of management's using employees in its campaign against outsiders.

Recently, a federal court adopted a very liberal rule for Delaware in a later stage of the contest for control of M.G.M. In Levin v. M.G.M., Inc., 269 the court refused Levin's motion to enjoin the incumbent O'Brien's slate from using corporate funds to pay for the services of specially retained attorneys, two proxy soliciting firms, and a public relations firm, and from using services of employees in the solicitation campaign. To a large degree, the court based its decision on the regularity of M.G.M. management's use of all the challenged methods. Similarly, another Delaware case has implicitly sanctioned the employment of professional proxy solicitors. In Steinberg v. Adams, where "the contest was conducted by printed appeals for proxies addressed to the stockholders, and employment of proxy solicitors and other devices not unusual in such campaigns," 270 the court held that all the expenses were proper if management fought for its policy.

b. Corporate Reimbursement of Insurgents

On the question of reimbursing successful insurgents, a Delaware court 271 has held that defrayment of reasonable expenditures of the insurgent in a policy dispute, including reasonable expenses for proxy solicitors, if ratified by a general meeting, is a company expenditure expended for a corporate purpose. The court reasoned that in a proxy campaign over policy issues, the insurgent performs the same function as the incumbents, i.e., to supply relevant information to shareholders. The court analogized to a derivative suit in which the successful derivative plaintiff recovers his costs (including attorney's fees) on the theory

that he has benefitted the company.\textsuperscript{272} The court saw "no reason why the stockholders should not be free to reimburse those whose expenditures succeeded in ridding a corporation of a policy frowned upon by the majority of stockholders."\textsuperscript{273}

The New York Rosenfeld case declared the New York rule\textsuperscript{274} no more stringent than the rule in Delaware. Judge Froessels disposed of the point: "Where a majority of the stockholders chose . . . to reimburse the successful contestants for achieving the very end sought and voted by them as owners of the corporation, we see no reason to deny the effect of their ratification nor to hold the corporate body powerless to determine how its own moneys shall be spent."\textsuperscript{275} Judge Van Voorhis, dissenting, opined that the insurgents' expenses in their entirety could not be charged to the corporation. He thought that because the insurgents were not charged with the responsibility for operating the company, their expenses did not benefit the company. He emphasized that the ultimate success does not assure benefits to the company, and that agitation of corporate issues can result in corporate advantage even if an insurgent loses. In short, he thought that the expenses of insurgents are ultra vires and hence not capable of being ratified by a majority of shareholders. As in the role for corporate gifts,\textsuperscript{276} only a unanimous general meeting could sanction them.

Both the Delaware and New York rules assure \textit{successful} contestants of corporate underwriting. The ratification requirement is a mere formality, because the new incumbents who have just won a proxy fight will have no problem in obtaining ratification. Nevertheless, one should ask what is the basis for the requirement of ratification. Prima facie,

\textsuperscript{272}This analogy was rejected by Van Voorhis, J., in the New York Rosenfeld case as "entirely without foundation." Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291, 293 (1955).


\textsuperscript{274}In Cullom v. Simmonds, 285 App. Div. 1051, 1051-52, 139 N.Y.S.2d 401, 402 (2d Dept. 1955), the court held sufficient a complaint maintaining that reimbursement to successful contestants was illegal despite ratification because the insurgents' campaign was not directed toward sharpening corporate policy but toward grasping control and defaming some of the incumbents.

\textsuperscript{275}Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291, 293 (1955). Desmond, J., apparently agreed that ratification invalidates corporate defrayment of insurgents' expenses that meet the "test of propriety." It was improper expenses—he did not distinguish between incumbents' and insurgents'—that he thought could not be ratified. \textit{Id.} at ——, 128 N.E.2d at 295.

either the expense is for a corporate purpose and a board decision to reimburse will suffice, or it is for an ultra vires purpose and no ratification can validate it. One writer has suggested that ratification is needed because of the self-interest of the new board in reimbursing their fraction, but (with all due respect), that proposition seems untenable. The old management has the same self-interest, and its expenses are charged to the corporation without need for shareholders' approval. This asymmetry of the law seems inexplicable.

The rule for allowing recovery to the successful opposition, as fashioned by the courts, assures reimbursement in a contested election and denies it in a contested corporate transaction that needs shareholders' approval. This result exposes the weakness of the rule. When the dispute concerns policy alone, the insurgents must finance their campaign even if they win. When the fight concerns control, with only lip service paid to policy issues, successful insurgents have a right to bill the captured corporation.

Legal commentators have emphasized that the law should reimburse a meritoriously defeated opposition as well as a successful one, reasoning that in a policy dispute defeated oppositions contribute to the intelligent decision of shareholders and serve a corporate purpose. In short, they employ Justice Van Voorhis' contention that success is not the criterion, but reverse the argument to allow every meritorious opposition to defray reasonable campaign expenses. The problem is how to formulate a rule that will not open the floodgates and dilute corporate capital by underwriting endless fights. Some writers have suggested a quantitative

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277 M. Feuer, *Personal Liabilities of Corporate Officers and Directors* 118 (1961). Feuer also submits that "a conclusive presumption of corporate benefit arises from the adoption of such [advocated by insurgents] policies by the majority of stockholders." This seems a poor contention. Why is a majority decision to present a gift not a conclusive presumption of the benefit to the company of the gift?

278 Compare the English decisions of Hogg v. Cramphorn, [1967] Ch. 254, and Bamford v. Bamford, [1970] Ch. 212, where the courts held that issue of shares to thwart a takeover bid is valid if ratified by the general meeting. See also note 300 infra.

279 Grodetsky v. McCrory Corp., 49 Misc. 2d 322, 267 N.Y.S.2d 356 (Sup. Ct. N.Y. 1966), aff'd 276 N.Y.S.2d 841, 27 A.D.2d 646 (1966). That is true because only if the insurgents become incumbents can they pass the reimbursing resolution. The Grodetsky court reasoned that it could only scrutinize the reasonableness of an award voted by shareholders and could not decree one.
minimum score at the ballot;²⁸⁰ others have suggested advance scrutiny by the court.²⁸¹ Case law has thus far refused²⁸² recovery to defeated insurgents, and the suggestion²⁸³ that the S.E.C. prescribe such a rule under its rule-making power, delegated in Section 14(a) of the 1934 Act, has not been implemented.

c. Government Underwriting

Another aspect of the complex problem of financing proxy fights is the extent to which the incidents of a fight should be borne by the government by allowing the adversaries to deduct expenses. Concerning management’s expenses, although it has always been assumed²⁸⁴ (and has thus been the practice) that these expenses fall within Section 162(a) of the Internal Revenue Code²⁸⁵ as “ordinary and necessary” expenses in carrying on the business, the Internal Revenue Service (IRS) has recently denied the deduction of management’s expenses for legal counsel, proxy solicitors, and public relations experts. However, the federal district court of Connecticut has found the IRS's position untenable and has allowed the deduction.²⁸⁶ The IRS has since acquiesced, inserting a proviso that expenses “made primarily for the benefit of the interests of individuals rather than in connection with questions of corporate policy” will be disallowed as deductions.²⁸⁷ In short, tax law has followed corporate law.

²⁸⁰E.g., Friedman, supra note 235, at 963-64. For elaborate suggestions of criteria for screening, see Emerson & Latcham, SHAREHOLDER DEMOCRACY 142 (1954); Emerson & Latcham, Proxy Contest Expenses and Shareholder Democracy, 4 W. RES. L. REV. 5 (1952); Note, 61 YALE L.J. 229 (1952).
²⁸¹FEUER, supra note 277, at 121.
²⁸³Friedman, supra note 235, at 960.
²⁸⁴Note, 42 TEX. L. REV. 558, 559 (1964).
²⁸⁶Locke Mfg. Companies v. United States, 237 F. Supp. 80 (D. Conn. 1964). This case makes interesting reading also in regard to the corporate aspects of financing a proxy fight. The court relied heavily on Congress' aim to promote corporate franchise in order to establish the regularity of the expenses of a full-scale proxy campaign.

A recent case ruled that both ousted management's and successful insurgents' expenses are deductible by the corporation. Foundry Co. v. Commissioner, 49 T.C. No. 25 (1967).
Regarding the deductibility of the insurgents’ expenses, one must distinguish expenses of a corporate insurgent from those of an individual insurgent. The former may be deducted because the proxy fight is waged to promote a corporate and is thus an ordinary and necessary expense of carrying on a business. The latter will be allowed a deduction under Section 212 of the Internal Revenue Code only if he can show that the expense was ordinary and necessary “for the production of income” or “for the management, conservation, or maintenance of property held for the production of income.” While the IRS first contended that expenses of a proxy fight were not proximately connected with the increase of dividends or the increase in value of the stock to qualify under Section 212, federal courts in the fourth and fifth Circuits have rejected the IRS’s interpretation of Section 212. Thus, the principle has emerged from the case law that a taxpayer who does battle with management to increase or preserve his income, and who does so with a reasonable expectation of success in a struggle over policy rather than in a “vendetta,” may deduct reasonable proxy expenses.

The rule of deductibility of management’s expenses decreases the burden on the corporation, but does not decrease the advantage of the incumbents. The “smaller” corporate cost still sets in motion the same proxy campaign. On the other hand, deductibility is an important advantage to insurgents because it gives them a right to pass on a portion of the expenses that they could have otherwise recovered only if they had won an election contest.

289 Graham v. Commissioner, 326 F.2d 878 (4th Cir. 1964); Surasky v. United States, 325 F.2d 191 (5th Cir. 1963). The IRS has partially acquiesced in the holding in Surasky (“except to the extent that the court in its opinion indicates that to be deductible proxy fight expenses need not be proximately related to the production or collection of income or to management, conservation, or maintenance of property held for the production of income”) and fully in the holding in Graham: Rev. Rul. 64-236, 1964 Cum. Bull. 64, 65.
290 Dyer v. Commissioner, 352 F.2d 948 (8th Cir. 1965).
292 Presumably the incumbents may deduct their proxy expenses under § 212 of the Int. Rev. Code of 1954. Because their marginal tax rate may be higher than the corporate rate, they may be passing on to the corporation a higher cost than they would have had to incur themselves. Note that, in making a § 212 case, directors might have to argue that they fought for their salaried positions, not for policy issues.
d. Disfranchisement of Proxies Obtained by Illegal Use of Corporate Funds

In most cases, incumbents have already 293 tapped the corporate coffers to finance their campaign when the insurgents rush to court to seek an injunction. The question then arises as to what is an adequate remedy where the court finds that some or all of the expenses were improper. One might well argue that equity will be done if, in addition to ordering recovery, the court will disfranchise the proxies obtained through misapplication of corporate assets. The question, however, is not an easy one. Incumbents may reply that they had a right to spend their private fortunes on the campaign, and such is the result if recovery is ordered. Why penalize them when they can be charged interest? It seems, however, that merely ordering recovery is not a sufficient remedy. Access to the corporate till virtually assures the incumbents' re-election, and a rule that requires only the repayment of a loan forced on the corporation has little if any deterrent effect. Further, the incumbents might not have been able to borrow the funds from other sources, and they might not now command sufficient personal funds to account to the corporation. However, one court has intimated that in the ordinary case disfranchisement is not warranted, and that recovery would make whole the injury. 294

3. Comparison

The English rule presumably sanctions the charging of incumbents' expenses for persuasion to the company, 295 while the American law, at


295 It is true that both Peel and Campbell involved abstract battles over policy and not policy issues in a control battle. Presumably, however, the same rules apply in both instances. Such was the holding of the Hall case in Delaware. See p. 471 supra. In England, the requirements for quorum are usually much lighter than in the United States. (The rule of a closed agenda compensates for a small quorum. In the United States, the quorum is higher and the agenda much more open). Gower, supra note 139, at 1391; Garrett, Attitudes on Corporate Democracy—A Critical Analysis, 51 Nw. U. L. Rev. 310, 313 (1956). Thus the need to gather a quorum cannot be argued as a justification for hiring professional solicitors. American writers accept such justifications, Friedman, supra note 235, at 954. When, by virtue of a statutory provision or a provision in the corporate constitution, shareholder action of a specified majority is required, the persuasion expenses may be justified in England as well as in the United States.
least in New York, is unsettled on that point. To be sure, the English cases do not involve professional proxy solicitors or public relations men; however, the cases rely on the principle that expenditures for persuasion in a policy contest are part of making an effective case by management. Shifting the burden of proof has not been considered in England, and the chances for fashioning such a rule are slim. Similarly, England has no "fairness rule" for conflicts of interest. Self-dealing is voidable even if fair, unless the articles of association allow the transaction, or it is ratified by the shareholders. Hence, there are no precedents from which to analogize that the burden shifts to the directors to show that they were motivated by policy considerations, and that the expenses were reasonable. Furthermore, the question of reimbursement of successful or meritorious unsuccessful insurgents has not yet been litigated in England. On one hand, the English rules of corporate purpose and incidental benefit to the corporation are narrower than those of the United States. Even a unanimous ratification of shareholders cannot validate an ultra vires expenditure, let alone a majority vote. On the other hand, recent decisions have held that a director's act not made for a corporate purpose, yet motivated by policy considerations, can be ratified. Arguably, the principle applies mutatis mutandis to the proxy expenses of insurgents. It can be maintained, however, that the analogy is not warranted because the principle applies to only well-motivated defective decisions of the board.

In the United States, the government to a certain extent underwrites the proxy campaign, whereas in England the question has not been litigated. It seems, however, that the incumbents' expenses in England

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207 In the Rosenfeld case, it was decided that the burden of proof is shifted by such an analogy. Rosenfeld v. Fairchild Engine & Airplane Corp., 309 N.Y. 168, 128 N.E.2d 291, 296 (1955). See Insider Trading, supra note 62, at 289.


300 The board's decision to reimburse the insurgents cannot be said to be motivated by a desire to promote the interests of the corporation. These interests have already been served by the insurgents. To say that the board's resolution serves a corporate purpose because it will encourage other shareholders to air their views seems farfetched. The shareholders' decision is designed to make the insurgents' campaign an act for a corporate purpose, not to make the board's decision such an act.
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could be deducted from the corporate income while an individual insurgent's expenses would not be deductible from his income.\textsuperscript{301}

CONCLUSION

The preceding analysis has noted those deficiencies in the corporate systems of England and the United States that frustrate corporate democracy and the functioning of the market for corporate control. It is submitted that legislators in these jurisdictions should devise rules that will make meaningful the power to hire and fire. In the United States, directors should be made removable by a simple majority without cause. In the United States and in England, the statutes should invalidate circumventing devices, such as the weighting of voting power solely for the purpose of blocking a removal resolution. In the United States, minority shareholders should have the right to call a general meeting, and the shareholders' register should be made open for inspection. The shareholders' proposal provisions in the United States and England should be revised to enable insurgents to make an adequate presentation at corporate expense. Further, rules should be devised for a fair allocation of corporate funds for incumbents' and insurgents' proxy campaigns. Finally, the regulation of proxy contests should be revised in order to achieve a better balance between providing shareholders with adequate information and not assisting managements to entrench themselves.

\textsuperscript{301} The rules for deduction of business expenses are similar in the two countries. \textit{Compare} WTS: United Kingdom, 7/2.1, and WTS: United States, 7/2.1. Since England, however, does not have a section comparable to § 212 of the Internal Revenue Code, the insurgent's expenses will be personal and not business.