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RIGHT OF A SUBSEQUENT STOCKHOLDER TO REDRESS CORPORATE WRONGS CONSUMMATED PRIOR TO HIS ACQUISITION OF THE STOCK

This question of rights presents a matter of very great interest and growing importance in the Federal and State courts of the United States. With the vast and increasing proportion of the active business of modern life which is done
by corporations, it is neither to be wondered at or to be re-gretted, that the courts of equity should be sought to settle controversies growing out of the relations between stockhold-ers and the corporation of which they are members. That the policy of the law is not set, but is being formulated gradu-ally by adjudications based on experience, necessity and rea-
on will be realized from an exhaustive search among the autho-
rities.

There is a direct split of authorities on this question. One line of decisions follows the lead of Pollitz v. Gould, 202 N. Y. 11, 94 N. E. 1088, holding that "a stockholder may, in the absence of special circumstances, maintain an action on behalf of the corporation for the benefit of himself and all other stockholders, to set aside an improper transaction consum-
mated at the expense of the corporation, although it was com-
plicated before he acquired his stock." In support are Raf-
ferty v. Donnelly, 197 Pa. 423, 47 Atl. 202; Appleton v. Amer-
ican Malting Co., 65 N. J. Eq. 375, 54 Atl. 454; Ramsey v. Gould, 57 Barb, 398. The special circumstances which these courts admit will defeat the subsequent stockholder's right to recover are:

1. When the suitor is not a bona fide stockholder. For-

2. When the suitor is guilty of acquiescence in the wrong. Past v. Beacon Co., 84 Fed. 371.

3. When the suitor is guilty of laches. Peabody v. Flint, 6 Allen (Mass.) 52.

4. In cases where the transferee derives his stocks from one who would have been barred from bringing suit because of laches or acquiescence. Venner v. A. T. & S. F. R. Co., 28 Fed. 581; Frooks v. Southwestern Ry. Co., 1 Smale & G. 142.

The other line of decisions, though in the minority, are to be found in the Federal courts and a number of the state courts. The Federal equity rule promulgated by the U. S. Supreme Court in 1882 and numbered 94 (now 27) is in sub-

stance, "that to entitle one to attack a fraudulent trans-
action or wrong on the part of the corporation, it must appear
that one was a stockholder at the time of the commission of
the act complained of, or that his shares have devolved on
him by operation of law." The court in deciding Hawes v.
Oakland, 104 U. S. 450, one year before the Federal rule was
promulgated, assumed this position, and never, in a single
instance has the decision of Hawes v. Oakland been deviated
from in the Federal court. There are numerous cases where
it has been sustained. United Electric Sec. Co. v. La. Elec.
L. Co., 68 Fed. 673; Church v. Citizen's Street R. Co., 78 Fed.
526; Dimpfell v. Ohio M. R. Co., 110 U. S. 209; Taylor v.
Holmes, 127 U. S. 489. It is argued by the proponents of
Pollitz v. Gould supra, that the Federal rule is a matter of
procedure and not of substantive law, and in Just v. Idaho
Canal Co., 16 Ida. 639, 102 Pac. 381, it was said: "It is a
rule that has been adopted for the purpose of preventing a
transfer of stock to a non-resident, in order to enable him
to bring the case in the Federal court. It is a rule of practice
instead of a principle of law, and is not applicable in state
courts." But the Federal courts and some state courts have
denied that this is a rule of procedure and have accepted the
L. Co., supra, that "as a general proposition, the purchaser
of stocks in a corporation is not allowed to attack the acts
and management of the corporation prior to the acquisition
of his stocks; otherwise we might have a case where the stock
duly represented in a corporation consented to and partici-
pated in bad management and waste, and after reaping the
benefits from such a transaction could easily be passed into
the hands of a subsequent purchaser, who could make his
harvest by appearing and contesting the very acts and con-
duct which his vendor had consented to." The rule must be
accepted as something more than a rule of practice to prevent
fraud and collusion to invoke the jurisdiction of the Federal
court.

Passing from the Federal authorities sustaining this
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proposition we come to the state courts which are in accord. Perhaps the leading case on this question is Home Fire Ins. Co. v. Barber, 67 Neb., 644, 93 N. W. 1024, which was decided in 1903 by Commissioner Pound, who is at the present time Dean of the Harvard Law School. The case is one in which the present stockholders who are maintaining an action in the name of the corporation are all subsequent purchasers, having obtained their stocks through the defendant, whom they are now suing for fraud on the corporation prior to their acquisition of the stocks. Pound, C., in holding that a present stockholder should not be allowed to sue for mismanagement prior to his purchase unless its effects are of a continuing nature and injurious to the purchaser, says of the particular case, "the present stockholders are contesting acts through which they got title to a large portion of their stocks, and acts which those through whom they derived the greater part of the remainder could not have challenged because they participated therein, and by contesting these acts which did not injure any of the present stockholders in the least, are seeking to recover back a large portion of the purchase price of the stock which was admittedly worth all they paid for it." It would appear from this case and others in accord, that the transferee of stocks acquires no greater rights by his purchase than his vendor had; Babcock v. Farwell, 245 Ill. 14, holding that the assignee of shares of stock in a corporation acquires no greater rights than his assignor's, as he holds by the same title and is subject to the same liabilities." Accord McCampbell v. Railroad, 111 Tenn. 55; Matter of Appl'n of Syn. C & N. Y. R. R. Co., 91 N. Y. 1; Graham v. Railroad Co., 102 U. S. 148; Prosser v. Edmonds, 1 Y. & C. 481; Upton v. Basset, Eliz., 445; and Schilling & Schneider Brewing Co. v. Schneider, 110 Mo. 83, where the stocks devolved upon the complainant by operation of law.

As to the subsequent stockholder's right to sue when the wrong is of a continuing nature, see Hymans v. Old Dominion Co. 1 Me. 294, L. R. A. 1915 D 1128.

But there are a number of cases in different jurisdictions
that follow the Federal rule and are of the opinion that the transforee's inability to sue for mismanagement is not dependent entirely upon the fact that his vendor could not have sued for mismanagement because of participation in such acts, but that the transferee has received all he bargained and paid for and that it would be inequitable to allow him to set aside former transaction and thereby increase the value of his stocks. Clark v. American Coal Co., 86 Iowa 436: "What he paid for and what he received was based on a portion not affected by the fraud consummated prior to his acquisition of the stock." Alexander Trus. v. Searcy, 81 Ga., 536-550: "The weight of authority seems to be that a person who did not own stock at the time of transaction complained of cannot complain or bring suit to have them declared illegal." Cited and approved in Hawes v. Oakland, supra, and Dimpfell v. Ohio & Miss. R. Co., supra. To the same effect Boldenweek v. Bullis, 40 Colo, 253-259.

That the law on this subject is unsettled appears from the conflict of opinions and authorities and it is difficult to predict which line of cases will ultimately be accepted as authority.

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