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REMOVAL OF THE CORPORATE DIRECTOR DURING HIS TERM OF OFFICE

Arthur H. Travers, Jr.*

The traditional rules governing the removal of corporate directors have evolved so as to insulate the board of directors from the shareholders who elect them. Professor Travers in his article examines initially the interests being advanced by protecting the board members from removal by their electorates. He then critically analyzes the law as it relates to these interests in order to suggest a more rational approach.

I. INTRODUCTION

Until recently the typical pattern of corporation statutes was to prescribe that shareholders should elect the corporation’s directors for a term of office set forth either in the statute itself or in the corporation’s bylaws. Between elections the business and affairs of the corporation were to be managed by that board. The courts deduced from this pattern that the shareholders were not to interfere with the board’s management or attempt to make policy themselves; their job was to review the performance of each director when he stood for re-election.

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1 See, e.g., ABA-ALI MODEL BUS. CORP. ACT § 34 (rev. ed. 1959); CAL. CORP. CODE ANN. § 805 (West 1955); N.Y. BUS. CORP. LAW § 703 (McKinney 1963); TEX. BUS. CORP. ACT art. 2.22 (Vernon 1956). All states which fix the term by statute prescribe one year, although many, like New York, permit classification of the board. See ABA-ALI MODEL BUS. CORP. ACT ANN. § 34, ¶ 2.02(5).

2 E.g., Pa. STAT. ANN. tit. 15, § 1402 (Purdon 1967). Some states have no explicit term of office set forth in the statute, and it is inferable that a bylaw on the matter would be appropriate. See, e.g., DEL. CODE ANN. tit. 8, § 141(b) (Supp. 1966); ILL. ANN. STAT. ch. 32, § 157.34 (Smith-Hurd Supp. 1966).

3 All statutes prescribe this as a basic norm of corporate government although the provisions vary in elaborateness. See ABA-ALI MODEL BUS. CORP. ACT ANN. § 33, ¶ 2.02(2).

4 See, e.g., Continental Sec. Co. v. Belmont, 206 N.Y. 7, 99 N.E. 138 (1912); Charlestown Boot & Shoe Co. v. Dunsmore, 60 N.H. 85 (1880). It is interesting to note that the English courts reached the same result without benefit of statute. See Automatic Self-Cleansing Filter Syndicate Co. v. Cuningham, [1906] 2 Ch. 34 (C.A.). However, some commentators believe that the rationale for the rule in England has been removed by the provision in the Companies Act of 1948, 11 & 12 Geo. 6, c. 33, § 184, which allows a majority of the shareholders to remove a director with or without cause. See Gower, Corporate Control: The Battle for the Berkeley, 68 HARV. L. REV. 1176, 1186–87 n.35 (1955).
and to refuse to re-elect those who had performed unsatisfactorily. It was uncommon for statutes to contain provisions setting forth what power the shareholders might have to remove one or more directors before their terms expired.  

In the absence of such provisions the courts were called upon to determine the exact extent of the shareholders' power of removal, or "amotion" as it was sometimes called, and the manner in which it might be exercised. The rules which the courts formulated, taken as a whole, seem to make it a difficult task to oust a director before his term expires; shareholders may not remove directors at will, but only for legally sufficient cause. An intra-corporate hearing must be held and the director afforded certain procedural safeguards, such as notice of the charges against him, an opportunity to prepare a defense, and an opportunity to present that defense before the shareholders vote on his removal. The director may seek judicial review of the removal proceedings to guarantee that there were no irregularities. Should the court for any reason decide that the attempted removal is invalid, it is empowered to restore the director to office by an appropriate remedy.

By contrast, corporate officers and agents, even high-level executives, are removable by the board of directors at pleasure, subject to any

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5 Of late there has been a trend toward a statutory provision permitting a majority of the shareholders to remove a director or directors with or without cause. See, e.g., Miss. Code Ann. § 5309-75 (Supp. 1964); Neb. Rev. Stat. § 21-2039 (Supp. 1965); Ore. Rev. Stat. § 57.193 (Supp. 1965); S.C. Code Ann. § 12-18.7 (Supp. 1966); Utah Code Ann. § 16-10-37 (Supp. 1985). In part this may be due to the fact that the ABA-ALI Model Business Corporation Act was amended in 1955 to include an optional section, §36A, which authorized removal with or without cause. Although this section represents a much more "shareholder-oriented" philosophy than that evidenced by the original act, see What's New in Corporation Laws, 8 Bus. Law., Jan. 1953, at 1, 27-32, at least one knowledgeable commentator believes the provision so important that making it optional is a mistake. See Jennings, The Role of the States in Corporate Regulation and Investor Protection, 23 Law & Contemp. Prob. 193, 203 (1958).


contractual rights which the executive may have against the corporation. As a practical matter, however, the phrase “at pleasure” may overstate the ease with which a corporation may amputate an unwanted executive. As the dependent clause concerning contractual rights suggests, the statement that a corporate officer holds office at the pleasure of the board refers only to the agency relationship between company and executive. Like all agencies, it may be terminated at will by either party. Many—perhaps most—executives have no employment contracts with their companies and, hence, may be cashiered without penalty. But a substantial number of executives do have such contracts; they hold office at the pleasure of the board, but the board may find it expensive to indulge the pleasure of discharging them.

Because the prospect of a large damage judgment against the corporation can deter a board from discharging an unsatisfactory executive, the courts have been moved to impose certain limits on the amount of liability to which a board may expose its corporation by invalidating contracts that seem of inordinate length. But it is not every contract which extends beyond the term of the board which will be held invalid. There is a legitimate corporate interest in giving executives some guarantee of tenure, and contracts for terms of five years have been upheld by the courts. In such instances discharging an executive can still prove a costly business unless the corporation can prove, if later challenged in an action for breach of contract, that it was justified in dismissing the executive. That is, that it had “cause.”

Most often justification is established by showing that the executive was himself in breach of an express or implied condition of the employment contract. The most common express condition seems to be one which the courts would imply in any event: an executive shall discharge his obligations of due care and loyalty to the corporation.

\[\text{References}\]

14 1 G. Hornstein, Corporation Law and Practice 220-21 (1959); cf. In re Paramount Publix Corp., 90 F.2d 441 (2d Cir. 1937).
15 See W. Seavey, Agency 87 (1964); Restatement (Second) of Agency § 118 (1959).
17 Id. at 36-37.
18 See General Paint Corp. v. Kramer, 57 F.2d 698 (10th Cir. 1932). See also cases cited in 1 G. Hornstein, supra note 14, at 221 n.16.
19 Realty Acceptance Corp. v. Montgomery, 51 F.2d 636 (3d Cir. 1930).
In addition to performing these fundamental duties, the employee must also observe his proper place in the corporate hierarchy, obey his superiors, and not struggle for power in a boorish or unseemly manner. As will be seen, the "cause" which affords the corporation a defense to an executive's contract action seems to be essentially the same as the "cause" which warrants removal of a director. It may be asked then in what sense the director's position differs from the executive's.

First, it appears that the director's right to be discharged only for cause results from his status, not from any contract. In the executive's case it is up to him in the first instance to bargain for his own protection; otherwise, the courts will not protect him. But the director's protection does not depend on this. The inference is that there is some policy of corporation law which is being thus furthered. Second, the executive is not entitled to hold his position. His remedy is money damages; only in the most extraordinary case will a court in effect restore an executive to his position by specifically enforcing his contract. By contrast the ousted director has an array of remedies which will reinstate him. He may seek mandamus, quo warranto, or an injunction against his replacement. Some states offer a statutory action to try title, and in rare instances a court may step in before the attempted removal and enjoin it, if the attempt is invalid on its face. Whatever the form or the label, the effect is the same. The director retains his office.

Finally, the law insists upon an intra-corporate hearing. Several


24 Id. at 240-42.

25 Fuller v. Plainfield Academy School, 6 Conn. 532 (1837); Detwiler v. Commonwealth ex rel. Dickinson, 131 Pa. 614, 18 A. 980 (1890).


29 E.g., Campbell v. Loew's, Inc., 36 Del. Ch. 553, 134 A.2d 852 (Ch. 1957); Laughlin v. Geer, 121 Ill. App. 534 (1905).
decisions have invalidated attempted removals solely because of the failure to afford the director the procedural safeguards which are his due. There is no similar requirement in the case of the executive. Naturally, if the potential judgment against the corporation is substantial, a circumspect board will wish to make sure of its facts and of the legal consequences of those facts before acting, but there is no requirement that this be done. The board may act as arbitrarily as it wishes. Later a court will conduct a trial de novo, make its own findings of fact, and apply the legal principles it deems appropriate.\textsuperscript{30} If the facts establish that cause actually existed, no damages will be awarded.\textsuperscript{31}

Judging from the rules themselves, if taken at face value, and these distinctions between the director's position and the executive's position, the legal rules regarding the removal of corporate directors are intended to loosen the shareholders' control over the board which they elect. This article will first attempt to discover what interest or interests are being furthered by insulating the board from the shareholders. It will then look more closely at some of the more salient features of the law of removal in an effort to see how these features are related to the apparent interests being furthered.

II. THEORETICAL JUSTIFICATIONS

A. The Evolution of the Present Rules

The present law governing the removal of corporate directors seems to have had its genesis in cases involving municipal corporations.\textsuperscript{32} Early writers on corporations did not distinguish between corporations serving very different functions.\textsuperscript{33} After a rather perfunctory classifying of the various types of corporations in existence, their discussion of legal principles and rules would proceed as if it were irrelevant whether the corporation to which the law was to be applied were lay or ecclesiastical, private or municipal, business or eleemosynary.\textsuperscript{34} Precedents involving particular types of corporations were treated as

\textsuperscript{30} E.g., Templeman v. Grant, 75 Colo. 519, 227 P. 555 (1924); Koppitz-Melchers, Inc. v. Koppitz, 315 Mich. 582, 24 N.W.2d 220 (1946).
\textsuperscript{34} See J. Angell & S. Ames, supra note 6, at 411–29.
interchangeable with precedents concerning distinctly different types.\textsuperscript{35} As a result, doctrines appropriate to a corporation performing one function were transferred without analysis to other corporations with wholly dissimilar functions.

More specifically, it could readily be concluded that the aldermen of a municipality should be insulated from the electorate between elections. Since it was their job to regulate the behavior of that very electorate, fulfilling that function would inevitably cause irritation among the citizenry. Some degree of independence had to be afforded them if their regulatory tasks were to be performed. It might be expected that the Crown would certainly take this view since it looked upon municipal corporations, for all their "ancient liberties," as instruments of royal policy.\textsuperscript{36} If other forces operating on the aldermen could be reduced or neutralized, the objectives of the Crown might well play a larger role in shaping their decisions. Initially, the great trading companies chartered by the Crown had a similar regulatory function, as did the guilds. Whereas the municipalities regulated all those within a given geographical area, the chartered corporations controlled all those persons who plied a particular trade.\textsuperscript{37} Here too there was reason to shield directors from the ire of those they regulated, and here too such shielding might well operate to make the directors more responsive to Crown policy by diminishing a counter-pressure.\textsuperscript{38} To be sure, both municipal aldermen and company directors would have to stand for re-election, but the time lag would give the electorate a chance to cool down, a process often hastened when the imagined ill-effects of some regulation failed to materialize or when the board made another, more popular decision.

These functional similarities, however, do not explain why the rule that the shareholders of a business corporation may not remove directors at will became embedded in American law. It would seem that only the tendency of the writers to treat all corporations as essentially subject to the same rules accounts for this. While the modern business corporation resulted from a fusing of the chartered corporation with the contractual financing device known as the joint stock company,\textsuperscript{39}

\textsuperscript{35}This tendency has shown up in relatively recent decisions by sophisticated courts. See \textit{In re Koch}, 297 N.Y. 318, 178 N.E. 545 (1931).


\textsuperscript{37}Williston, \textit{supra} note 33, at 198, 201.

\textsuperscript{38}See \textit{generally} J. Clapham, \textit{A Concise Economic History of Britain From the Earliest Times to 1750}, at 253-72 (1963).

\textsuperscript{39}Chayes, \textit{supra} note 36, at 33. See \textit{generally} A. DuBois, \textit{The English Business Company After the Bubble Act, 1720-1800} (1938), for an historical account of this development. An interesting student note has recently dusted off the joint stock device and suggested it as a possible tool for solving some of the current
American law has always tended to emphasize the entity, the corporation. During the early nineteenth century, when American law was being molded, the natural law approach of legal thinkers induced them to conceive of their task as elaborating the characteristics of a metaphysical entity. By contrast, England, which tended to focus on the contractual aspects of the corporation, has had a rather different development. The idea that shareholders may not remove directors at will seems strange to English observers.

Such considerations no longer justify making removal of corporate directors difficult and complicated if easy removal would better serve contemporary needs. If the director is to continue to occupy a unique and enviable status so far as tenure is concerned, it should be because modern conditions continue to warrant differing treatment for directors and executives.

B. The Conceptualistic Approach

The most common explanation of the difference between the rules governing removal of a director and those governing the ouster of an executive is that the latter is an agent, whereas the former is not. It may be freely conceded that directors of a corporation are not the agents of the shareholders since they are not subject to direct control by the shareholders while in office. Even if the directors were removable at will and, thus, subject to somewhat greater shareholder influence than exists under the present rules, the directors and not the shareholders would still be the group which in the first instance made problems of close corporations. See Note, The Joint Stock Company and the Problems of the Close Corporation, 50 Iowa L. Rev. 118 (1964).


In Inderwick v. Snell, 2 Mac. & G. 216, 42 Eng. Rep. 83 (Ch., 1850), the court apparently laid down a rule which would permit shareholders to remove directors at will. Later, in Imperial Hydropathic Hotel Co. v. Hampson, 23 Ch. D. 1 (1882), the court refused to sanction an attempt by the shareholders to remove an unwanted director. Although there were certain differences in the provisions of the articles of the two companies involved and both courts acted as if the issue were largely one of construction, these differences do not completely explain the results. The Hampson court did not refer to the Inderwick case. As noted in note 4 supra, removal with or without cause is now expressly permitted by statute in England.

the decisions regarding the corporate objectives and the means to be employed in attaining them. For this reason, it would seem that removal at will is not inconsistent with non-agent status since direct, ongoing control over the agent by the principal is the distinctive feature of the agency relationship. Thus, simply saying that directors are not agents does not advance the analysis very far. The director's status as a non-agent does not depend upon the removal rules, and more fundamentally, such a statement relates nothing positive about the true status of a director. It leaves open, therefore, the possibility that he could be placed in a different pigeonhole which also admitted of removal at will.

Recognition of this fact has often induced courts or commentators to go further and affix a label to the director: he is a "trustee" or a "political representative." While it is true that a trustee may be removed only for "cause," the removal is done by an equity court. On the other hand, a majority of the courts which have passed on the point have held that an equity court has no inherent power to remove a director, even for cause. The most distinctive aspect of the law regarding removal of the corporate director is the requirement of an intra-corporate hearing. Courts have not required beneficiaries to conduct similar hearings. Moreover, it is not the usual custom for trustees to run for re-election.

This last objection to the label "trustee" can be avoided by using the label "political representative." This also has the virtue of suggesting the apparent origin of the removal rules, but as noted above, the regulatory task of the political representative provides a reason for complicating the procedures for his removal which does not apply to the corporate director. Furthermore, several states and municipalities permit the recall of political representatives before their terms expire, so the label itself is not an infallible guide to the appropriate rule in governing removal. Regardless of which label is selected, the basic difficulty remains: functionally and conceptually the director is

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40 Restatement (Second) of Agency § 14C (1959); W. Seavey, Agency 18–19 (1954).
50 1 A. Scott, supra note 49, at § 107.3.
sui generis despite his sharing certain attributes with agents, trustees, and representatives. That being so, why choose one label over another? Inevitably, this approach leads back to the starting point; the question of justification remains unanswered.

C. An Interest Analysis

A more productive approach would seem to be to determine exactly what interests are in fact being furthered by making removal difficult. Any shift from the conceptual level to the factual level requires some attempt to put the matter in perspective. The most important single fact is that attempts to remove directors during their terms are rare occurrences which signal a deep factional cleavage within the corporation. While this lack of attempts may result in part from the difficulty of removal, it may be more significant that in the ordinary course the shareholders will have an opportunity to vote on the director's performance in less than a year. Only if the shareholders are highly incensed will they be moved to immediate action. For this to happen, the director's alleged blunder or dishonesty must be quite egregious, and the chance of a repetition extremely high. This conclusion seems borne out by the experience of those states and municipalities which instituted the recall; fears that the device would lead to political instability and government by demagogue as the passionate masses toppled governments proved completely unfounded. Shareholders seem to possess the same level of apathy.

Contrariwise, it would seem likely that if there is hostility between the shareholders and the directors, it will become manifest long before removal proceedings are commenced. Many, probably most, directors would prefer to resign their positions if it appeared that a majority of the shareholders wanted them out. Indeed, boards have been known to resign after an unsuccessful attempt to remove them when the vote in favor of removal was substantial.

54 C. Williams, Cumulative Voting for Directors 57 (1951). The tabulation of the frequency with which certain issues were proposed by non-management shareholders under the SEC's proxy rules contained in F. Emerson & F. Latcham, Shareholder Democracy 125-27 (1954), shows that removal proposals were quite uncommon.
55 E.g., E. Bacon & M. Wyman, Direct Elections and Lawmaking By Popular Vote 50-77 (1912).
58 See E. Aranow & H. Einhorn, Proxy Contests for Corporate Control 69-70 (1957).
Clearly, then, making removal at will possible is not enacting shareholder democracy. All it allows is the ouster of unwanted directors in those rare cases in which the shareholders can be moved to action. Any attempt to justify the present rules must take account of the relative infrequency of removal attempts and the high emotion which ordinarily accompanies them.

1. Protecting the Minority Shareholder

It may be argued that the board must be independent in order to protect minority shareholders. To say that the director has certain duties to the corporation is merely a shorthand way of saying that he has duties to all shareholders as a group and not merely the faction which put him in office. If removal at will were possible, the board would become unduly responsive to the desires of the majority. The first problem raised by such an argument is one of standing. If it is the interest of the minority shareholder which is being protected, why not require him to raise the point? In almost all instances, however, the party lodging an objection to an attempted removal is the director himself. The courts have ordinarily not objected to this. Indeed, in the leading case of Campbell v. Loew's, Inc., when a shareholder attempted to enjoin a proposed ouster, an issue was made of his standing. Objections of this kind are hardly conclusive, but they do suggest that there is some problem in explaining the cases in terms of the minority shareholder's interest, or any interest other than the director's.

More fundamentally, the argument speaks of "majority" and "minority" as if they were unchanging masses rather than shifting coalitions of individual shareholders. To the extent that each shareholder has roughly the same opportunity to be a member of the "majority," it cannot be said that permitting removal at will would lead to the

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69 This may be seen most clearly in the case of a corporation in which cumulative voting is permitted. See, e.g., In re Rogers Imports, Inc., 202 Misc. 761, 116 N.Y.S.2d 106 (Sup. Ct. 1952); 22 U. Chi. L. Rev. 751 (1955). But even if a given director cannot be identified as the representative of a minority, the threat of removal may induce directors to favor the majority view. Cf. F. O'Neal & J. Derwin, EXPULSION OR OPPRESSION OF BUSINESS ASSOCIATES § 3.05 (1961).

60 This was the theory of Automatic Self-Cleansing Filter Syndicate Co. v. Cuninghame, [1906] 2 Ch. 34 (C.A.). As noted in note 4 supra, Professor Gower believes that doubt has been cast upon the continued vitality of Cuninghame by the change in the English removal rules which now permit a majority of the shareholders to remove a director without cause. Professor Gower apparently sees the restrictions on removal as basically designed to protect the minority shareholders.


It is true, of course, that shareholdings vary greatly in size and that the larger blocs have a greater potentiality for influence as a result of voting by share instead of by head. In any case, unless the voting blocs are fixed, even the small shareholder may hold important votes.

If the blocs are rigidly formed into majority and minority, as where one shareholder holds sixty percent of the shares and the other, forty percent, the argument has somewhat more force, but is still not compelling. With the majority thus fixed, there is a great likelihood that its views will be known. Indeed, it is possible for the majority to convene a shareholders’ meeting simply to put its views on record. In the nature of things it is going to exert more influence over the board than the minority. The question is whether making removal more difficult has much value in keeping majority influence within proper bounds. Allowing removal without cause is a long way from permitting the majority to intervene directly to overrule a board decision. Apart from simple shareholder inertia, there are other reasons why a majority which would be willing to overrule a board would not wish to remove it. The majority might feel that the board was in general doing a satisfactory job, or it might not have any replacements who could do better. Given the infrequency with which removals are attempted, it is doubtful that facilitating removal by majority vote would add greatly to the majority’s power to oppress.

Any such increase in power must be balanced against any benefits which would accrue from making removal easier. The rationale of protecting minority rights does not discriminate between large and small minorities; apparently any shareholder vote short of unanimity would still leave a minority to be oppressed. Under such circumstances one recalcitrant shareholder could saddle an overwhelming majority with a totally unsatisfactory board. At this point one wonders just who is being oppressed.

Suppose, however, that the shareholders vote unanimously to oust a director. If the sole purpose of the rules is to protect the minority shareholders, it would seem that there would be no restrictions on

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63 Cf. Maddock v. Vorclone Corp., 17 Del. Ch. 39, 147 A. 255 (1929) (majority may amend charter to eliminate cumulative voting since this right inheres in each share and not in a minority).


65 66 HARV. L. REV. 531 (1953). Professor Lattin seems to take a contrary view, arguing that allowing removal at will would convert the directors into “mere puppets of the shareholders.” N. LATTIN, CORPORATIONS 213 (1959).

66 One leading commentator believes that the shareholders should be able to make corporate decisions directly if they are unanimous. 1 G. HORSTIN, CORPORATION LAW AND PRACTICE § 178 (1959). A fortiori, they should be able to cashier an unwanted director. But see LATTIN, supra note 65, at 213.
what the shareholders might do unanimously. Three cases have been found in which the directors were removed by unanimous vote, but they are complicated by other issues. In one case, what appears to have been the only two shareholders of a corporation met informally in a hospital waiting room and held a discussion. It was alleged that this was an official shareholders' meeting and that the directors were validly removed. The court apparently took the view that the meeting was not called for the purpose of removal, that it just happened, and that it could not be deemed a shareholders' meeting. Furthermore, the subsequent conduct of the shareholders was inconsistent with their contention that this was a valid shareholders' meeting. All in all, the case is hardly strong support for the idea that directors may not be removed at will if all of the shareholders concur.

In Frank v. Anthony, the plaintiff was the sole shareholder of the corporation as well as a director and the president. Shortly after the formation of the corporation, which had occurred recently, two of the original directors resigned and plaintiff filled the vacancies. Thereafter, his appointees asked him to resign as president and, upon his refusal, they discharged him. The plaintiff immediately convened himself as a shareholders' meeting and voted to remove his two appointees. In an action for declaratory judgment, the court held the plaintiff's ouster as president valid and the removal of the directors invalid.

Taking the case at face value, it would seem to indicate that other interests are being protected by the law governing removal besides that of the minority, for here there was no minority to protect. It is true that the opinion recites additional facts which suggest that the court may not have treated the case as one involving unanimous shareholder action. Plaintiff and defendants had been interested in an existing partnership, and the corporation had been formed to acquire valuable real estate from the partnership. Their arrangement anticipated that the defendants would soon become substantial shareholders in the corporation; plaintiff's position as sole shareholder was a temporary expedient. In a sense the plaintiff attempted to squeeze the defendants out, and they retaliated by squeezing him out. This analysis certainly explains a result which would otherwise seem inexplicable if only the interest of the minority were involved. However, it raises the question why the court remarked:

As to whether or not appellant was the sole stockholder of the corporation, the trial court made no finding and such was not necessary to the determination of the issues decided by the court.

67 In re Louisiana Inv. & Loan Corp., 224 F. Supp. 274 (E.D. La. 1963), aff'd, 342 F.2d 999 (5th Cir. 1965).
70 107 So. 2d at 138.
This seems to suggest that the absence of a minority was irrelevant.

In the case of *Textite, Inc. v. Wineburgh*,71 a Texas court took a different tack. Plaintiff and his family sold their holdings, amounting to practically all the stock in Textite, but plaintiff remained as a director and was appointed executive vice-president. Two months later, at a special shareholders' meeting, the buyers unanimously voted to remove the plaintiff as director and to direct the board to abolish the office of executive vice-president, which the board promptly did. Plaintiff who had no notice of either the shareholders' or the directors' meeting, contested the validity of the shareholders' acts.

The court first dismissed the procedural objections to the shareholders' meeting, holding these to be for the benefit of the shareholders; the plaintiff, a non-shareholder, had no standing to raise them. Moving to the issue of the shareholders' power to remove a director, the court first agreed that at common law a majority of the shareholders could not oust a director without cause. Then it said:

> But this is not to say that all of the stockholders, acting in unison, cannot lawfully remove a director, *who is not a shareholder*, at any time with or without cause. We do not mean to announce one rule applicable to a majority of shareholders and another rule applicable where the decision is unanimous; it is simply a matter of determining who has the right to complain of such action. If a director be removed by a majority of the shareholders without cause, those of the minority have to object on the ground that the action breaches the understanding among shareholders implicit in the organization of the corporation under the statute, that the directors elected shall remain in office for the term . . . [for which elected unless removed in accordance with the bylaws],72 to represent all the shareholders in managing the affairs of the company. But can the removed director be heard to complain, when it appears he is neither shareholder in nor creditor of the corporation? We think not, and hold that under the facts of this case appellee had no right to complain of his removal as a director and that such removal was therefore effective.73

Regardless of how the *Texlite* opinion is interpreted, it seems to be denying any personal right of the director to his position. As previously noted, this seems contrary to the bulk of the decisions, which simply assume that the director has standing to complain.74 It runs counter also to language appearing in some opinions that the director has a vested right to his position.75 Yet, the court in *Texlite* seemed

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72 This insert is from *Tex. Bus. Corp. Act* art. 2.32 (Vernon 1956). The court used the word "etc.," but it appears from the context that this is the language to which "etc." referred.
73 373 S.W.2d at 328–29.
75 *In re Automotive Mfrs. Ass'n*, 120 Misc. 405, 199 N.Y.S. 313 (Sup. Ct. 1923).
unwilling to actually tie the law of removal entirely to the interest of the minority shareholders. The court's insistence that it was not laying down a separate rule for unanimous action, that it was treating the issue solely as one of standing, and its suggestion that a creditor might be able to object, raise the possibility that the removal rules may be designed, at least in part, to protect the interests of non-shareholder constituencies of the directors, such as creditors, employees, customers, and suppliers.

It goes without saying that the result in Frank is also consistent with the hypothesis that the interests of such constituencies are being furthered by the rules making removal difficult. Frank, however, may also be explained on the ground that the court was protecting the interest of the director in holding his office.

2. Balancing the Interests of Corporate Constituencies

The idea that the directors and executives of a corporation should manage the enterprise solely in the interests of the shareholders is now widely considered an antiquarian notion by both managers and scholars. According to spokesmen for this view, managers have responsibilities toward all groups having a significant interest in the earnings of the enterprise and in an equitable distribution thereof. The essence of managerial statesmanship is seen as the striking of an appropriate balance among the interests asserted by these groups. Of the interests involved only that of the shareholders may be asserted through the franchise, with the other groups being left to press their cases through other means. Fortunately, the oft-noticed "separation of ownership and control" and the attendant apathy among shareholders in corporate giants largely neutralizes the advantage afforded by the franchise. It may be argued that making it easier for shareholders to remove directors would disturb the balance of forces operating upon the directors and make them unduly responsive to the shareholders, thus diminishing the influence of the other interest groups. In a sense this modern reason for insulating the board from the shareholders parallels the original reason. It allows for the operation of desirable counter-pressures.


77 The classic statement on this is Dodd, For Whom Are Corporate Managers Trustees?, 45 Harv. L. Rev. 1145, 1156-61 (1932). This led to the famous Berle-Dodd debate. Berle, For Whom Corporate Managers Are Trustees: A Note, 45 Harv. L. Rev. 1365 (1932); Dodd, Is Effective Enforcement of the Fiduciary Duties of Corporate Managers Practicable?, 2 U. Chi. L. Rev. 194 (1934).

78 The classic exposition on this point, which remains the best today, is A. BERLE & G. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932).
This theory would account for the result in *Frank* as well as the suggestion in *Texlite* that a creditor would have standing to complain about the removal of a director without cause by a unanimous shareholder vote. But this theory raises problems too. In the first place it is only theory. Apart from the *Frank* and *Texlite* cases—and both may be explained on other bases—there is little in the removal cases to suggest that this is what the courts are doing. To the contrary, the fact that the directors are usually the complaining parties raises the same questions of standing which were noted above in connection with the discussion of the minority shareholder. As a general matter there is little support in corporation precedents of any type for the suggestion that the courts have discarded the traditional idea that the job of the corporation's managers is to maximize profits for the shareholders.

Moreover, the theoretical case for broadening the concept of the corporate constituency remains unproven. Experiments in other countries with representatives of labor, or the public, have not produced the salutary results anticipated. Furthermore, it may be doubted whether this theory provides any guidelines for the director. Whatever the defects of the profit-maximization standard, it at least indicated in a general way what policies the board should adopt. But a standard which tells the director to work out an equitable adjustment of various interests, some of which are in direct conflict, essentially leaves him on his own. It is far too vague to be a judicially enforceable standard of conduct. This may explain why the courts have given no indication that the law governing removal is even remotely tied to a policy of implementing this theory.

Even if the courts were to adopt this broader conception of the director's responsibilities, it is by no means clear that facilitating re-

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79 *Frank* may be viewed as not involving unanimous shareholder action; the remark in *Texlite* may be dismissed as ill-considered dictum.

80 See text accompanying note 61, supra.

81 An exception might be the more liberal attitude toward charitable contributions by corporations although these are sometimes explained as good public relations and hence profitable in the long run. See R. Baker & W. Cary, *supra* note 76, at 366-67.


83 See E. Nolte, *Three Faces of Fascism* 261 (1966) (discussion of the "syndicalism" of the Italian fascists). It is revealing that Nazi Germany rejected the Italian solution in favor of more indirect state controls. See Vagts, *supra* note 82, at 84.

84 Id. at 76-78, 85-87.


moval would be inconsistent with it. Again, it is important not to magnify the likelihood that the removal device would be used. As a practical matter, it is unlikely to increase significantly the number of removal attempts. It is true that the additional control given the shareholders may well influence the board in the case of a conflict among interest groups, but the strength of this influence in any given case is almost entirely a matter of speculation. So much turns on the psychological makeup of individual directors and the power position of the group opposed to the shareholders\textsuperscript{87} that generalization seems futile. There seems to be no single delicate equilibrium which would be inevitably destroyed.

In sum, it is doubtful if the courts have been protecting such a balance; it is questionable whether they can or should protect it, if it exists; and it is problematical whether it does exist. The interest protected by complicating removal, however, is something else.

3. The Corporate Interest

In a sense, the corporate interest is a variant of the preceding theory, but it breaks away from the interest or interests of any distinct group. It asserts that there is a separate corporate interest to be furthered by preventing the shareholders from removing directors at will. This theory eliminates any standing problem because there is no other group to whom the job of asserting the corporate interest can be assigned. In reality this argument is a form of elitist theory.\textsuperscript{88} Conceiving of the business enterprise as an organic whole, it states that the managers know best how to keep the organism healthy and growing. Allowing for even a bit more shareholder intervention will result in a lowering of the quality of the corporate decisions because it tampers with the elite's autonomy. Only if the elite is left free in its discretion can it function with maximum effectiveness.\textsuperscript{89} Poorer decisions leave all groups interested in the enterprise, including the shareholders, worse off. As members of this elite the directors have an unusually keen appreciation of exactly what the corporate interest is.

To the extent that this argument reflects nothing more than a fear of sharp reversals in corporate policy as the shareholders unseat boards with the same gleeful abandon with which the parliament of the Fourth Republic unseated governments, one may once again summon the answer that experience shows it does not happen. However, the theory stands for something more. Even if the removal power


\textsuperscript{88} See generally P. Bachrach, The Theory of Democratic Elitism (1967).

\textsuperscript{89} Cf. J. Schumpeter, Capitalism, Socialism and Democracy 285 (3d ed. 1950).
is rarely used, the board may be cowed by the threat of it and refrain from taking some vital but unpopular step. The fear of this sort of subtle psychological pressure is largely speculation and, it would seem, poor speculation. It assumes that, owing to the maladroitness of the board or the impenetrable stupidity of the shareholders, the board simply will not be able to explain why it took the steps it did and why those steps are best for the corporation. Further, it assumes that directors are so pusillanimous as to be constantly haunted by the possibility of being removed. There is no evidence that either assumption is correct, and in the absence of such evidence it might better be assumed that the directors have enough courage to do what they think best and enough talent to explain themselves, and that the shareholders have enough good sense to understand the explanation.

Moreover, if the elitist hypothesis were really behind the rules regarding removal, it would apply only to removal by the shareholders. On the other hand, if the removal were by the board itself, the logical thing for a court to do would be withdraw, leaving the majority of the elite to discern the elusive corporate interest. In fact, the courts have even been tougher on attempts by boards to remove one of their members.\(^9\) Not only do the courts deny any inherent power in the board to remove its own members, even for cause,\(^9\) but the delegation of power from the shareholders must be explicit.\(^9\) A general delegation of the power to make bylaws will not authorize the board to pass a bylaw giving itself the power to remove its own members.\(^9\) Even an explicit bylaw will not transfer the whole of the removal power; the shareholders still retain their “inherent” power to remove directors.\(^9\) These restrictions suggest that the courts are not really protecting some form of elitist structure.

4. The Director's Personal Interest

All that remains, then, is the director's personal interest in remaining in office. This theory accounts for the language in the cases about vested rights, for the almost complete failure to question the director's standing to object to his own removal, and for such rules as the pro-

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\(^9\) See Annot., 63 A.L.R. 776 (1929), and cases cited.


\(^9\) Explicit delegations have been upheld. See Petition of Singer, 189 Misc. 150, 70 N.Y.S.2d 550 (Sup. Ct.), aff'd, 75 N.Y.S.2d 514 (App. Div. 1947).


hibition against retroactive application of any charter or bylaw amend-
ment which broadens the removal power.95 It may be asked why it
took all this time to reach a conclusion which was pretty obvious from
the beginning. The answer, it seems, is that while it was obvious that
the courts were protecting the director, it was not clear whether they
were doing this as an end in itself or as a means of protecting some
other interest. The preceding analysis suggests that there is no other
interest; hence, the emphasis is on “personal.”

It was noted earlier that the executive’s remedy, presuming he had
a contract, was an action for damages for breach of contract;96 his
contract would not be specifically enforced. This refusal to award
specific relief to the executive persists despite the fact that the con-
ventional reasons for not enforcing personal service contracts are often
inapplicable to a corporate executive. There would be little difficulty
in ascertaining whether the corporation was fulfilling its promises;97
there is no “involuntary servitude” on the part of the corporation;98
and it may well misdescribe the circumstances to speak of an intimate
personal relationship which it would be onerous to enforce.99 In
essence, what the courts are doing is limiting judicial protection to
the pecuniary rewards of the position. Any other rewards which
might accrue to the executive go unprotected.

The remedies available to the director, however, put him back in
office, or keep him there if the removal has not yet been consummated.
In effect, the director’s interest in the psychological pleasure of his
title or the political pleasure of being a high-level decision-maker is
what is being protected by such remedies. This latter pleasure, how-
ever, can be given only limited protection. Although the courts can
protect his spot on the board, they cannot shield him from being system-
atically outvoted by the other board members or from being com-
pletely sterilized by the shareholders, who may “pack” the board of
directors at the annual meeting100 or a special meeting101 and convert

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95 E.g., H. Henn, Corporations 304 (1961); cases cited note 110 infra.
96 See text accompanying notes 13-24 supra.
97 See 5A A. Corbin, Contracts § 1204 (1964), for a list of the various rationales.
98 There would, of course, be such a problem if the defendant were the em-
ployee, and this may be thought to raise problems of “mutuality.”
99 In the case of the closely held corporation, however, specific enforcement
would compel such a personal relationship. See Chayes, Madame Wagner and
the Close Corporation, 73 Harv. L. Rev. 1532 (1960). The courts have not in-
dicated that they would relax the rules on specific enforcement for larger
companies.
100 Gow v. Consolidated Coppermines Corp., 19 Del. Ch. 172, 165 A. 136 (Ch.
1933).
101 Gold Bluff Mining & Lumber Corp. v. Whitlock, 75 Conn. 669, 55 A. 175
(1903); In re A.A. Griffing Iron Co., 63 N.J.L. 168, 41 A. 331 (1898); Republic
an erstwhile majority into a minority. What remains to the members of the old majority is the opportunity, however small, to persuade some of the new members to come over to its side.

By treating these interests as worthy of judicial protection, the courts are recognizing claims which seem to have been rejected in the case of executives and have been explicitly rejected in the case of labor union officials. It may be argued that the director should be given distinct treatment because the typical director has no contract with his company and, despite the urgings of some noted commentators, paid outside directors are not prevalent. Customarily the director qua director is a non-participant in the company's deferred compensation plans and entitled to no salary apart from a nominal fee for each meeting. Since the position carries no economic rewards, the psychological and political rewards are the director's only incentives. Granting that this argument has force, it would not seem a complete answer. It assumes that making removal at will possible would substantially dry up the supply of directors. This assumption appears doubtful since directors are probably little concerned with tenure as such when they come on a board. To the extent that the board is an inside board, the members will be receiving the tangible rewards accruing from their positions as executives. If some difficulty in recruiting outside directors should be experienced, it may easily be remedied by private adjustments, such as paying the director a salary. Solutions of this nature would seem more satisfactory than according the director a different legal status from that given executives.

5. Summary

The legal rules making removal of corporate directors difficult seem designed to further a somewhat limited interest of the director in the non-financial rewards of being a director. Others are entitled to protection of their financial rewards only. It does not appear that the director is accorded this treatment as a means to achieving some other end, such as preventing oppression of minority shareholders or preserving a balance of interests among various corporate constituencies. Furthermore, it does not appear necessary to do so in order to insure a supply of future directors, even outside directors.

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Talton v. Behncke, 199 F.2d 471 (7th Cir. 1952). "The only loss he [the president] has suffered is his pleasure and satisfaction in being president of the union,—a privilege not of legal character." Id. at 474.


105 Id. at 266-67.

106 See R. GORDON, supra note 87, at 305-12.
III. SOME ASPECTS OF THE LAW IN OPERATION

A. What Is Legally Sufficient Cause?

The requirement that there be sufficient cause for the removal of a director continues to be a significant factor. Despite the fact that a growing number of states have passed legislation permitting the shareholders to remove directors with or without cause, a majority of the corporation statutes remain silent, thus presumably giving the common-law rules full room to operate. A well-drafted provision in the articles or bylaws may authorize removal at will in these latter states, but such a provision may not be effective in all cases. If it first appears in an amendment, the provision ordinarily may not be used against incumbent directors. Also it may be deemed to conflict with some other norm embodied in the statute, articles, or bylaws. In such cases, the courts quite often resolve the conflict by invalidating that portion of the article or bylaw which purports to dispense with the requirement of cause. Finally, notwithstanding the article or bylaw, shareholders in a closely held corporation may agree to retain themselves as directors. Where such agreements exist, the courts will likewise be called upon to strike a balance between the bylaw authorizing removal without cause and the evident intention of the parties to the agreement. Again, permitting removal only for cause is the usual solution.

Despite the importance of the issue, sophisticated practitioners and legal scholars alike have suggested that it is not possible to give

110 Abberger v. Kulp, 158 Misc. 210, 281 N.Y.S. 373 (Sup. Ct. 1935); In re Automotive Mfrs. Ass'n, 120 Misc. 405, 199 N.Y.S. 313 (Sup. Ct. 1923); In re Schwartz, 119 Misc. 387, 195 N.Y.S. 679 (Sup. Ct. 1922).
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a meaningful, comprehensive definition. Other writers seem to accept this view since they confine their remarks on “cause” to cataloging, with greater or less completeness, instances in which a court has passed on the sufficiency of a particular ground for dismissal. Such catalogs may readily be compiled. Cause for removal exists where the director is guilty of “misconduct,” or has misapplied corporate funds, or has attempted to divert corporate business to another enterprise in which he has an interest, or has acted beyond his authority as an officer, or has engaged in a planned scheme of harassment. Contrariwise, cause does not exist simply because the director has been indiscreet, or verbally abusive to other directors; or has failed to attend meetings; or to carry out an assignment given him by the board; or has been uncooperative; or has attempted to gain control of the corporation. The trouble with such catalogs is that they are at once too abstract and not abstract enough. They are too abstract in that they summarize in a word or phrase a total fact situation, and these summaries fail to indicate what turns abuse into harassment. They are not abstract enough in that they are unrelated to any principle which would enable a lawyer to predict the result of a case which does not fit any existing precedent.

Given the scarcity of precedents, this cataloging may be the wisest course. Nevertheless, there is possibly some value in suggesting a few tentative generalizations. A good starting point would seem to be the few generalizations essayed by the courts. These have differed somewhat in phraseology, but the fundamental ideas seem virtually

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119 Roberts v. J.A. Masquere Co., 158 La. 642, 104 So. 484 (1925); People v. Lyon, 119 App. Div. 361, 104 N.Y.S. 319, aff’d per curiam, 189 N.Y. 544, 82 N.E. 1130 (1907).
120 Campbell v. Loew’s, Inc., 36 Del. Ch. 563, 134 A.2d 852 (Ch. 1957); Markovitz v. Markovitz, 336 Pa. 145, 8 A.2d 46 (1939).
122 Fuller v. Plainfield Academic School, 6 Conn. 532 (1827).
124 Fuller v. Plainfield Academic School, 6 Conn. 532 (1827).
125 Campbell v. Loew’s, Inc., 36 Del. Ch. 563, 134 A.2d 852 (Ch. 1957).
the same as those set forth by Lord Mansfield in *Rex v. Richardson*,\(^{127}\) one of the fountainhead municipal corporation cases:

There are three sorts of offences for which an officer or corporator may be discharged.

1st. Such as have no immediate relation to his office; but are in themselves of so infamous a nature, as to render the offender unfit to execute any public franchise.

2d. Such as are only against his oath, and the duty of his office as a corporator; and amount to breaches of the tacit condition annexed to his franchise or office.

3d. The third sort of offence for which an officer or corporator may be displaced, is of a mixed nature; as being an offence not only against the duty of his office, but also a matter indictable at common law.\(^{128}\)

Offenses of the first sort should be established by a jury verdict in a formal legal proceeding,\(^{129}\) but offenses of the other types might be tried by the corporation itself.\(^{130}\) After any of these offenses had been established by the appropriate tribunal, removal would be proper.

There is no dearth of cases deciding what duties a director owes his corporation, but these almost always involve a lawsuit by the corporation, or a shareholder suing in its behalf, against the director for damages for injuries sustained by the corporation as a result of the director’s violation of his duty. Lord Mansfield’s formulation suggests that those cases, and the standards evolved in them, might be used to determine when cause for removal exists. Thus, the first hypothesis is that cause for removal exists whenever the director’s actions would subject him to liability for damages in a suit brought by the corporation.\(^{131}\) Not only would this make available a large number of precedents elaborating the duty of care or the duty of loyalty as guides to determining if cause exists, but this hypothesis is also doctrinally appealing. It seems anomalous that a director’s conduct would justify a damage judgment against him but not warrant his being removed from office. Moreover, if the cause requirement is designed to protect the director’s interests by limiting removal to flagrant cases, such a definition would be roughly tailored to that objective.

But transferring the doctrine from one context to another is tricky business and should be done with an awareness of the limitations of the method. In this particular instance, there are several pitfalls to be avoided. In the first place, suits to surcharge the directors do not occur until after there has been an actual injury to the corporation.

\(^{127}\) *1 Burr. 517, 97 Eng. Rep. 426 (1758).*

\(^{128}\) *Id.* at 538, 97 Eng. Rep. at 438.

\(^{129}\) This seems akin to the modern power of a board to declare a director’s position vacant under certain circumstances, such as a conviction of a crime. *Henn, Corporations* 336 (1961).


Since it would be unreasonable to compel the shareholders to wait until a director's antics harmed the corporation, most removal cases will call upon the courts to judge the conduct of the director in the abstract, without benefit of actual harm. But certain acts, or more properly omissions, of the directors may not appear as violations of any duty if no harm has resulted. For example, several cases have held that the failure of a director to attend any board meetings at all is not sufficient cause to remove him. On the other hand, courts have surcharged directors when their failure to attend a reasonable number of board meetings has caused harm to the corporation. Similarly, in Fuller v. Plainfield Academic School the refusal of a director to attend meetings of the building committee, to which he had been appointed by the board, was held insufficient grounds for removal. Surely he would have been liable if harm had resulted from his petulant refusal. Although some tangible injury would be required if it is sought to surcharge the director, the absence of such an injury should not be an obstacle to removing a director for cause. Thus, in the absenteeism cases, the failure of the director's inattendance to cause injury to the corporation would be irrelevant in determining whether cause for removal existed. If the cases rested on the absence of harm, they would seem wrongly decided. To the extent that the courts have heretofore made the presence of harm a determinative factor in deciding whether the director has violated a duty to his corporation, the surcharge cases adhere to a more restrictive standard than would be appropriate in a removal case.

This means that the courts must push beyond the standards of the surcharge cases, and this, in turn, raises another problem. Courts may tend to rely too heavily on the concepts of duty of care and duty of loyalty and push a case into one of these molds when it really does not fit there. It would seem that there already exist a number of cases which arguably involve no breach of duty to the corporation. For example, in Campbell v. Loew's, Inc., the accused directors sought to enjoin forthcoming removal proceedings on the ground, among others, that the charges set out in the president's letter were inadequate as a matter of law. Summarizing the letter, the court said:

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133 See Dyson, supra note 131, at 363 n.93 and authorities cited therein.
134 Conn. 532 (1827).
136 36 Del. Ch. 563, 134 A.2d 852 (Ch. 1957).
First of all, it charges that the two directors (Tomlinson and Meyer) failed to cooperate with Vogel [the president] in his announced program for rebuilding the company; that their purpose has been to put themselves in control; that they made baseless accusations against him and other management personnel and attempted to divert him from his normal duties as president by bombarding him with correspondence containing unfounded charges and other similar acts; that they moved into the company's building, accompanied by lawyers and accountants, and immediately proceeded upon a planned scheme of harassment. They called for many records, some going back twenty years, and were rude to the personnel. Tomlinson sent daily letters to the directors making serious charges directly and by means of innuendos and misinterpretations.\(^{137}\)

The court held that the desire of the director to seize control of the corporation was perfectly legitimate in itself, and hence neither it nor refusal to cooperate with Vogel constituted cause for removal. But conducting a planned scheme of harassment was another matter:

Certainly a director may examine books, ask questions, etc., in the discharge of his duty, but a point can be reached when his actions exceed the call of duty and become deliberately obstructive. In such a situation, if his actions constitute a real burden on the corporation then the stockholders are entitled to relief. The charges in this area . . . are legally sufficient to justify the stockholders in voting to remove such directors. . . .\(^{138}\)

One way of looking at the case is to view it as involving a breach of the duty of loyalty. Although it is perfectly proper for a director to try to advance his own interests by grappling for control of the corporation, this is because he sincerely identifies the best interests of the corporation with his coming to power. But it may happen that the director's desire to control will get the better of him. While few persons would deliberately destroy an enterprise in order to preside over the rubble, the director may take steps which he knows will cause the company some injury or, probably more likely, stop considering the company's interest altogether. This could easily be deemed disloyalty, a placing of the director's personal welfare ahead of the company's.

By the same token, the case may be viewed as a violation of the director's duty of care. Under this theory the director's will to power so warps his judgment that he no longer can discern where the best interests of the company lie. He still believes he is advancing the interests of the company, but his judgment is almost completely faulty.\(^{139}\) He takes positions and performs acts which a reasonable, objective observer would avoid.

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\(^{137}\) Id., at 576, 134 A.2d at 860.

\(^{138}\) Id., at 576-77, 134 A.2d at 860-61.

\(^{139}\) For example, the counsel for Vogel in the bitter fight over Loew's has described in detail some of the tactics employed by his opponents. In one letter Tomlinson questioned the wisdom of a particular move from a tax standpoint. Whatever other objections might have been made, it seems clear that it was poor judgment for a director to go on record in a way which might ultimately be used against the corporation by the tax authorities. See L. Nizer, My Life in Court 449-51 (1961).
However, there is yet another element in the case. Suppose a reasonable man could have decided that Vogel’s rebuilding program was the sheerest folly, that it was likely to cost the corporation dearly. Suppose further that this reasonable man could also conclude that Vogel’s presidency represented, in effect, the continuation in power of a discredited faction of the corporation. Could it not be argued that under such circumstances he would have a duty to the corporation to seek power, to refuse to cooperate with Vogel, and even to harass Vogel? In any case, could it be said that the director was being disloyal or negligent if he turned obstructionist?

The director’s position in the case hypothesized requires the court to make an assessment of the probable impact of a projected program. Courts are notoriously reluctant to make legal rights and obligations turn on an evaluation of the wisdom of management policy. The so-called “business judgment” rule which protects directors charged with negligence seems largely an acknowledgement by the courts that only in extreme cases are they qualified to judge policy. One alternative to doing this is to enforce rigidly the hierarchy set up by the statute, the corporate papers, the board, or custom. Corporate officials are expected to respect their places in that hierarchy, to obey their superiors, to decline to arrogate power to themselves, and to employ the accepted channels in presenting their views. Once decisions have been made in the appropriate manner, officials should accept them or seek to get them reversed by going through the same channels; they should not subvert the hierarchy by obstructing decisions. One way of enforcing the structure is to approve the ouster of any director who seeks to subvert it, regardless of the merits of the policy dispute. In other words, cause for removal exists if the director is not being a good organization man, regardless of whether his conduct constitutes a breach of duty.

The Campbell case may be looked upon as an example of this theory. As such, it would fit in with a group of cases which do not easily fit the breach-of-duty mold. The clearest of these are those cases which hold that insubordination by a director-officer is per se cause for his removal. Similarly, there are also cases involving a director-officer acting without authority or attempting to bring improper pressure

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140 This is apparently a very unlikely hypothesis. See the account of the results of Vogel’s program, id. at 521–22.

141 Some objective observers, such as bankers, did take this view. Id. at 441.

142 See Dyson, supra note 131, at 367–71, for a perceptive discussion of this “rule.”


144 Smock v. Buchanan & Smock Lumber Co., 95 N.J. Eq. 308, 125 A. 115 (Ct. Err. & App. 1928); People v. Lyon, 119 App. Div. 361, 104 N.Y.S. 319, aff’d per curiam, 189 N.Y. 544, 82 N.E. 1130 (1907). Both of these cases involved execu-
to bear upon the board by stirring up employees, customers, and suppliers. In none of these cases were the courts much concerned with who was right. It was found to be enough that the ousted party stepped out of line. On the other hand, several cases have held the shareholders do not have cause to remove directors who have ousted a president with whose policies the shareholders agreed. Here the judicial concern with enforcing the hierarchy led to a finding that the cause was insufficient, but the same principle was operating.

These cases go beyond Lord Mansfield's dictum, since insubordination or uncooperativeness per se would not necessarily be grounds for surcharging a director even if some harm to the corporation might result. The second hypothesis, that cause for removal exists where the ousted official has not been a good organization man, would seem necessary to explain them. It is notable that this hypothesis is also roughly related to the objective of protecting the non-financial rewards accruing to the director from his position. It may seem paradoxical that any expansion of the right of removal beyond the flagrant cases could protect the director. But the rewards of prestige and decision-making power largely depend upon the preservation of the corporate hierarchy. By protecting this hierarchy even if it means permitting the removal of the obstreperous director, the courts protect the rewards of all directors as a class. Therefore, the interests of all directors are furthered by sacrificing the isolated individual director who threatens the system upon which those interests depend.

In sum, then, cause for removal exists when the director has been guilty of conduct which, had it led to injury to the corporation, would warrant his being surcharged. Removal is also proper if the director has in one way or another attempted to subvert the corporate power structure. Clearly, both types of cause are broad enough to encompass cases requiring difficult fact-finding and delicate judgments about the significance of those facts. In such cases, the nature of the tribunal is important. This raises the question of the extent to which the courts defer to the findings of fact and the ultimate decisions of the intra-corporate tribunals which are required to conduct the removal proceedings.

tives, but they were elected for a term, not appointed, thus making their status much like a director's.

147 A subordinate might well conclude that the policy was so injurious to the corporation that the short-run injury caused by friction would be much less than the long-run injury resulting from the pursuit of the superior's policy.
B. The Intra-corporate Hearing

It would be possible to permit removal only for cause and yet not require any hearing, which is essentially the situation with regard to the executive with a contract.\textsuperscript{149} Or it would be possible to require that certain procedural formalities be met, such as notice and an opportunity to be heard, without restricting the discretion of the shareholders as to the grounds upon which they are entitled to remove a director.\textsuperscript{150} In such a case, the requirement of a hearing would seem to be a bit of judicial paternalism. It would give the director some chance to present his side, even though his arguments would inevitably fall on deaf ears, and it would guarantee the shareholders the chance to hear both sides, even though they have their minds made up and could care less what the director has to say.

The fact that the law contains both rules suggests that the shareholders are expected to function as an adjudicatory body and that the various rules regarding the hearing are designed to facilitate the process of adjudication. Both the secondaries and the decisions contain language to the effect that the shareholders are to act judicially,\textsuperscript{151} although it seems agreed that this does not necessarily mean that the procedures must be as formal as those of a court.\textsuperscript{152} Even more striking evidence of the fact that the requirement of legally sufficient cause and the procedural rules are designed to interact are two cases in which such an interaction is an integral part of the holding. In one case,\textsuperscript{153} the plaintiff was removed as a director of a membership corporation which had a bylaw authorizing the board to remove one of its members at any time with or without cause. When the plaintiff sought reinstatement, the court held that it was unnecessary to decide whether the bylaw violated the statute. In the plaintiff's case his expulsion was ostensibly for cause and, hence, the plaintiff was entitled to fair notice and an opportunity to be heard, neither of which he received. In other words, the court suggests that certain procedural consequences followed from the decision to remove the plaintiff for cause even though the board was apparently free to act as arbitrarily as it liked. On the other hand, where the corporation's bylaws permitted removal without cause and the plaintiff was removed arbitrarily, he was not

\textsuperscript{149} See text accompanying notes 20–31 supra.

\textsuperscript{150} This appears to be the situation in England under § 184 of the Companies Act of 1948, 11 & 12 Geo. 6, c. 38.

\textsuperscript{151} See, e.g., Costello v. Thomas Cusack Co., 96 N.J. Eq. 83, 124 A. 615 (Ch. 1922); Auer v. Dressel, 306 N.Y. 427, 434, 118 N.E.2d 590, 594 (1954) (dissenting opinion); 2 W. Fletcher, supra note 115, at § 360.

\textsuperscript{152} Campbell v. Loew's, Inc., 36 Del. Ch. 563, 134 A.2d 832 (Ch. 1957).

\textsuperscript{153} Norman v. Roosevelt Democratic Club, 17 Misc. 2d 219, 184 N.Y.S.2d 980 (Sup. Ct. 1959).
entitled to complain of the lack of notice and hearing. These cases seem consistent only with the view that the hearing is an adjudication and the director's right to notice and hearing are shaped by their function of facilitating this adjudication.

Thus, the notice to the director serves as an initial pleading and must be detailed enough to enable the director to prepare his case. The typical vague notice of meeting sent to shareholders in American corporations would not be detailed enough for these purposes. It has been held that a simple statement that the agenda includes a vote on the removal of a particular director is not adequate notice. Similarly, the fact that the shareholders are to act judicially implies certain things about the amount of time for preparation a director should be given. Since an adjudicator is supposed to base his decision solely on the evidence and not on emotional appeals, the director will need more time to prepare than he would if emotional appeals were proper. In some instances, the director is entitled to present evidence and witnesses and to be represented by counsel. The time allowed must therefore be appropriate for preparation for trial rather than to writing a political address.

Suppose, however, that the director is afforded all of these safeguards. What is to prevent the shareholders from ignoring what he says? What is to prevent disingenuous fact-finding or the labeling of perfectly innocuous behavior as incompetence or honest attempts to help as disloyalty? If there is to be some guarantee that the whole hearing will not be a sham, there must be some judicial review of the intra-corporate proceedings. The issue is what the scope of this review shall be. To the extent that the reviewing court defers to the corporate tribunal, the director's protection clearly becomes less complete. Anything less than a trial de novo subjects the director to certain risks. Moreover, in certain specific cases, there is less reason to trust the findings of the corporate tribunal, as where the director removed was a minority representative, or there is evidence that the

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removal resolution was drafted before the meeting, or there is evidence of widespread prejudice among the shareholders.

Nevertheless, if the court is to conduct a trial de novo, why bother to hold an intra-corporate hearing in the first place? The executive under contract can go directly to court and get an impartial hearing. With a trial de novo the director gets that and an intra-corporate hearing too. The intra-corporate hearing takes on the aspect of a weapon to be used by the recalcitrant director in a war of attrition against those who seek to oust him. Since no one has suggested that the director's enemies are entitled to get judicial review of an unsuccessful removal attempt, it is doubtful if the hearing would be an equally potent weapon for the other side.

There seems to be no consensus among the cases as to the proper scope of judicial review. Some courts have conducted trials de novo and reached their own conclusions. Other courts, however, have seemingly gone to the opposite extreme and refused to review the proceedings at all. The early English case of *Inderwick v. Snell* sums up the position of these authorities:

> But the question is, whether by this deed the shareholders duly assembled at a general meeting might not, or had not a right to, remove a director for a cause which they thought reasonable, without its being incumbent upon them to prove to this or any other Court of Justice that the charge was true and the decision just, or that the case was substantiated after a due consideration of the evidence and charge.

The court decided that the shareholders had that right. In effect, these courts are saying that removal at will is proper, and there is not much point in talking about judicial review at all.

There are, of course, intermediate positions which might be adopted. The courts could apply the standards used in reviewing an administrative agency or in reviewing the findings of fact of a trial judge. If the courts were to adopt an intermediate position, it would be incumbent upon them to prescribe what sort of a record the corporate tribunal should make. If the shareholders are all present at the hearing, so that there is no proxy literature at all, should the courts require a transcript? If the bulk of the votes are to be cast by proxy,

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168 *Id.* at 222-23, 42 Eng. Rep. at 86.
170 *Fed. R. Civ. P. 52(a).*
should there be any adaptations of the SEC's proxy rules to take account of the fact that the shareholders are now acting "judicially"? In any event, the decision of the tribunal will be most like a jury verdict, with no accompanying statement of justifications. Should a general verdict be accepted or should the shareholders be required to render a special verdict?

These questions suggest that any intermediate position on the scope of review would require the courts to face and to answer a large number of questions which have as yet seldom been asked. This is an unpalatable prospect, but the other options are to conduct a trial de novo, which makes the hearing superfluous, or to decline to review the proceedings at all. This last approach seems the most attractive, but it seems incompatible with the law as it presently stands. Unless the law is changed to allow the shareholders simply to vote rather than adjudicate, it is doubtful that any satisfactory solution can be reached.

IV. CONCLUSION

This survey of the law regarding removal of corporate directors has suggested that the interest being furthered by making removal difficult is the director's personal interest in the non-financial rewards which accrue to him by virtue of his position. The possibility of other interests being furthered seems excluded by one or more of the rules of law in this area. Generalization from the cases defining "cause" for removal produces definitional hypotheses which seem consistent with the idea that it is the director's interest in the political and psychological rewards of his position which is being protected. Yet the courts have not definitely committed themselves to making that protection as complete as possible by decreeing a trial de novo when review of an intra-corporate hearing is sought by an ousted director. To the extent that the courts will defer to the decisions of the corporate tribunal, the removal rules become little more than traps for the unwary; they will not protect a director against a determined, well-counselled majority which is willing to preserve all the outward trappings of a fair hearing. With a trial de novo, the intra-corporate hearing becomes superfluous except as a weapon to be wielded by the director.

It would seem that a strong case may be made for allowing shareholders to remove corporate directors at will without having to justify their act in a court or being forced to hold a hearing. Establishing removal at will as the basic norm certainly would not eliminate all of the problems in this area. In states in which cumulative voting is permitted or required, safeguards would have to be devised to prevent a majority faction from using its removal power to oust minority repre-
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Possible conflicts with other corporate norms would also have to be resolved, as would various problems presented by shareholder agreements in close corporations. Nevertheless, it would seem that a rule permitting removal at will is a better starting point for reaching a satisfactory solution of these problems than the present rule. Those states which already established removal at will as the basic norm by legislation seem on sound ground.

All of this is not intended to slight in any way the interest of the director. Many directors make substantial sacrifices when they accept their positions; many are forced to forego subsequent opportunities. The director is entitled to the same protection as the corporate executive. If the director or the executive is ousted arbitrarily, it may be that he has sustained an injury for which a tort remedy is available. Such a remedy would not depend on contract. Moreover, making removal at will possible would probably induce directors to get contracts from their corporations containing some guarantee of tenure. With such a contract, the director would be given the same remedies as the executive has now. He would not get specific relief, and there would be no intra-corporate hearing. The director would thus have available the same remedies as the executive.

171 The Model Act resolves this conflict by prescribing:

If less than the entire board is to be removed, no one of the directors may be removed if the votes cast against his removal would be sufficient to elect him if then cumulatively voted at an election of the entire board of directors, or, if there be classes of directors, at an election of the class of directors of which he is a part. ABA-ALI MODEL BUS. CORP. ACT § 36A (rev. ed. 1959).

The court in Campbell v. Loew's, Inc., 36 Del. Ch. 563, 134 A.2d 852 (Ch. 1957), relied on the procedural safeguards and the cause requirement to protect the minority.

172 E.g., Essential Enterprises Corp. v. Automatic Steel Prods., Inc., 39 Del. Ch. 371, 159 A.2d 288 (Ch. 1960) (classification of board held to conflict with power to remove at will—removal at will restricted to removal for cause).

173 See, e.g., cases cited in note 112 supra.

174 In an article entitled Individual Freedom vs. Employment at Will: On Limiting the Abusive Exercise of Employer Power, to be published in a forthcoming issue of the Columbia Law Review, Professor Lawrence E. Blades argues persuasively that a tort theory is needed to protect legitimate employee interests left unprotected by traditional contract theories.

175 As a practical matter, it would seem advisable to get the shareholders to approve such contracts as an incident of electing directors; otherwise any contract made by the directors themselves might be held subject to the superior power of the shareholders to remove at will. See Read v. Astoria Garage (Streatham), Ltd., [1952] 1 All E.R. 922, aff'd, 1 Ch. 637 (C.A.), discussed by Professor Gower in 16 Mo. L. REV. 82 (1953).