

SECURITIES AND EXCHANGE COMMISSION
Corporation Finance Division
Office of the Counsel

MEMORANDUM TO ATTORNEYS ON STAFF

Re: Commonwealth v. Green

A recent judicial decision in which a question arose as to the persons who may challenge violations of the Commission's Proxy Rules is attached. Part of the opinion which discussed the necessity of nominations as a prerequisite to election to the office of corporate director has been omitted.

Edward H. Cashion
Counsel

Attachment

IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY,
PENNSYLVANIA

COMMONWEALTH OF PENNSYLVANIA, *ex rel.* JOHN E. LAUGHLIN, JR. and T.
W. KIRKPATRICK

vs.

EDWARD H. GREEN AND D. S. FAULKNER

No. 459 July Term, 1944

Before: Dithrick and Kennedy, JJ.

OPINION

By DITHRICH, J.

This action of quo warranto is now before the court for judgment on the pleadings. It was previously before the court on a motion to quash the writ. The motion was refused. Respondents then answered on the merits, to which answer relators entered a general demurrer, and respondents have joined in the demurrer. Thus issue is joined and under common law practice the averments of fact in the answer, if well pleaded, must be taken as verity. The issue involves a disputed election of directors for the National Supply Company, a Pennsylvania corporation.

The by-laws of the corporation provided for a board of twelve directors to be elected at the annual stockholders' meeting in April 1944 in three groups or classes, viz.; directors of the third class to serve for three years, directors of the second class to serve for two years, and directors of the first class to serve for one year. Those receiving the four highest number of votes at the April 1944 meeting were to be elected directors of the third class, those receiving the next four highest number of votes directors of the second class, and those receiving the next four highest number of votes directors of the first class. At each subsequent annual meeting, four directors are to be elected for terms of three years each.

At the April 1944 meeting twelve persons, including the two respondents, were nominated for directors. Neither of the relators was nominated. Laughlin, one of the relators, received the seventh highest number of votes, which, had the votes been counted, would have entitled him to membership on the board as a director of the second class. Kirkpatrick, the other relator, placed thirteenth in the balloting and thus failed to be elected. Green, one of the respondents, received the ninth highest vote, and Faulkner, the other respondent, placed fourteenth in the balloting and thus failed of election. However, Green objected to any votes being received for any person who had not been nominated, the objection was sustained by the Judges of the election, and the votes cast for Laughlin and Kirkpatrick were rejected. Green, who received the ninth highest number of votes, was declared a director of the second class for a term of two years and Faulkner a director of the first class for a term of one year.

Objection also was made to the voting of any stock for which the minority group, as distinguished from the management group, had received proxies, on the ground that the proxies had been obtained by false and fraudulent representations. The objection was overruled by the Judges of election.

After the twelve names had been placed in nomination for the twelve offices to be filled, a motion was made that the nominations be closed. The motion carried without any dissenting vote, but Laughlin, who held the proxy of the Pittsburgh Steel Company, voted its stock cumulatively for himself, and certain other stock, for which the minority group held other proxies, was voted for Kirkpatrick, although neither Laughlin or Kirkpatrick had been nominated. J. H. Hillman, Jr., who was nominated and elected a director of the third class, had originally held the Pittsburgh Steel Company proxy, but through the exercise of the power granted him by the proxy he substituted Laughlin for himself.

Since Kirkpatrick, who placed thirteenth in the balloting, cannot succeed if Green is ousted from the office of director of the second class, since Laughlin then would automatically succeed to that office, and Green would be relegated to the office of director for one year, Kirkpatrick's claim to a seat on the board of directors is not being pressed.

(The Court then held that there was no requirement that the two relators had to be nominated before being eligible for election and that a shareholder has a "fundamental right . . . to vote for whomsoever he pleases.")

There remains to be disposed of the question whether the proxy committee, representing the minority interests, violated the Federal Securities and Exchange Act or the rules and regulations of the Securities and Exchange Commission in soliciting proxies on the representation that no effort would be made to defeat any of the present directors when, in fact, it was their intention to unseat two of them. Regardless of whether or not such action was in violation of the Act or rules and regulations of the Commission, respondents have no right or authority to challenge the action of the Judges of election in refusing to reject the votes on that ground. Only the shareholders, whose proxies had been obtained by the minority group, or the Securities and Exchange Commission would have that right, and, in the case of the latter, it could be asserted only in a District Court of the United States. The demurrer will be sustained.