

ANNOUNCEMENT

The REVIEW takes pleasure in announcing the election of the following members of the Third Year class to the Editorial Board: Edward A. Kaier, Guy W. Knight, Joseph J. Lawler, Joseph M. Leib, William C. Wise and Max M. Yaffe.

NOTES

SHAREHOLDERS' RESPONSIBILITY FOR IMPROPER DIVIDENDS—It has frequently been stated that the responsibility of shareholders for receiving a so-called improper dividend is determined by a group of factors often vague and uncertain.¹ Here, as in other types of cases, the indiscriminate use of such terms as profits, surplus, capital and insolvency is often the cause of confusion. Furthermore, the statutes which regulate the declaration of dividends are not as uniform as one is lead to believe² but often vary in respect to funds from which payments are to be made and to conditions precedent concerning depletions of capital stock. However, the usual type of statute, as at common law, limits the declaration of dividends to payments out of profits or surplus.³

Since the possible situations under which a contested payment may be distributed are numerous, an examination of only the more usual ones will be made. The first situation exists where the corporation, after the payment to shareholders having no knowledge of conditions, has enough assets left to meet the claims of creditors existing at the time of the allegedly improper payment; but the remaining assets are not equal to the amount of creditor's claims plus the par value of shares outstanding which had been created and fully paid at par. In this situation the Supreme Court of the United States⁴ has refused to recognize any responsibility on the part of shareholders and this result has since been reached by other courts.⁵ On the other hand an unfortunate use of terms in an earlier federal case⁶ has been the basis for decisions permitting recovery.⁷ It was stated that "the capital stock is a trust fund⁸ for creditors and the stock-

¹ 2 COOK, CORPORATIONS (8th ed. 1923) § 548; 12 FLETCHER, CYCLOPÆDIA OF CORPORATIONS (1932) §§ 5422-5424; 7 THOMPSON, CORPORATIONS (3d ed. 1927) § 5346.

² See Weiner, *Theory of Anglo-American Dividend Law* (1929) 29 COL. L. REV. 461, 462. It is the failure to comply with this rule which usually renders a dividend improper, and the present discussion will be confined to this situation. However, improper dividends are not restricted to those dividends which impair capital stock, but also exist where the declaration has not complied with the set technique. See *Atherton v. Beaman*, 264 Fed. 878 (C. C. A. 1st, 1920) and *Berryman v. Bankers Life Insurance Co.*, 117 App. Div. 730, 102 N. Y. Supp. 695 (1907). In both of these cases dividends were paid without the formal declaration by the directors. Yet in view of the "solvency" of the corporation, responsibility of the shareholders was denied in both cases.

³ 2 COOK, *op. cit. supra* note 1, § 546; 11 FLETCHER, *op. cit. supra* note 1, § 5329; 7 THOMPSON, *op. cit. supra* note 1, § 5290.

⁴ *McDonald v. Williams*, 174 U. S. 397, 19 Sup. Ct. 743 (1899).

⁵ *Great Western Mining & Mfg. Co. v. Harris et al.*, 128 Fed. 321 (C. C. A. 2d, 1903); *Forster v. Folz, W. D. Pa.*, U. S. Daily, Aug. 22, 1932, at 1166; *Carlisle v. Ottley*, 143 Ga. 797, 85 S. E. 1010 (1915). See *Bartlett v. Smith*, 160 Atl. 440 (Md. 1932) (for dissenting opinion see 161 Atl. 509). *Miller v. Bradish*, 69 Iowa 278, 28 N. E. 594 (1886) (decided before *McDonald v. Williams*, *supra* note 4). It is immaterial in these cases whether the action be in equity or at law.

⁶ *Wood v. Dummer*, 3 Mason 308 (C. C. Me. 1824).

⁷ *Dudley v. Price's Adm'r*, 10 B. Mon. 84 (Ky. 1849); *Mobile Towing & Wrecking Co. v. Hartwell*, 208 Ala. 420, 95 So. 191 (1922).

⁸ The trust fund theory is a misnomer for there is neither a trustee nor a *cestui que trust* in the strict sense of the word. See Hunt, *The Trust Fund Theory and Some Substitutes for It* (1902) 12 YALE L. J. 63, 65. For a discussion of the theory in its application to other situations, see Note (1908) 8 COL. L. REV. 303; Note (1916) 4 VA. L. REV. 131. For an interesting historical and psychological discussion of the theory see Zettler, *The "Trust Fund Theory": A Study in Psychology* (1925) 1 WASH. L. REV. 81.

holders upon the division take it subject to all the equities attached to it." This statement is very convenient if a court is desirous of protecting the creditors since by the use of trust terms the "trust" property may be recovered from one who is a mere donee.⁹ The same result has been reached by using language of a different nature, such as constructing a contract between the shareholders and the creditors at the time the corporation incurred the debts, the terms of which are that capital shall be applied only to the satisfaction of the demands of creditors, and until such satisfaction, the creditors are given an equitable lien.¹⁰

But the protection of creditors can be accomplished by means of a far more rational theory requiring a sufficient excess of assets over liabilities to third parties to remain after payment of the dividend in order to provide a margin for the normal shrinkage of assets or increase of liabilities. This accords with the normal business policy of a prudent creditor who usually tries to protect himself by insisting upon a net worth which will adequately cover this margin. The apparently conflicting cases can be reconciled if this fundamental concept is retained as a standard by which to judge the decisions.

Although the situation usually arises when suit is brought to recover the amount of the dividend from the shareholder, the question might very well be asked what result would be reached should the shareholder bring suit to recover an unpaid dividend declared from a fund other than the statutory designation of profit.¹¹ This query seems to be partially answered in a case¹² which permitted a stockholder to recover his *pro rata* share of a dividend declared "in excess of the net profits" even though this was "an impairment of the capital stock." It is important to note that no creditors were involved and that the amount of the corporation's debts were negligible so that the creditors who did exist at the time were amply protected from any normal depreciation in assets.

If the status of the creditor is changed in the original set of facts, by causing the debt to arise subsequent to the allegedly improper payment, it would seem, as suggested by a learned text writer,¹³ that the creditor's equitable claim can "attach only to the property of the corporation." But this of course assumes the answer, *i. e.*, whether the corporation has a property interest in dividends improperly declared.¹⁴ The decisions tend to favor the creditors. One case¹⁵ treated the shareholders as representing the capital stock to be of the nominal amount and held them liable for having secretly withdrawn part of it. Here, however, only fifty per cent. of the capital stock was paid in. Another court considered the injury as great to subsequent creditors as to prior creditors, and allowed recovery in both cases. In a suit¹⁶ by a trustee in bankruptcy against

⁹ It has been repeatedly held that a stockholder who receives a dividend which is wrongful is not a *bona fide* purchaser. *Wood v. National City Bank*, 24 F. (2d) 661 (C. C. A. 2d, 1928); *Davenport v. Lines*, 72 Conn. 118, 44 Atl. 17 (1899); *Clapp v. Peterson*, 104 Ill. 26 (1882). Accordingly, it may be traced into his hand. *Arnold v. Knapp*, 75 W. Va. 804, 84 S. E. 895 (1915).

¹⁰ *Clapp v. Peterson*, *supra* note 9. This case is also interesting because of the use of the term "insolvency". The court considered the corporation insolvent because it was unable to meet not only claims of third parties but also the par value of the stock outstanding. The capital stock on the balance sheet of a corporation is considered a liability but under the usual interpretation of the figures for the purpose of determining insolvency, it is not included either as an asset or a liability. See *Rett, When Is a Corporation Insolvent?* (1932) 30 MICH. L. REV. 1040, 1043.

¹¹ Ordinarily if a dividend is properly declared the relation of debtor and creditor arises between the corporation and the stockholder. See 7 THOMPSON, *op. cit. supra* note 1, § 5308.

¹² *Thiry v. Banner Window Glass Co.*, 81 W. Va. 39, 93 S. E. 958 (1917).

¹³ 2 MORAWETZ, PRIVATE CORPORATIONS (2d ed. 1886) § 800.

¹⁴ One case definitely answers this question by asserting that they are property of the corporation. *Gager v. Paul*, 111 Wis. 638, 87 N. W. 875 (1901).

¹⁵ *Williams v. Boice*, 38 N. J. Eq. 364 (1884).

¹⁶ *Cottrell v. Albany Card & Paper Manufacturing Co.*, 142 App. Div. 148, 126 N. Y. Supp. 1070 (1911).

a single shareholder the same result was reached by saying that the withdrawal of funds was constructive fraud.¹⁷ Where a stock dividend instead of a cash dividend was involved,¹⁸ the court implied a promise to pay the par value, but only in favor of subsequent creditors. One court,¹⁹ in *obiter dicta*, has gone so far as to recognize the right of shareholders to receive improper dividends as against subsequent creditors.

Where a shareholder sought to enforce payment of notes received in payment of a dividend, part of which was declared from the fund created by the par value of the stock, generally known as capital, a lower Pennsylvania court held that he could share in the same proportion as subsequent creditors when the corporation became insolvent.²⁰

If the original set-up is varied by giving the shareholders reasonable grounds to believe that the payment was out of capital then there is no receipt in good faith. The decisions are scant but there is some *dictum*²¹ to the effect that the shareholder is liable. An eminent jurist²² has stated this difference in result when bad faith is present, to be based on ordinary legal principles, for where there is good faith, the shareholders are "innocent participants" and not "accomplices to its commission."²³ The distinction, of course, is immaterial if statutory liability is incurred by receiving a dividend other than from a proper fund.²⁴

Where the corporation is not only unable to satisfy the par value of outstanding shares fully paid, as in the original set of facts, but also is unable to meet all its obligations to third parties, the courts will usually sustain the action of the party attempting to recover the payment.²⁵ Trust terms²⁶ are again²⁷ used in this connection,²⁸ but the courts indicate that good faith of the recipient

¹⁷ Mackall v. Pocock, 136 Minn. 8, 161 N. W. 228 (1917).

¹⁸ Anglo-American Land, Mtge. & Agency Co. v. Lombard, 132 Fed. 721 (C. C. A. 8th, 1904).

¹⁹ See Montgomery v. Whitehead, 40 Colo. 320, 90 Pac. 509 (1907). To substantiate the *dictum* the court cited several cases which are not in point.

²⁰ *In re Beitzel & Sons*, 45 York Legal Record 9 (1931).

²¹ See Johnston v. Laffin, 103 U. S. 800, 803 (1880).

²² Judge Learned Hand in Wood v. National City Bank, *supra* note 9.

²³ It has been advanced that the mental attitude should have no weight in reaching a decision because the stockholders have chosen the directors and if they have failed in judging their integrity and honesty they should be held liable since they have represented that there will be a compliance with the law. (1915) 81 CENT. L. JOUR. 225, 227. This is theoretically correct but practically untrue since it is known that a choice of directors is made today by a comparatively few stockholders.

²⁴ American Steel & Wire Co. v. Eddy, 138 Mich. 403, 101 N. W. 578 (1904).

²⁵ Ulness v. Dunnell, 61 N. D. 95, 237 N. W. 208 (1931); Hayden v. Williams, 96 Fed. 279 (C. C. A. 2d, 1899).

²⁶ Bartlett v. Drew, 57 N. Y. 587 (1874). A recovery was denied in MacLean v. Eastman, 21 Hun 312 (N. Y. 1880), on the ground that it was brought in law and not in equity. One court stated that there was constructive notice to the stockholders of the "insolvent" condition. Penzel v. Townsend, 128 Ark. 620, 195 S. W. 25 (1917).

²⁷ A Mississippi court has a commendable approach refusing to succumb to the path of least resistance offered by the use of trust terms. "The capital stock of a corporation is a fund set apart, among other purposes, for that of paying the debts of the corporation; and whether or not it be a trust fund, impressed with all the attributes of such a fund, it seems to be universally held, upon sound and plain principles of common honesty, that it cannot be withdrawn by the stockholders until all the debts then owing by the corporation have been paid." Kimbrough v. Davies, 104 Miss. 722, 735, 61 So. 697, 698 (1913).

²⁸ In Gaunce v. Schoder, 145 Wash. 604, 261 Pac. 393 (1927), the court draws an analogy to stockholder's liability for unpaid subscriptions, stating that after insolvency the liability for both was only in equity to the extent that it is necessary to complete the trust fund to pay all creditors. The basis of a creditor's bill in equity is the inability, at law, of creditors to reach certain corporate assets in the possession of stockholders. See Barrows, *The Equitable Liability of Stockholders, the Ground Upon Which It Rests* (1903) 13 YALE L. J. 66, 67. This, however, seems to be assuming the answer to the problem, *i. e.*, whether or not it is a corporate asset, as has been noted above. A more appropriate analogy might be drawn to the case of a receiver of an insolvent estate bringing an action against legatees for sums received before payment to creditors. See (1928) 37 YALE L. J. 1157.

is immaterial since these sums are gifts.²⁹ If the defendant had knowledge from which he might reasonably infer that the payment was made from an improper fund, it becomes an *a fortiori* case.³⁰

If the creditors, who are claiming rights, became such subsequent to the time of payment, the result in the federal courts is in favor of the shareholder.³¹ An Indiana court refused to recognize a distinction between these two classes of creditors.³² In the latter case, however, the item "capital stock" was carried on the balance sheet as an asset instead of a liability, and although this gave the appearance of solvency, the corporation was actually unable to meet its obligations to creditors. This seems to demonstrate further the suggestion advanced, for even though the subsequent creditor is not involved at the time of the payment he is nevertheless deemed to have been harmed by the improper payment. This indicates that the predominating thought in the minds of the judges is the preservation of the structure of business activity by adequately protecting those who are or may become creditors of the corporation. If the business world was advised of the ease with which capital can be withdrawn from these enterprises the results would be destructive of the very system itself.³³

A probable situation, as yet undiscussed by the courts, might arise where the subsequent creditor has inquired into the financial status of the corporation and in spite of an unfavorable report from a reliable business agency nevertheless advanced the credit. This problem may arise either when the corporation is still in a position to meet claims of third parties or when it is unable to do so. In the latter situation it seems that the creditor is doing nothing more than gambling, and if he has wilfully walked into his unfortunate position, innocent persons should not be affected by his foolhardy act. The decisions, couched in terms of implied contract, forms of estoppel, and constructive trust, indicate that the basis of recovery is the inability of the creditor to ascertain the true financial position of the corporation. If, therefore, with full knowledge of conditions, the creditor assumes the risk, then applying the suggested underlying philosophy of all these cases, there seems to be no reason why the court should desire to protect one who has recklessly extended credit where ordinarily a prudent business man would have refused to do business other than on a cash basis.

Another interesting factor which might be considered is whether or not the stock was sold for a price less than its par value. The courts apparently do not place much stress on this consideration since it is mentioned casually, if at all. There is, however, a case³⁴ in which only thirty per cent. of the par value was paid in, and a contract between the shareholders and the corporation provided

²⁹ Powers v. Heggie, 268 Mass. 233, 167 N. E. 314 (1929). See comment thereto in (1930) 28 MICH. L. REV. 337.

³⁰ Hayden v. Thompson, 71 Fed. 60 (C. C. A. 8th, 1895); Corn v. Skillern, 75 Ark. 148, 87 S. W. 142 (1905); Finn v. Brown, 142 U. S. 56, 12 Sup. Ct. 136 (1891).

³¹ See Ratcliffe v. Clendenin, 232 Fed. 61 (C. C. A. 8th, 1916). The exact question was raised in Wood v. National City Bank, *supra* note 9, where a bill was held insufficient for failing to allege whether the creditors were prior or subsequent.

³² Fricke v. Angemeier, 53 Ind. App. 140, 101 N. E. 329 (1913).

³³ Another possible ground of recovery is fraud on creditors. See Johnson v. Canfield Sugart Co., 292 Ill. 101, 115, 126 N. E. 608, 614 (1920). A text-writer on this subject has suggested that the statutory direction preventing depletion of capital is for the benefit of the stockholders under one view, or for the protection of creditors under another view. Under the latter view a recovery is always permitted when the dividend impairs capital, while under the former view there can only be a recovery when the corporation is actually insolvent at the time of payment. Furthermore, he asserts that a creditor should have no right to object to dividends if there are enough assets to pay all the debts. GLENN, FRAUDULENT CONVEYANCES (1931) § 421. This last statement is quite in accord with the suggestion advanced in this note.

³⁴ Gager v. Paul, *supra* note 14.

that the balance was to be disregarded. The corporation at the time of the improper distribution was unable to meet claims of third parties and the court would undoubtedly have affirmed liability except that the suit was brought against the wrong party. Had the corporation been able to meet claims of third parties and were the buffer large enough to cover normal losses, the court would probably have applied, although perhaps not patently, the business man's attitude and have refused to recognize liability.

Somewhat affiliated to the last problem is the right of a shareholder to set off an "improperly" declared but unpaid dividend against an unpaid stock subscription. If the original declaration is invalid, no debt is created, and it would seem that there is nothing to set off.³⁵ On the other hand, there is some *dictum*³⁶ to the effect that if at the time of the declaration there were enough assets to meet claims of third parties, there could be a valid set off. This seems proper in the light of the above discussion, since the court has taken into consideration the margin of protection and has realized that the creditors' safety is the important factor.³⁷

The margin may be reduced by failing to take into account certain contingencies³⁸ which, as managers of a careful business enterprise, the directors should have considered. Where such a failure proved detrimental to the financial condition of the corporation, the court again applied, perhaps unconsciously, the principle enunciated, and concluded that the dividends were improper and must be refunded. On the other hand, where the corporation at the time of declaration and payment was on a high plane of prosperity, but subsequently an unforeseen destruction of property tumbled it into hopeless insolvency, the propriety of the dividend was not questioned.³⁹

An Iowa case⁴⁰ presents a notable illustration of the soundness of the theory herein advanced. In spite of a payment out of a fund consisting of the par value of the outstanding shares, the court refused to recognize any liability. A ten per cent. dividend of \$10,686 was declared entirely out of this fund. However, the remaining assets of \$146,218.65 were more than enough to meet the liabilities to third parties of \$56,065.23. The court was fortunate in being able to rest its decision on a strict construction of a statute which provided for liability of shareholders for receiving improper dividends when there were insufficient assets to meet liabilities.⁴¹ The language of the decision is permeated with the unexpressed thought that the creditors have no right to object since they are amply protected.

Such thoughts, however, have found expression in connection with an analysis of legislation requiring payments to be made out of designated funds.

"The statute [referring to dividends] does not allow capital to be depleted by means of dividends up to the very point of insolvency; on the contrary the capital is to be kept intact and unimpaired and creditors have

³⁵ Roney v. Crawford, 135 Ga. 1, 68 S. E. 701 (1910).

³⁶ See Reid v. Owensburg Savings Bank and Trust Co., 141 Ky. 444, 132 S. W. 1033 (1911).

³⁷ Cf. Shields v. Hobart, 172 Mo. 491, 72 S. W. 699 (1903).

³⁸ Lexington Life, Fire and Marine Ins. Co. v. Page & Richardson, 17 Mon. 412 (Ky. 1856) (directors considered premiums on unexpired risks as profits failing to realize that many of these might result in losses); Anglo-American Land, Mortgage & Agency Co., Ltd. v. Lombard, 132 Fed. 721 (C. C. A. 8th, 1904) (certain outstanding guarantees had not materialized).

³⁹ Reid v. Eaton Mfg. Co., 40 Ga. 98 (1869).

⁴⁰ Miller v. Bradish, *supra* note 5.

⁴¹ A different construction might be based on the fact that under this statute liabilities included capital stock. Another possible interpretation is that the statute is not exclusive in respect to liabilities of stockholders and that liability might be based on the common law prohibition as to declarations of dividends. See Note (1932) 30 MICH. L. REV. 1070, 1074.

a right to rely upon this policy of the law in their dealings with corporations. The argument of respondent, if admitted⁴² would manifestly put a premium on fraud, as then the entire net assets of a corporation, including capital paid in, over and above its actual debts and liabilities at any one time, could be secretly withdrawn by its stockholders in the form of dividends, thus forcing its creditors to bear all the risk of insolvency arising from any slight business loss or shrinkage of assets."⁴³

Similarly,

"The purpose of such legislation undoubtedly was to render it reasonably safe as far as practicable, to extend credit to corporations. With that view two conditions precedent to their right to declare dividends were created: first, payment into the corporation of its authorized capital; second, solvency so apparent as to leave directors no reasonable ground to believe the situation to be otherwise."⁴⁴

Yet the proper perspective of this problem cannot be maintained by a consideration of creditors exclusively. It must be remembered that the shareholders are not only the contributors to the large funds which form the basis of the corporate structure, but are also innocent parties where the payment of dividends, as well as the corporate activity in general, is concerned. Participation in the corporate form of business is induced by the prospect of receiving a return on the investment. The United States Supreme Court⁴⁵ has expressly said that a part of the course of business of a corporation is the declaration and payment of dividends. Therefore, if shareholders are to be confronted with liability for receiving the very incentive to their becoming members of the corporation, the result is quite obvious: the creation of corporate ventures would become increasingly difficult due to the scarcity of available funds.

Further, to encumber the ordinary layman with the duty of analyzing a balance sheet or of employing accountants to explain to him the significance of the financial statement would be an undue burden for which the compensation would be inadequate.⁴⁶ A recent case takes cognizance⁴⁷ of this peculiar position of the shareholders who are supposed to be owners of the enterprise, yet under present normal conditions are "in no better position to know the condition of the company than the creditors."

Some jurisdictions have attempted to solve the problem through legislation,⁴⁸ and various laws have been passed defining the extent of liability. One type of statute states that there is liability under any circumstances, so long as the shareholder has received a dividend paid out of funds other than profit or surplus.⁴⁹ On the other hand, there is a statute which adds the word "knowingly",

⁴² The argument was that the payment of the dividends did not render the corporation insolvent.

⁴³ Cottrell v. Albany Card & Paper Mfg. Co., *supra* note 16, at 152, 126 N. Y. Supp. at 1073.

⁴⁴ Williams v. Brewster, 117 Wis. 370, 385, 93 N. W. 479, 484 (1903).

⁴⁵ McDonald v. Williams, *supra* note 4.

⁴⁶ "Any other rule would greatly impair the transfer and ownership of stock, for if it were necessary for every person receiving dividends on stock to make an expert investigation of the books of the company to determine that the dividend proffered to him came from net profits it would be impossible to have stock move freely in the markets." Gaunce v. Shoder, 145 Wash. 604, 611, 261 Pac. 393, 395 (1927).

⁴⁷ Bartlett v. Smith, *supra* note 5. The dissenting opinion would limit recovery to cases where payment of the dividend affects the rights of creditors.

⁴⁸ An early Maine statute permitted a judgment creditor a bill in equity to reach dividends improperly paid. See ME. REV. ST. (1857) c. 46, § 80.

⁴⁹ R. I. GEN. LAWS (1923) c. 248, § 38. In the West Virginia act the stockholder is liable not only to the creditors but also to the directors who have incurred loss through pay-

thus making good faith the element upon which the outcome of the litigation turns.⁵⁰ In some statutes,⁵¹ the shareholder's liability is determined by the liability and financial status of the directors, and exists only when (1) the director is not liable or (2), even though the director is liable, the corporation is unable to satisfy a judgment against him. This is interesting when contrasted with cases which expressly say that the liability of a director in no way absolves the shareholder from any responsibility.⁵² Finally, there are certain statutes which define the general liabilities of the shareholder but fail to mention his status in regard to the receipt of improper dividends. Some statutes⁵³ leave the question open to judicial interpretation while others⁵⁴ specifically state that the liability shall be incurred *only* in the instances enunciated.

The solution of the problem as presented in these enactments does not, in any one of them, recognize the merits of the respective positions of the creditors and shareholders. Some favor the creditors and others favor the shareholders, but the necessity of adequately satisfying both groups has unfortunately been overlooked. Some will say that the statutory liability of directors should satisfactorily adjust the equities of the situation. True enough that it is not only logical but also equitable to force the director to suffer the loss since he is the party who initiated the unfortunate occurrences. But the problem is unsolved as long as there remains the possibility of the director being judgment-proof. There seems to be but one answer, the step which invariably results when a loss is to be protected against: a form of insurance. It would be advisable to have statutory regulation compelling the bonding of directors in respect to improperly declared dividends. This would assure shareholders that the dividends which they receive will not be subject to confiscation and at the same time afford creditors a comfortable margin of protection.

E. H. F.

FURTHER DISCUSSION OF THE EVIDENTIARY VALUE OF FINGERPRINTS¹—
With reference to a recent Note in the *University of Pennsylvania Law Review*² on the evidentiary value of fingerprints, it appears there has been some misappre-

ment to the creditors for the wrongful declaration. W. VA. CODE ANN. (Barnes, 1923) c. 31, Art. 1, p. 78. The Michigan statute declares the stockholder liable to any creditor for the amount of capital stock refunded to him. MICH. COMP. LAWS (1929) § 10018. This displaces a former statute which limited the liability of the stockholder to the corporation. Mich. Laws, 1903, Act 232, § 21. See also VT. GEN. LAWS (1917) § 4940, and WIS. STAT. (1929) § 182.19. The present Maine statute still requires a judgment against the corporation as a condition precedent to recovery against the stockholders. ME. REV. STAT. (1930) c. 56, § 102.

⁵⁰ CAL. CIV. CODE (Deering, 1931) § 364. The Ohio statute in addition to making bad faith a condition precedent, limits the liability "to the corporation." OHIO GEN. CODE (Page, 1931) § 8623-123 b. Whether a creditor may maintain an action under this statute is doubtful.

⁵¹ Idaho Laws 1929, c. 262, p. 561. The Louisiana statute is identical except the liability of the director to the creditor is substituted for his liability to the corporation. La. Laws 1928, Act 250, p. 27.

⁵² Powers v. Heggie, *supra* note 29. The converse is also true, *i. e.*, that a stockholder does not have to be sued before liability of director is fixed. See Quintal v. Greenstein, 142 Misc. 854 (N. Y. 1932).

⁵³ MINN. STAT. (Mason, 1927) § 7465.

⁵⁴ S. D. COMP. LAWS (1929) § 8779.

¹ This Note represents a communication received from the Captain of the Detective Bureau of the Police Department of Berkeley, California. Written as a comment on a Note appearing in this REVIEW, it ably represents the practical side of the problem as viewed by an active enforcement official who has given the matter scientific and critical examination.—Ed.

² Note (1932) 80 U. OF PA. L. REV. 887.

hension regarding the opinion of identification men with reference to the forgeability of fingerprints. Webster defines forgery as a false imitation of something which if genuine would import legal efficacy. Shorn of its legal aspect, then, a forgery implies merely a false imitation, on which basis anything susceptible of false imitation may be forged.

Most identification specialists know something about photography, and with such knowledge it must have been realized that replicas could be made of fingerprints, as well as of any other physical object. Some of us, however, did not believe that fingerprints could be so perfectly imitated that the forged print could not be distinguished from the genuine. We had in mind the fact that a genuine fingerprint is an impression from the living skin made with a natural secretion of the living tissue, and that the impression carries over a certain life-like appearance which would be difficult to simulate.

Long before Carlson or Wehde made their great discoveries, some of us had experimented with fingerprint forgeries. We utilized a collotype photographic emulsion, by means of which an ink impression may be photographed and the ridges made to stand up a trifle on the plate or film. By oiling the ridges lightly, a forged impression could be placed wherever desired. These were easily distinguished from genuine impressions.

Later we learned that a genuine latent (invisible) impression could be picked up bodily and transplanted, but we were not informed as to the nature of the medium used for this purpose. A little experimentation revealed a suitable transfer material, surprisingly simple. This looked formidable at first, but on examining the transferred impressions microscopically it was discovered that they differed in two aspects from the genuine. First, the oil particles in the form of ellipsoids in the original were found to be divided into very minute spheroids in the transplant; and second, the relative width of ridge and interspace (normally approximately even) was unnatural due to the flattening and consequent widening of the ridge. Other distinguishing features were noted.

Fingerprint "lifters" soon came into general use to supplant the camera where photography was difficult on account of inaccessibility of the latent. By means of a lifter, the impression after being developed with powder, is picked up by a slightly sticky material (transparent), and taken to the dark-room, where as many photographic prints as needed are made by using the lifter as a negative. This is a type of transfer forgery, inasmuch as the impression itself is picked up, but its evidentiary value has never been questioned by the courts.

Now comes Wehde, who describes an etching process for making a negative in metal, from which a positive may be made with material approximating the texture of the skin. So far as the negative is concerned, there was nothing new or startling in that, since fingerprint circulars bearing printed facsimilies had been in use some time before his so-called discovery. However, theretofore no one seems to have thought of making skin-like positives in this manner, possibly because those most interested in fingerprints were too busy identifying recidivists and sending criminals to jail on honest fingerprint evidence, or perhaps because they lacked the incentive or training for such technical research. Be that as it may, the fact remains that Wehde broadcast his discovery to the world in 1924, and in spite of it the courts are still admitting this type of circumstantial evidence and will continue to do so.

While the problem of planting forged fingerprints at the site of crime is probably not quite so simple as Wehde implies, we have no doubt that in practice it could be done so skilfully as to escape detection and permit the forgeries to pass for genuine. But fabricated evidence is usually badly overdone, and the plotter would need to guard against stamping his forged impressions around too generously. Again, the matter of position of the impressions would require some consideration, as the thief uses his fingers mostly for picking things up

(perhaps more so than honest people). So instead of just simply a stray impression here and there, the prints should be so placed as to simulate the picking up of a jewel box, say, or lifting the lid; or manipulating the combination of a safe; or pulling a piece of broken glass from the window through which entry was made. To accomplish this, one would require stamps for at least two fingers, preferably three—the thumb, index and middle fingers. One would need to have in mind, also, that in grasping some objects the thumb does not register exactly opposite the index and middle fingers; that it does not always lie flat on the object so as to register the complete pattern; and that sometimes the index and middle fingers are impressed in exact juxtaposition and at other times with the middle extended beyond the index, depending upon whether the object is round or flat and upon other factors.

Another small difficulty likely to be overlooked is the matter of sweat pores. In their physiological functioning the mouths of these pores are sometimes open, sometimes closed. This means that in successive impressions of healthy skin different pores may be open and active one moment and closed the next, whereas in stamped impressions there will be no such change. The resulting "fixed" expression of the forged prints might well serve to distinguish them as such.

However, these are small matters, and as stated above, in practice, where original impressions are often not available for comparison, the planted forgery may pass muster, especially if its authenticity is unchallenged. This brings to mind the fact that in our twenty-six years' experience, in which many convictions have been secured largely on fingerprint evidence, not a single case has been encountered in which the possibility of forgery was advanced as a defense.

To return to the *Review* commentator. He mentions fingerprints accidentally left at the site of crime by persons having legitimate business there, and concludes—"When considered from this viewpoint, the value of such fingerprint evidence appears to be slight."³ His reasoning is sound in theory but not quite so compelling in practice, for he considers only the element of time in connection with the question of legitimacy of fingerprints found in public or other places to which the owner of the prints had innocent access. He contends that since it is impossible to establish the time when the impression was made, it cannot be proved thereby that the person was present at the time the crime was committed, since the impression could have been made before or after the crime. Why not consider also the location and position of the impression?

Smith runs a jewelry store which is visited by hundreds of people daily. Smith's fingerprints, or those of his trusted employees on the safe would have no significance after it is burglarized, but what of the casual customers? The customer's fingerprints on Smith's showcase might be innocent enough, but not on a number of empty jewel trays after the store has been burglarized, or on the glass broken out of the window in effecting entrance.

Our commentator mentions *McGarvy v. State*⁴ and *Garcia v. State*⁵ in which the courts ruled against fingerprints on glass because the buildings which had been burglarized were public places and the glass was exposed to the public. It would be interesting to know whether the judges were cognizant of the significance of fingerprints on broken glass. For illustration, it is highly improbable, not to say impossible, for an imprint of the index finger to appear on one side of a piece of glass and the thumb on the other side except *after* the glass is broken or removed from the door or window. Innocent fingerprints made in opening a door or raising a window are easily distinguished by their manner of implantation from those made on glass broken or removed from door or window.

³ *Id.* at 890.

⁴ 82 Tex. Crim. 597, 200 S. W. 527 (1918).

⁵ 26 Ariz. 597, 229 Pac. 103 (1924).

Fingerprints are not conclusive proof of guilt in any case, nor of the presence of their owner at the scene of crime. But just what type of evidence, unsupported by other corroborative evidence, is absolutely conclusive? The testimony of eye witnesses is ordinarily given the greatest credence. Yet who has not experienced cases of mistaken identity or erroneous conception of events transpiring under his very eyes? Again, psychological tests show that no two persons in a considerable group will perceive and describe a series of events in the same manner, though all have viewed the happenings at the same time and under the same conditions.

Are we therefore to view with suspicion even the testimony of eye witnesses, haunted by the fear that somehow, some time, someone may be convicted of a crime he did not commit? It is submitted that the basic idea underlying penal law is the protection of society, that the interests of society are paramount as against those of the individual, and that if an occasional individual's liberty or even his life is sacrificed in war or in peace for the welfare of his state or country, or of society, the sacrifice is not in vain.

C. D. Lee.