10-1978

Burks v. Lasker

Lewis F. Powell Jr.

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PRELIMINARY MEMORANDUM

Summer List 13, Sheet 2

No. 77-1724-CFX

BURKS, et al. (a mutual fund, a majority of its directors, and its investment adviser)

Cert. to CA 2 (Lumbard, Oakes and Meskill)

v.

LASKER (mutual fund stockholder)

Federal/Civil

Timely

SUMMARY: Petrs challenge the CA's holding that the determination by a quorum of a mutual fund's board of directors, comprising a disinterested minority of all the directors, that assertion of a legal claim on behalf of the fund would not be in the fund's best interest, cannot prevent stockholders from asserting that claim by way of a derivative action.

FACTS AND DECISIONS BELOW: Petrs are 1) an opened-ended diversified investment company, incorporated in Delaware and registered under the Investment Company Act of 1940 (a nominal defendant), 2) its investment adviser, and 3) former and present directors of the company who either were directors in late 1969 or are affiliated with the investment advister. Resps are two owners of shares in the investment company. In November and December of 1969, the investment company purchased $20 million worth of Penn Central commerical paper from Goldman, Sachs & Co. In January, 1970 Penn Central filed for reorganization, and accordingly the commercial paper was not paid at maturity. In settlement of an action by the investment company against Goldman, Sachs, the paper was returned to Goldman, Sachs in return for $5.25 million and an assignment of 73.75% of whatever dividend is eventually paid on paper in the reorganization.

60 days later

Resps brought this action as a derivative action under the Investment Company Act, the Investment Advisers Act, and state contract and corporation law, for damages to the investment company resulting from the sale and retention ~~of~~ the paper. The investment company's board ~~that~~ resolved five directors (a minority of the whole board) who were (1) not affiliated with the investment adviser, (2) had not been directors at the time of the events giving rise to the claim and (3) were not defendants in this action should act as a quorum of the board to determine what position the fund should take regarding the suit. The five "independent directors" retained Stanley Fuld, formerly Chief Judge of the New York Court of Appeals and not related to any party to this action, as special counsel. After a lengthy investigation, Judge Fuld submitted a report stating, inter alia,

independent directors

sp. counsel, thought Δs would successfully defend the suit

that, despite some uncertainties, it was likely that defendants would prevail in this case.

After a number of meetings, lengthy questioning of Judge Fuld, and request for and submission of a supplemental report by Judge Fuld, the five directors determined that prosecution of the action would not be in the best interest of the company, and that the corproation would not prosecute the claims. Petr thereupon moved to dismiss the complaint.

District Judge Werker initially held that the determination by a disinterested quorum of the board of directors not to prosecute the action required dismissal of the complaint. He denied the motion without prejudice, however, to afford resps an opportunity for discovery aimed at uncovering evidence that the five directors were not, in fact, disinterested. After discovery, the motion was renewed. Judge Werker found that resps offered no evidence impugning the directors' disinterestedness, and granted the motion.

DC dismissed

to dismiss

The CA reversed. Judge Lumbard stated that the appeal "raise[d] an important question of first impression: Can minority directors of a registered mutual fund, who were nominated by the majority directors of the fund to be "independent" directors pursuant to the requirementsof the Investment Company Act . . . terminate a non-frivolous stockholder's derivative action against the fund's majority directors and its investment adviser?" The CA held not, even though the court had "no doubt that the five minority directors acted in good faith in all they did."

CA reversed

The CA expressly rejected as immaterial cases dealing with the power of directors of other sorts of corporations to terminate derivative suits, or with the effect of the Fed. R. Civ. P. 23.1 demand requirement. Instead, it based its decision "on the unique nature of the investment company and its symbiotic relationship with its investment adviser." In particular, Judge Lumbard noted that the enactment of the Investment Company Act was motivated in part by the belief that investment companies tended to be dominated by their investment advisers. He emphasized the addition of § 36(b) of the Act, in 1970, which authorizes shareholders to sue derivatively to recover excessive fees paid by the investment company to the adviser and the principal underwriter, and found it anomolous that mutual fund directors should be able to terminate other actions.

On the basis of observations concerning, e.g., the day-to-day working relationship between interested and disinterested directors, he concluded, "It is asking too much of human nature to expect that the disinterested directors will view with the necessary objectivity the actions of their colleagues in a situation where an adverse decision would be likely to result in considerable expense and liability for the individuals concerned."

good deal of truth to this

CONTENTIONS: Petrs assert that the traditional rule for companies in general has been that, absent fraud, corruption or the like, the directors' determination in the exercise of their business judgment not to prosecute a claim bars a derivative action. They note that with respect to this and most other cases, no provision of the Investment Company Act is to the contrary. They contend that the CA erred in creating a novel, federal rule regarding investment companies, because in general the powers and duties of coporation directors are to be determined by the law of the state of incorporation, citing, e.g., Santa Fe Industries, Inc. v. Green, 430 U.S. 462 (1977).

Petrs also assert that the CA's decision conflicts with In re Kaufman Mutual Fund Actions, 479 F.2d 257 (1st Cir.), cert. denied, 414 U.S. 857 (1973). That case held that the demand requirement of Fed. R. Civ. P. 23.1 was not excused, in a derivative action on behalf of a mutual fund, by the fact that some of the directors were interested. Language in that opinion stated that mutual funds were to be treated no differently than other corporations under Rule 23.1. Finally, they contend that the narrow application of the new § 36(a), together with the legislative history of that provision, shows that Congress did not intend to abrogate the usual power of directors to terminate . derivative actions in most cases involving mutual funds. CA 1

The Investment Company Institute and Investors Diversified Services, Inc. have filed briefs as amici curiae in support of the petition for certiorari. Both stress the disruptive potential of the CA's decision on the investment company industry, by way of an increased number of derivative actions. The Institute also makes the argument that the CA decision conflicts with the policy of the Investment Company Act, of ensuring the existence of, and giving special powers to, the independent directors for the purpose of protecting the shareholders. It further contends that disinterested directors, elected by the stockholders, are far more likely to act in the interest of stockholders as a whole than individual stockholder plaintiffs.

Resp replies that no corporate directors may ever terminate derivative actions after they proceed beyond the threshold issue of demand. They further asserts that neither Delaware law nor the decisions of this Court relied on by petrs authorize a minority of the board/ to block a derivative action against a majority of the boar Resps distinguish this Court's decisions, cited by petrs, concerning preservation of the states' authority regarding corporate governance on the ground that they concerned the existence of private rights of action under federal statutes. Finally, resp denies that the CA's decision conflicts with the CA 1 decision in Kaufman Mutual Fund on the ground that in that case a majority of directors were disinterested.

DISCUSSION: It is my impression, based on very brief research, that petrs are correct about the authority of directors to terminate derivative actions under Delaware law. Certainly there seems little basis for resps' distinction between a minority and a majority of distinterested directors: so long as the decision is made by a distinterested quorum, every vote which counts toward determining the company's action is disinterested.

The actual rule of Delaware law, however, is beside the point. The issue proposed for review is whether the CA acted properly in ignoring Delaware law altogether, and formulating a federal rule concerning the powers of investment company directors. Santa Fe Industries v. Green, in which this Court held that SEC Rule 10b-5 does not afford a basis for a federal common law concerning the substantive responsibilities of directors in th management of companies, is contrary in spirit to the CA's decision to adopt a federal rule.

Even if a federal rule should be devised regarding mutual fund directors, the CA's holding that such directors may never terminate a derivative action is unfortunate. The holding shifts the decision as to whether to prosecute a claim from directors to individual stockholders. Whereas the director is likely to be sufficiently familiar with the company's affairs so as to be able to decide what course is in the company's best interest, the stockholder is not. Whereas the director is under a legal duty to act in the best interests of the company as a whole (without regard for the questionable impact of the fact that he is elected), the stockholder is not. Finally, the stockholder's decision is likely to be made by a lawyer. Lawyers are not disinterested with respect to whether to prosecute a claim or not: they are economically motivated to litigate.

The briefs of two amici in support of the petition indicate the importance which the mutual fund industry attaches to this case. Like anyone who manages other people's money, investment advisers are susceptible of incurring liabilities which are huge relative to their own assets. An investment company cannot expect aggressive management from its investment adviser unless it has the power to forego asserting plausible claims against it.

I am personally familiar with the uproar this case has produced in the New York City bar. With that caveat regarding my own disinterestedness, I recommend certiorari be granted.

There is a response.

8/10/78 Lacy Opn in petn
WS

BB

Fed statutes, there is arguable conflict, & a CA2 decision on this type issue is imp.

Independent directors of an Investment Company, constituting a quorum of entire Board & who were not parties defendants in a derivative suit, decided that a suit on behalf of the Company (by means of a derivative action) would not be in best interest of Co & shareholders. The DC thereupon dismissed a derivative suit brought by shareholders. CA2 reversed, holding as matter of fed. law that under Investment Co Act & Investment Advisors Act, independent directors have no such authority.

SUPPLEMENTAL MEMORANDUM

Summer List 13, Sheet 2

No. 77-1724

BURKS

v.

LASKER

Cert to CA 2 (Lumbard, Oakes, and Meskill)

Federal/Civil

Timely

CA2 did not expressly consider whether State law (Delaware) was preempted even though the fed acts are silent on this Q

This case presents the important problem of the authority of the independent directors of a registered investment company, constituting a minority but a quorum of the board of directors, to terminate a derivative action naming the interested directors as defendants. The case presents two questions for review.

1. Should the authority of the independent directors be governed by state or federal law? No provision of the Investment Company Act or the Investment Advisers Act explicitly governs the situation. The DC did not even linger over the question of the existence of the authority, and so never inquired about the source of authority. The CA 2 assumed rather than held that federal law should apply, and spent its efforts addressing the second question, *infra*. *Santa Fe Industries v. Green*, 430 U.S. 462 (1977), is implicated. ask counsel

2. If federal law governs, did the CA 2 correctly determine that the statutorily independent directors do not have the authority to terminate shareholder derivative suits against the interested directors of the investment company?

Because of the way they approached the first issue, neither the DC nor the CA 2 discussed or determined what authority the relevant state law (Del. Corp. Law) gave to the disinterested minority directors in this situation. But if state and federal law accord minority directors the same amount of authority in this kind of situation, then I think the case could be decided without reaching Question 1 *supra*.

I recommend discussing this case with a view to granting the petition.

Bruce

8/17/78

Argued ...., 19... Assigned ...., 19... No 77-1724
Submitted ...., 19... Announced ...., 19...

BURKS

vs.

LASKER

(who put this on list)
Byron says
the issue should
be ruled by state
rather than fed. law.
Here CA2 created fed
com. law. I'm inclined
to agree with Byron.
John thinks decision
is wrong but be denied
because no conflict.

Granted

	HOLD FOR	CERT.		JURISDICTIONAL STATEMENT				MERITS		MOTION		ABSENT	NOT VOTING
		G	D	N	POST	DIS	AFF	REV	AFF	G	D		
Burger, Ch. J.			✓										
Brennan, J.			✓										
Stewart, J.		✓											
White, J.				Join 3									
Marshall, J.			✓										
Blackmun, J.		Ask SG or Grant											
Powell, J.		✓											
Rehnquist, J.		✓											
Stevens, J.			✓										

77-1724 BURKS v. LASKER Argued 1/17/79

application of "business judg. rule" to independent members of Bd. of a mutual fund.

Pollock (Petrs)

Penn Central Commercial Paper was rated "Prime" at time of purchase.

Three yrs after purchase two of 90,000 shareholders filed their suit.

Independent directors made careful investigation in addition to opinion of J Fulda

§141a of Del. Law - directors empowered to manage affairs of corps. This power has been held to include right to determine whether to sue.*

This is primarily a matter of State law, but recognize that policies of Investment Co Act. are relevant - to extent it preempts. But doesn't think Investment Co Act policies ~~[illegible]~~ are inconsistent with Del law

DC found as fact that independent directors were independent.

§144(a)(1) Del. code - majority of independent directors may act. (See Green Brief. 16)

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* United Copper Securities case, 244 U.S. 261

Pollack (cont)

SEC says judg. of independent directors must be "reasonable". Pollack's argues

Quest. ~~was~~ raised ~~by~~ Rep. as to "minority" as contrary to Del law.

Also By-laws of this corp. allow a minority to be a quorum

~~[illegible]~~

Ferrara (G/Counsel for SEC)

See my notes on SG's Brief.

§ 36 a - imposing fiduciary standards of independent directors implies obligation that they act reasonable

(Stewart & Stevens emphasized this was private rt. of action - not under Inv. Co. Act)

J White pressed Ferrara ~~[illegible]~~ as to where in Act any fed, authority to tell Bd of Directors when to settle a suit or not bring it.

Ferrara (cont.)
All directors are fiduciaries
- but investment co directors
are "super-directors under 36 a

Einstein (Resp.)
Discovery was too limited -
wanted to discover bases of Judge
Fuld's information.
(no answer filed & no discovery

Agree Del. law allows a
minority to be a quorum

Pollack (Reply)
As to Remand, see Note 21
of SEC Brief inviting us to
"find" reasonableness. If this
Court can make this finding
on this record, then certainly
DC had ~~s~~ sufficient ev to
make this same finding.

Footnote 11 in Santa Fe (10b case)

BOBTAIL BENCH MEMORANDUM

TO: Mr. Justice Powell

FROM: Paul

RE: Burks v. Lasker, No. 77-1724

DATE: January 18, 1979

This case involves the power of independent directors of a mutual fund to terminate a derivative suit brought against the interested directors. The Second Circuit held that unless a district court determines that the derivative action is frivolous, the independent directors are without power to prevent prosecution of the suit. The issue is presented especially sharply, as the court below did not upset the trial court's findings that the independent directors in this case were truly independent and acted in good faith.

The parties' briefs are not especially helpful, but there some good amici briefs. I thought the SEC's brief was useful, perhaps because I agreed with many of its observations. The SEC demonstrates convincingly that the ruling of the court below is hard to maintain, as it holds the independent directors hostage to the whims of a few disgruntled shareholders. Further, if the independent directors are denied all power to terminate a derivative suit, their statutory function as watchdogs is substantially undercut. Respondents' arguments that (1) minority quorums do not have the authority to terminate a derivative suit, and (2) Rule 23.1 supports the result of the Court below, are frivolous, and unless they trouble you I will not deal with them further.

The case appears to present two difficult issues: (1) whether the "fiduciary duty" which § 36(a) of the Investment Company Act imposes on the independent directors can be interpreted to specify a substantive standard by which the decision not to pursue a lawsuit can be evaluated; and (2) if so, what the content of that standard should be. The most directly applicable precedent, Tannenbaum v. Zeller, 552 F.2d 402 (2d Cir. 1977), cert. denied, 434 U.S. 934 (1978), adopted the SEC's position that § 36(a) does require independent directors, in approving the operations of the investment advisor, (1) to be free of undue influence, (2) to receive all the necessary information, and (3) to exercise reasonable business judgment. If state law were to apply, however, the obligation of the independent directors would be limited to not approving a transaction so manifestly injurious to the corporation as to exceed the bounds of business judgment. See Selheimer v. Manganese Corp., 423 Pa. 563, 224 A.2d 634 (1966); Cary, Corporations 513-549.

The proposition that directors have an obligation to exercise reasonable business judgment, apart from their obligation not to act out of self-interst, does not seem controversial. As I learned corporation law, however, the former duty carries with it a strong presumption of regularity on the part of the directors; courts have been exceedingly reluctant to second-guess the disinterested business decisions of informed directors. See Briggs v. Spaulding, 141 U.S. 132, 147 (1891); 3A Fletcher, Cyclopedia of the Law of Corporations § 1029 (1975 ed.) Some decisions, although arrived at in good faith, may be so manifestly wrong as to permit judicial intervention, but in practice there have been few, if any, instances where courts have acted to correct such errors of judgment. The SEC's position, in essence, is that the Investment Company Act requires more of the independent directors. As I understand the SEC's argument, the fiduciary duty imposed by § 36(a) comprises a duty of care more akin to modern concepts of tort law. To achieve the special purposes of the Investment Company Act, the independent directors must not only exercise sound business judgment, but also reach a decision that a hypothetical reasonable director acting in his shoes would have approved. ?

In a formal sense, there is nothing too objectionable about the SEC's position. The federal courts have an obligation to interpret the meaning of "fiduciary duty" as it appears in § 36(a), and nothing on the face of the statute prohibits the courts from reading into that term more than state law traditionally has required. The SEC argues that the structure and policies of the Act support a stricter standard of care.

Strong arguments, however, can be made for the other side. "Fiduciary duty" is a term of art, and it is reasonable for federal courts to refer to the common law in deciding what it means. Such has been the practice with respect to the Sherman Act, among other statutes incorporating common law terms. Furthermore, fairness to those persons who become directors of these funds cuts against a retroactive expansion of their liability. Finally, the policy reasons that support the common law rule apply here-- courts are not in the position to second-guess the business decisions of directors acting in good faith. It would be highly undesirable to require the parties to try the merits of the underlying claim in order to determine whether the directors can terminate the suit, a procedure the SEC position entails. See SEC Brief at 24 n. 20. It should be enough that the directors were fully and accurately informed on the state of the law at the time they decided to terminate the litigation and, in acting on that information, did not exceed the bounds of business judgment.

The district court, as I read its opinion, applied the appropriate state law standard to these facts. See Del. Code. tit. 8, § 144(a)(1):

> "(a) No contract or transaction between a

> corporation and one or more of its directors or officers, or betwen a corporation and any other corporation, partnership, association, or other organization in which one or more of its directors or officers are directors or officers, shall be void or voidable solely for this reason, or solely because the director or officer is present at or participates in the meeting of the board or committee thereof which authorizes the contract or transaction, or solely because his or their votes are counted for such purpose, if:
>
> "(1) The material facts as to his relationship or interest and as to the contract or transaction are disclosed or are known to the board of directors or the committee, and the board or committee in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors, even though the disinterested directors be less than a quorum." (emphasis supplied).

I think the finding of good faith incorporates a determination of reasonable care. Thus this Court could reinstate the district court's judgment of dismissal, rather than remanding the case to the court of appeals. This detail is not as important as how the opinion is written.

One final point should be mentioned. Petitioners have conceded that a private cause of action exists under § 36(a) of the Investment Company Act. As far as I am aware, no decision of this Court has so held, although the authority in the Second Circuit decidedly is in favor of such an action. It is not necessary for purposes of this case to decide whether § 36(a) supplies an action, but it is important for this Court to recognize that the question remains open. It would be unfortunate for the Court to repeat its experience with Rule 10b-5 and slip into the position of accepting an implied cause of action without fully considering the problem.

Reverse 7-1
WHR Out.

77-1724 BURKS v. LASKER Conf. 1/19/79

no reason to remand - as SG suggests - to determine reasonableness. In sum, would apply state law & state standard.

Leg. history of 1940 statutes n... intent to limit auth. of Bd/Dir

The Chief Justice Reverse

Quorum of independent directors exercised reasonable care - engaged J. Fuld, studied his opinion. DC's findings included ~~a statement~~ that directed acted reasonably (?) & in good faith.

CA 2: even if Investment Act qualifies state laws, ~~it need not~~ should not have adopted per se rule. In this case, clear that ~~directors acted reasonably~~

Mr. Justice Brennan Reverse

Q is extent to which, if at all, Act of '40 limits state law. If state law governs, this case must be reversed.

There is nothing explicit in Fed Act, & so we would have to infer intent to qualify state law.

Cort v Ash standard not met

Mr. Justice Stewart Reverse

CA 2 clearly wrong. SEC argues that altho CA 2 went too far, Act of 40 does impose obligation of Fed Cts to review reasonableness. SEC also wrong.

Mr. Justice White Reverse

Agrees with CJ, WJB & P.S.
Santa Fe is persuasive.
State law applies
SEC argument not persuasive

Mr. Justice Marshall Affirm

Agrees these are "super-directors" & have higher degree of duty

Mr. Justice Blackmun Reverse

CA2's action clearly inconsistent with leg. hist of 40 Act.
Del. law controls.

Even under SEC's analysis would Reverse.

Mr. Justice Powell Reverse

DC's findings that legal quorum of of independent directors acted in good faith, were ~~not~~ accepted by CA2

Q is whether state law - business judgment rule - is qualified by 1940 Act. I agree with P.S. that CA2 & SEC are both wrong.

~~Hard not~~

Mr. Justice Rehnquist

Out

Mr. Justice Stevens Reverse

& remand for CA or DC to determine that law. But I'm not happy with his grudging approach to authority of the disinterested Board members.

Potter may write. (He will let me know.

4/23

To: The Chief Justice
Mr. Justice Stewart
Mr. Justice White
Mr. Justice Marshall
Mr. Justice Blackmun
Mr. Justice Powell
Mr. Justice Rehnquist
Mr. Justice Stevens

From: Mr. Justice Brennan

Circulated: 18 APR 1979

Recirculated: ________

1st DRAFT

SUPREME COURT OF THE UNITED STATES

No. 77-1724

Harry G. Burks, Jr., et al., Petitioners, v. Howard M. Lasker et al.	On Writ of Certiorari to the United States Court of Appeals for the Second Circuit.

[April —, 1979]

MR. JUSTICE BRENNAN delivered the opinion of the Court.

The question presented in this case is whether the disinterested directors of an investment company may terminate a stockholders' derivative suit brought against other directors under the Investment Company and Investment Advisers Acts, 15 U. S. C. § 80a-1 *et seq.*; 15 U. S. C. § 80b-1 *et seq.* To decide that question, we must determine the appropriate roles of federal and state law in such a controversy.

Respondents, shareholders of Fundamental Investors, Inc., an investment company registered under the Investment Company Act, brought this derivative suit in February 1973 in the District Court for the Southern District of New York. The action was brought against several members of the company's board of directors and its registered investment advisor, Anchor Corporation. The complaint alleged that the defendants had violated their duties under the Investment Company Act (ICA),[1] the Investment Advisers Act (IAA),[2] and the common law in connection with the 1969 purchase by the corporation of $20 million in Penn Central Transportation Company

[1] § 13 (a)(3), 15 U. S. C. § 80a-13 (a)(3), and former § 36, 15 U. S. C. § 80a-35 (1964 ed.), 54 Stat. 841.

[2] § 206, 15 U. S. C. § 80b-6.

commercial paper.[3] In response to the suit, Fundamental's board of directors determined that the five of its members who were neither affiliated with the investment advisor[4] nor defendants in the action would decide what position the company should take in the case. On the basis of outside counsel's recommendation and their own investigation, the five, acting as a quorum pursuant to the company's bylaws, concluded that continuation of the litigation was contrary to the best interests of the company and its shareholders and moved the District Court to dismiss the action.

The District Court held that under the so-called "business judgment rule," a quorum of truly disinterested and independent directors has authority to terminate a derivative suit

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[3] The complaint alleged, *inter alia*,

"that Anchor breached its statutory, contractual and common law fiduciary duties by relying exclusively upon the representations of Goldman, Sachs & Co. (a seller of commercial paper), rather than independently investigating the quality and safety of the Penn Central 270-day notes purchased by the Fund. It is further alleged that the defendant directors knew or should have known of Anchor's failure to meet its responsibility; that they violated their . . . duties by acquiescing in Anchor's omissions; that the financial condition of the Penn Central steadily worsened during the period from November 28, 1969 to June 21, 1970, the date that it filed for reorganization; and that during this period of decline all of the defendants failed to investigate and review the financial condition of the Penn Central and the quality and safety of its commercial paper." *Lasker* v. *Burks*, 426 F. Supp. 844, 847 (SDNY 1977).

[4] The five were "disinterested" within the meaning of the Investment Company Act, see *Lasker* v. *Burks*, 567 F. 2d 1208, 1209 (CA2 1978), which provides that

"No registered investment company shall have a board of directors more than 60 per centum of the members of which are persons who are interested persons of such registered company." 15 U. S. C. § 80a-10 (a).

The definition of "interested person" is found at 15 U. S. C. § 80a-2 (a) (19). See n. 12, *infra*.

Of the remaining six directors, five were defendants in the *Lasker* suit, and one was a director of the investment adviser. *Lasker* v. *Burks*, 404 F. Supp. 1172, 1175 (SDNY 1975).

which they in good faith conclude is contrary to the company's best interests. 404 F. Supp. 1172 (SDNY 1975). After permitting discovery on the question of the directors' independence, the District Court entered summary judgment against respondents, finding no evidence that the directors who voted to terminate the suit had acted other than independently and in good faith. 426 F. Supp. 844 (SDNY 1977). The Court of Appeals for the Second Circuit reversed, 567 F. 2d 1208, 1212 (CA2 1978), holding that as a consequence of the Investment Company Act, "disinterested directors of an investment company do not have the power to foreclose the continuation of nonfrivolous litigation brought by shareholders against majority directors for breach of their fiduciary duties." We granted certiorari, — U. S. — (1978). We reverse.

I

The first step in determining whether state or federal law governs this case is to ascertain what law creates the cause of action alleged by the plaintiffs. Neither the Investment Company Act nor the Investment Advisers Act—the plaintiffs' two federal claims—expressly creates a private cause of action for violation of the sections relevant here. However, on the basis of District and Circuit precedent, the courts below assumed that an implied private right of action existed under each Act. *Brown* v. *Bullock*, 194 F. Supp. 207, 222–228 (SDNY), aff'd, 294 F. 2d 415 (CA2 1961) (en banc) (ICA); *Abrahamson* v. *Fleschner*, 568 F. 2d 862 (CA2 1977) (IAA); *Bolger* v. *Laventhol, Krekstein, Horwath & Horwath*, 381 F. Supp. 260 (SDNY 1974) (IAA). The two courts also sanctioned the bringing of the suit in derivative form, apparently assuming that, as we held in *J. I. Case Co.* v. *Borak*, 377 U. S. 426, 432 (1964), "[t]o hold that derivative actions are not within the sweep of the [right] would . . . be tantamount to a denial of private relief." As petitioners never disputed the existence of private, derivative causes of action under the

Acts, and as in this Court all agree that the question has not been put in issue, Brief for Petitioners 28; Brief for Respondents 15, we shall assume without deciding that respondents have implied, derivative causes of action under the Investment Company and Investment Advisers Acts.[5]

Since we proceed on the premise of the existence of a federal cause of action, it is clear that "our decision is not controlled by *Erie R. Co.* v. *Tompkins,* 304 U. S. 64," and state law does not operate of its own force. *Sola Electric Co.* v. *Jefferson Co.,* 317 U. S. 173, 176 (1942). See *Board of Commissioners* v. *United States,* 308 U. S. 343, 349–350 (1939); *Deitrick* v. *Greaney,* 309 U. S. 190, 200 (1940); C. Wright, Federal Courts 284 (3d ed.); Mishkin, The Variousness of "Federal Law," 105 U. Pa. L. Rev. 797, 799–800 (1957); Hart, The Relations Between State and Federal Law, 54 Colum. L. Rev. 489, 529 (1954); 2 L. Loss, Securities Regulation 971 (2d ed.). Rather, "[w]hen a federal statute condemns an act as unlawful, the extent and nature of the legal consequences of the condemnation, though left by the statute to judicial determination, are nevertheless federal questions, the answers to which are to be derived from the statute and the federal

[5] The question whether a cause of action exists is not a question of jurisdiction, and therefore may be assumed without being decided. Cf. *Mt. Healthy City Board of Ed.* v. *Doyle,* 429 U. S. 274, 279 (1977); *Bell* v. *Hood,* 327 U. S. 678, 682 (1946). Other Courts of Appeals have agreed with the Second Circuit that the Investment Company and Investment Advisers Acts create private causes of action. As to the Investment Company Act, see *Moses* v. *Burgin,* 445 F. 2d 369, 373 (CA1 1971); *Esplin* v. *Hirschi,* 402 F. 2d 94, 103 (CA10 1968). See also *Herpich* v. *Wallace,* 430 F. 2d 792, 815 (CA5 1970); *Taussig* v. *Wellington Fund, Inc.,* 313 F. 2d 472, 476 (CA3 1963). Compare *Greater Iowa Corp.* v. *McLendon,* 378 F. 2d 783, 793 (CA8 1967), with *Brouk* v. *Managed Funds, Inc.,* 286 F. 2d 901 (CA8 1961), vacated as moot, 369 U. S. 424 (1962). As to the Investment Advisers Act, see *Lewis* v. *Transamerica Corp.,* 575 F. 2d 237 (CA9 1978), cert. granted, No. 77–1645, — U. S. — (1978); *Wilson* v. *First Houston Investment Corp.,* 566 F. 2d 1235 (CA5, 1978), cert. granted, No. 77—, — U. S. — (1978).

policy which it has adopted." *Sola Electric Co.* v. *Jefferson Co.*, 317 U. S., at 176. See *Tunstall* v. *Brotherhood of Locomotive Firemen & Enginemen*, 323 U. S. 210, 213 (1944); *Board of Commissioners* v. *United States*, *supra*. Cf. *United States* v. *Kimbell Foods, Inc.*, No. 77-1359, at 9–10, — U. S. —, — (1979); *Butner* v. *United States*, — U. S. — (1979). Legal rules which impact significantly upon the effectuation of federal rights must, therefore, be treated as raising federal questions. See *Robertson* v. *Wegmann*, 436 U. S. 584, 588 (1978) (statute of limitations); *Auto Workers* v. *Hoosier Corp.*, 383 U. S. 696, 701 (1966) (same); *J. I. Case Co.* v. *Borak*, 377 U. S., at 435 (security for expense statute); *Sola Electric Co.* v. *Jefferson Co.*, 317 U. S., at 176 (rules of estoppel); *Dietrick* v. *Greaney*, 309 U. S., at 200 (affirmative defense to federal claim). See generally Friendly, In Praise of *Erie*—and of the New Federal Common Law, 39 N. Y. U. L. Rev. 383, 408 (1964); Hill, State Procedural Law in Federal Nondiversity Litigation, 69 Harv. L. Rev. 66, 92–93 (1955). Thus, "the overriding federal law applicable here would, *where the facts required*, control the appropriateness of redress despite the provisions of state corporation law . . . ." *J. I. Case Co.* v. *Borak*, 377 U. S., at 434 (emphasis added).

II

The fact that "the scope of [respondents'] federal right is, of course, a federal question" does not, however, make state law irrelevant. *De Sylva* v. *Ballentine*, 351 U. S. 570, 580 (1956). Cf. *United States* v. *Kimbell Foods, Inc.*, No. 77-1359, at 11, — U. S. —, —. It is true that in certain areas we have held that federal statutes authorize the federal courts to fashion a complete body of federal law. See *Textile Workers* v. *Lincoln Mills*, 353 U. S. 448, 451, 456–457 (1957). Corporation law, however, is not such an area.

A derivative suit is brought by shareholders to enforce a claim on behalf of the corporation. See Note, The Demand and Standing Requirements in Stockholder Derivative Actions, 44 U. Chi. L. Rev. 168 (1976). This case involves the question whether directors are authorized to determine that certain claims not be pursued on the corporation's behalf. As we have said in the past, the first place one must look to determine the powers of corporate directors is in the relevant State's corporation law. See *Santa Fe Industries* v. *Green*, 430 U. S. 462, 479 (1977); *Cort* v. *Ash*, 422 U. S. 66, 84 (1975). "Corporations are creatures of state law," *Cort* v. *Ash*, *supra*, and it is state law which is the font of corporate directors' powers. By contrast, federal law in this area is largely regulatory and prohibitory in nature—it often limits the exercise of directorial power, but only rarely creates it. Cf. *Price* v. *Gurney*, 324 U. S. 100, 107 (1945). In short, congressional legislation in this area is generally enacted against the background of existing state law; Congress has never indicated that the entire corpus of state corporation law is to be replaced simply because a plaintiff's cause of action is based upon federal law. *Cort* v. *Ash*, *supra*; *Santa Fe Industries* v. *Green*, *supra*. See *United Copper Co.* v. *Amalgamated Copper Co.*, 244 U. S. 261, 264 (1917). Cf. *United States* v. *Yazell*, 382 U. S. 341, 352–353 (1966) (state family law); *De Sylva* v. *Ballentine*, 351 U. S., at 580 (same); P. Bator, P. Mishkin, D. Shapiro and H. Wechsler, The Federal Courts and The Federal System 470–471 (1973 ed.).

Federal regulation of investment companies and advisers is not fundamentally different in this respect. Mutual funds, like other corporations, are incorporated pursuant to state, not federal law. Although the Court of Appeals found it significant that "nothing in . . . the legislation regulating investment companies and their advisers . . . suggests that . . . disinterested directors . . . have the power to terminate litigation brought by mutual fund stockholders . . . ," 567 F. 2d, at 1210, such silence was to be expected. The Investment Company Act does not purport to be the source of authority for managerial power; rather, the Act functions primarily to "impose[] *controls and restrictions* on the internal management of investment companies." *United States* v. *National Assn. of Securities Dealers*, 422 U. S. 694, 705 n. 13 (1975) (emphasis added).

The Investment Company and Investment Advisers Acts, therefore, do not require that federal law displace state laws governing the powers of directors unless the state laws permit action prohibited by the Acts, or unless "their application would be inconsistent with the federal policy underlying the cause of action." *Johnson* v. *Railway Express Agency*, 421 U. S. 454, 465 (1975).[8] Cf. *Robertson* v. *Wegmann*, 436 U. S., at 590; *Auto Workers* v. *Hoosier Corp.*, 383 U. S., at 706-707; *Sola Electric Co.* v. *Jefferson Co.*, 317 U. S., at 176. Although "[a] state statute cannot be considered 'inconsistent' with federal law merely because the statute causes the plaintiff to lose the litigation," *Robertson* v. *Wegmann, supra*, at 593, federal courts must be ever vigilant to insure that application of state law poses "no significant threat to any identifiable federal policy or interest . . . ." *Wallis* v. *Pan American Petroleum Corp.*, 384 U. S. 63, 68 (1966). See *Auto Workers* v. *Hoosier Corp.*, 383 U. S., at 702. Cf. *Brown* v. *Western R. of Alabama*, 338 U. S. 294, 298 (1949). And, of course, this means that "unreasonable," *Wallis* v. *Pan American Petroleum Corp., supra*, at 70, or "specific

[8] This is not a situation where federal policy requires uniformity, and therefore where the very application of varying state laws would itself be inconsistent with federal interests. In enacting the Investment Company and Investment Advisers Acts, Congress did declare that "the activities of such companies, extending over many States . . . make difficult, if not impossible, effective State regulation of such companies . . . ." 15 U. S. C. § 80a-1 (a)(5). But as long as private causes of action are available in federal courts for violation of the federal statutes, this enforcement problem is obviated. The real concern, therefore, is not that state laws be uniform, but rather that the laws applied in suits brought to enforce federal rights meet the standards necessary to insure that the "prohibition of [the] federal statute . . . not be set at naught," *Sola Electric Co.* v. *Jefferson Co.*, 317 U. S. 173, 176 (1942). The "consistency" requirement described in text guarantees that state laws failing to meet these standards will be precluded.

abberant or hostile state rules," *United States* v. *Little Lake Misere Land Co.*, 412 U. S. 580, 596 (1973), will not be applied. See, *e. g.*, *Levitt* v. *Johnson*, 334 F. 2d 815, 819–820 (CA1 1964). The "consistency" test guarantees that "[n]othing that the state can do will be allowed to destroy the federal right," *Board of Commissioners* v. *United States*, 308 U. S., at 350, and yet relieves federal courts of the necessity to fashion an entire body of federal corporate law out of whole cloth.

III

The foregoing indicates that the threshold inquiry for a federal court in this case should have been to determine whether state law permitted Fundamental's disinterested directors to terminate respondents' suit. If so, the next inquiry should have been whether such a state rule was consistent with the policy of the Investment Company and Advisers Acts. Neither the District Court nor the Court of Appeals decided the first question, apparently because neither considered state law particularly significant in determining the authority of the independent directors to terminate the action.[7] And in that circumstance, neither court addressed the question of inconsistency between state and federal law. At least implicitly, however, the Court of Appeals did make a related determination. Its holding that nonfrivolous derivative suits may never be terminated makes manifest its view that no other rule—whether state or federal—would be consistent with the Investment Company Act.[8] We disagree.

The Court of Appeals correctly noted, 567 F. 2d, at 1210–1211, that Congress was concerned about the potential for abuse inherent in the structure of investment companies. A mutual fund is a pool of assets, consisting primarily of port-

[7] See 567 F. 2d 1208; 404 F. Supp. 1172.

[8] The Court of Appeals did not undertake any separate analysis of the policy behind the Investment Company Act's companion statute, the Investment Advisers Act.

folio securities, and belonging to the individual investors holding shares in the fund. *Tannenbaum* v. *Zeller*, 552 F. 2d 402, 405 (CA2 1977). However, as Congress recognized,

> "Mutual funds, with rare exception, are not operated by their own employees. Most funds are formed, sold, and managed by external organizations, that are separately owned and operated [investment advisers] . . . . The advisers select the funds' investments and operate their businesses. . . . Since a typical fund is organized by its investment adviser which provides it with almost all management services, . . . a mutual fund cannot, as a practical matter sever its relationship with the adviser. Therefore, the forces of arm's-length bargaining do not work in the mutual fund industry in the same manner as they do in other sectors of the American economy." S. Rep. No. 184, 91st Cong., 1st Sess., 5 (1969).

As a consequence, "[t]he relationship between investment advisers and mutual funds is fraught with potential conflicts of interest," *Galfand* v. *Chestnutt Corp.*, 545 F. 2d 807, 808 (CA2 1976). See generally S. Rep. No. 184, 91st Cong., 1st Sess., 5 (1969); H. R. Rep. No. 2337, 89th Cong., 2d Sess., 9, 45-46, 64 (1966); H. R. Doc. No. 136, 77th Cong., 1st Sess., 2485-2490, 2569, 2579-2580, 2775 (1942); Hearings on H. R. 10065 before a Subcommittee of the House Committee on Interstate and Foreign Commerce, 76th Cong., 3d Sess., 58-59 (1940); SEC, Report on the Study of Investment Trusts and Investment Companies, pt. 3, 1-49 (1940); 15 U. S. C. § 80a-1 (b) (findings and declaration of policy).[9] Yet, while these potential conflicts may justify some restraints upon the unfettered discretion of even disinterested mutual fund direc-

[9] See also *Tannenbaum* v. *Zeller*, 552 F. 2d 402, 405 (CA2 1977); Radmer, Duties of the Directors of Investment Companies, 3 Journ. Corp. L. 61, 63 (1977); Note, 47 Ford. L. Rev. 568 (1979).

tors, particularly in their transactions with the investment adviser,[10] they hardly justify a flat rule that directors may never terminate nonfrivolous derivative actions involving co-directors. In fact, the evidence is overwhelming that Congress did not intend to require any such absolute rule.

The cornerstone of the Investment Company Act's effort to control conflicts of interest within mutual funds is the requirement that at least 40% of a fund's board be composed of independent outside directors.[11] 15 U. S. C. § 80a–10 (a). As originally enacted, § 10 of the Act required that these 40% not be officers or employees of the company or "affiliated persons" of its adviser. 54 Stat. 806. In 1970, Congress amended the Act to strengthen further the independence of these directors, adding the stricter requirement that the outside directors not be "interested persons." See §§ 80a–10 (a), 80a–2 (a)(19).[12]

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[10] See, *e. g.*, § 36 of the Investment Company Act, 15 U. S. C. § 80a–35, and § 206 of the Investment Advisers Act, 15 U. S. C. § 80b–6, imposing minimum standards on the behavior of investment company directors and advisers which presumably apply as much to their decisions regarding litigation as to the other decisions they may be called upon to make. See *Santa Fe Industries, Inc.* v. *Green*, 430 U. S. 462, 471 n. 11 (1977) (". . . Congress intended the Investment Advisers Act to establish federal fiduciary standards for investment advisers."); *SEC* v. *Capital Gains Research Bureau*, 375 U. S. 180, 191–192 (1963); *Cramer* v. *General Tel. & Electronics Corp.*, 582 F. 2d 259, 275 (CA3 1978); *Tannenbaum* v. *Zeller*, 552 F. 2d, at 418–419.

[11] Under certain circumstances, independent directors must constitute a majority rather than 40% of the board. See § 80a–10 (b).

[12] 15 U. S. C. § 80a–2 (a)(19) defines an "'interested person' of another person . . . when used with respect to an investment company," as

"(i) any affiliated person of such company,

"(ii) any member of the immediate family of any natural person who is an affiliated person of such company,

"(iii) any interested person of any investment adviser of or principal underwriter for such company,

"(iv) any person or partner or employee of any person who at any time since the beginning of the last two fiscal years of such company has acted as legal counsel for such company, To these statutorily disinterested directors, the Act assigns a host of special responsibilities involving supervision of management and financial auditing. They have the duty to review and approve the contracts of the investment adviser and the principal underwriter, 15 U. S. C. § 80a–15 (c); the responsibility to appoint other disinterested directors to fill vacancies resulting from the assignment of the advisory contracts, 15 U. S. C. § 80a–16 (b); and are required to select the accountants who prepare the company's Securities and Exchange Commission financial filings, 15 U. S. C. § 80a–31 (a).

Attention must be paid as well to what Congress did *not* do. Congress consciously chose to address the conflict of interest problem through the Act's independent directors section, rather than through more drastic remedies such as com-

"(v) any broker or dealer registered under the Securities Exchange Act of 1934 or any affiliated person of such broker or dealer, and

"(vi) any natural person whom the Commission by order shall have determined to be an interested person by reason of having had, at any time since the beginning of the last two fiscal years of such company, a material business or professional relationship with such company or with the principal executive officer of such company or with any other investment company having the same investment adviser or principal underwriter or with the principal executive officer of such other investment company."

15 U. S. C. § 80a–2 (a)(2) states that "'affiliated company' means a company which is an affiliated person," and 15 U. S. C. § 80a–2 (a)(3) defines "'affiliated person' of another person" as

"(A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person; (E) if such other person is an investment company, any investment adviser thereof or any member of an advisory board thereof; and (F) if such other person is an unincorporated investment company not having a board of directors, the depositor thereof."

plete disaffiliation of the companies from their advisers or compulsory internalization of the management function. See Report of the SEC on the Public Policy Implications of Investment Company Growth, H. R. Rep. No. 2337, 89th Cong., 2d Sess., 147–148 (1966). Congress also decided *not* to incorporate into the 1940 Act a provision, proposed by the SEC, that would have forced investment companies to seek court approval before settling claims against "insiders" that could be the target of derivative suit. See S. 3580, 76th Cong., 3d Sess. § 33 (a) (1940); *Wolf* v. *Barkes*, 348 F. 2d 994, 997 n. 4 (CA2 1965). And when Congress did intend to prevent board action from cutting off derivative suits, it said so expressly. Section 36 (b), 15 U. S. C. § 80a-35 (b)(2), added to the Act in 1970, performs precisely this function for derivative suits charging breach of fiduciary duty with respect to advisor's fees.[13] No similar provision exists for derivative suits of the kind involved in this case.

Congress' purpose in structuring the Act as it did is clear. It "was designed to place the unaffiliated directors in the role of 'independent watchdogs,'" *Tannenbaum* v. *Zeller*, 552 F. 2d, at 406, who would "furnish an independent check upon the management" of investment companies, Hearings on H. R. 10065 before a Subcommittee of the House Committee on Interstate and Foreign Commerce, 76th Cong., 3d Sess., 109 (1940). This "watchdog" control was chosen in preference to the more direct controls on behavior exemplified by the options not adopted. Indeed, when by 1970 it appeared that the "affiliated person" provision of the 1940 Act might not be adequately restraining conflicts of interest, Congress turned not to direct controls, but rather to stiffening the requirement of independence as the way to "remedy the act's deficiencies."

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[13] See also § 16 (b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78p (b), which authorizes shareholder suits to recover insider "short swing" profits on behalf of the company notwithstanding the decision of the board of directors not to sue.

S. Rep. No. 184, 91st Cong., 1st Sess., 32–33 (1969).[14] Without question, "[t]he function of these provisions with respect to unaffiliated directors [was] to supply an independent check on management and to provide a means for the representation of shareholder interests in investment company affairs." *Ibid.*

In short, the structure and purpose of the Investment Company Act indicate that Congress entrusted to the independent directors of investment companies, exercising the authority granted to them by state law, the primary responsibility for looking after the interests of the funds' shareholders.[15] There may well be situations in which the independent directors could reasonably believe that the best interests of the shareholders call for a decision not to sue—as, for example, where the costs of litigation to the corporation outweigh any potential recovery. See Note, 47 Ford. L. Rev. 568, 580 (1979); Note, 44 U. Chi. L. Rev., at 168, 196. See, *e. g., Tannenbaum* v. *Zeller*, 552 F. 2d, at 418; *Cramer* v. *General Tel. & Electronics Corp.*, 582 F. 2d 259, 275 (CA3 1978). In such cases, it would certainly be consistent with the Act to allow the independent directors to terminate a suit, even though

yes

[14] See n. 12, *supra*.

[15] As an adjunct to its main argument which rested upon the structure of the Investment Company Act, the Court of Appeals was also of the view that mutual fund directors can never be truly disinterested in suits involving their codirectors. 567 F. 2d, at 1212. While lack of impartiality may or may not be true as a matter of fact in individual cases, it is not a conclusion of law required by the Investment Company Act. Congress surely would not have entrusted such critical functions as approval of advisory contracts and selection of accountants to the statutorily disinterested directors had it shared the Court of Appeals' view that such directors could never be "disinterested" where their codirectors or investment advisers were concerned. In fact, although it was speaking only of the statutory definition, Congress declared in the second section of the Act, "[t]hat no person shall be deemed to be an interested person of an investment company solely by reason of his being a member of its board of directors or advisory board . . . ." § 80a–2 (a)(19). See also § 80a–2 (a)(9) ("A natural person shall be presumed not to be a controlled person within the meaning of this subchapter.")

not frivolous. Indeed, it would have been paradoxical for Congress to have been willing to rely largely upon "watchdogs" to protect shareholder interests and yet, where the "watchdogs" have done precisely that, require that they be totally muzzled.[16]

IV

We hold today that federal courts should apply state law governing the authority of independent directors to discontinue derivative suits to the extent such law is consistent with the policies of the Investment Company and Investment Advisers Acts. Moreover, we hold that Congress did not require that States, or federal courts, ~~absolutely~~ forbid director termination of all nonfrivolous actions. However, since "[w]e did not grant certiorari to decide [a question of state law]," *Butner* v. *United States*, No. 77-1410, at 3, — U. S. — (1979), and since neither the District Court nor the Court of Appeals decided the point,[17] the case is reversed and remanded for further proceedings consistent with this opinion. *Butner* v. *United States, supra; Wallis* v. *Pan American Petroleum Corp.*, 384 U. S., at 72.

Reversed.

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[16] As an alternative ground in support of the judgment below, respondents urge that Fed. Rule Civ. Proc. 23.1 prohibits termination of this derivative action. That rule states that a derivative action "shall not be dismissed or compromised without the approval of the court . . . ." However, as Judge Friendly noted with respect to former Rule 23 (c), those words apply only to voluntary settlements between derivative plaintiffs and defendants, and were intended to prevent plaintiffs from selling out their fellow shareholders. They do not apply where the plaintiffs' action is involuntarily dismissed by a court, as occurred in this case. *Wolf* v. *Barkes*, 348 F. 2d 994, 996–997 (CA2 1965). The same is true of the identically worded Rule 23.1. See C. Wright and A. Miller, Federal Practice and Procedure § 1839, at 427, 435, 436 (1972); 3B J. Moore, Federal Practice ¶ 23.1.24 [2], at 23.1-131 (1976).

[17] In this Court, the parties hotly dispute the content of the correct state rule. Company Brief for Petitioners 36–38, with Brief for Respondents 35–39.

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE WILLIAM H. REHNQUIST

April 18, 1979

Re: No. 77-1724 Burks v. Lasker

Dear Bill:

Please note at the end of your opinion that I took no part in the consideration or decision of this case.

Sincerely,

Mr. Justice Brennan

Copies to the Conference

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE THURGOOD MARSHALL

April 24, 1979

Re: No. 77-1724 - Burks v. Lasker

Dear Bill:

Please join me.

Sincerely,

T.M.

T.M.

Mr. Justice Brennan

cc: The Conference

Join note

Mr. Justice Brennan
Mr. Justice White
Mr. Justice Marshall
Mr. Justice Blackmun
Mr. Justice Powell
Mr. Justice Rehnquist
Mr. Justice Stevens

From: Mr. Justice Stewart

Circulated: 30 APR 1979

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1st DRAFT

SUPREME COURT OF THE UNITED STATES

No. 77-1724

Harry G. Burks, Jr., et al., Petitioners, *v.* Howard M. Lasker et al. | On Writ of Certiorari to the United States Court of Appeals for the Second Circuit.

[May —, 1979]

MR. JUSTICE STEWART, concurring in the judgment.

The Investment Company Act and the Investment Advisers Act are silent on the question whether the disinterested directors of an investment company may terminate a stockholders' derivative suit. The inquiry thus must turn to the relevant state law. I cannot agree with the implications in the Court's opinion, *ante*, at 8, 9–10, 14, that there is any danger that state law will conflict with federal policy.

The business decisions of a corporation are normally entrusted to its board of directors. A decision whether or not a corporation will sue an alleged wrongdoer is no different from any other corporate decision to be made in the collective discretion of the disinterested directors. *E. g., Swanson* v. *Traer*, 354 U. S. 114, 116; *United Copper Sec. Co.* v. *Amalgamated Copper Co.*, 244 U. S. 261, 263; *McKee* v. *Rodgers*, 18 Del. Ch. 81, 156 A. 191 (Ch. 1931); *Rice* v. *Wheeling Dollar Savings & Trust Co.* (Ohio App.), 130 N. E. 2d 442 (1954); *Goodwin* v. *Castleton*, 19 Wash. 2d 748, 144 P. 2d 725 (1944).

On remand, the issue will be whether the state law here applicable recognizes this generally accepted principle and thereby empowers the directors to terminate this stockholder suit. Since Congress intended disinterested directors of mutual funds to be "independent watchdogs," *ante*, at 12, I can see no possible conflict between this generally accepted principle of state law and the federal statutes in issue.

I would join.
P.

May 1, 1979

77-1724 Burks v. Lasker

Dear Potter:

Please join me in your concurring opinion.

Sincerely,

Mr. Justice Stewart

lfp/ss

cc: The Conference

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
THE CHIEF JUSTICE

May 8, 1979

Re: 77-1724 - Burks v. Lasker

Dear Bill:

I join.

Regards,

WEB

Mr. Justice Brennan

Copies to the Conference

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE BYRON R. WHITE

May 9, 1979

Re: 77-1724 - Burks v. Lasker

Dear Bill,

It took a little time, but please add my name to your list in this case.

Sincerely yours,

Mr. Justice Brennan
Copies to the Conference
cmc

THE C. J.	W. J. B.	P. S.	B. R. W.	T. M.	H. A. B.	L. F. P.	W. H. R.	J. P. S.
	1/22/79							
join w JB 5/8/79	1st draft 4/18/79	1st draft concurring in the judgment	Join w JB 5/4/79	join WJB 4-24-79	Concurring opinion typed draft	join PS 5/1/79	out 4/18/79	join w JB 4/19/79
	2nd draft 5/4/79	4/30/79			5/7/79 1st draft 5/8/79			

77-1724 Burks v. Lasker